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United Utilities Water Limited

Annual Report and Financial Statements

31 March 2021

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Regulatory reporting:
Regulatory reporting information for the year ended 31 March 2021 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 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

Chairman and Chief Executive Officer's review

We have responded well to the challenges of a year that has been dominated by the impact of COVID-19 in maintaining service and support so critical to customers in the North West. Our operational performance has been strong, building on the improvements we delivered in the previous regulatory period and providing us with a great start to achieving our targets for the new 2020–25 price review period (AMP7).

This has been an unprecedented year in which we have had to adapt our operations to protect customers, employees and supply chain partners from the impact of COVID-19.

We responded well to the challenges and delivered our best ever year of operational performance for customers and the environment. Customer satisfaction remains high and we have made a strong start against our customer outcome delivery incentives (ODIs). This year has seen us reduce leakage to its lowest ever level and supply interruptions to customers have been halved. We are on track to achieve the maximum 4 star rating in the Environment Agency's assessment for 2020, and have reduced environmental pollution incidents by around a third.

Our operational performance has been strong against key metrics and we are pleased to have met or exceeded over 80 per cent of our performance commitments for year 1 of AMP7. In those areas where we have fallen short of our target – such as sewer flooding – we are innovating and investing in new technology in order to improve performance and service to customers over the longer term.

We witnessed further variability in weather conditions now characteristic of climate change. Our region experienced a hot, dry spring that, coupled with people spending more time at home, resulted in a high level of demand for water. We continued to encourage customers to save water through water efficiency programmes, helping them to preserve this precious resource and save money on their bills. Throughout this period we maintained supplies to customers, demonstrating the benefits of our Systems Thinking approach and supported by the investment we made in previous regulatory periods to enhance the resilience of our services.

We have a deep and strong relationship with the environment and communities of the North West. Our plans ensure we protect and improve the natural environment and for many years we have been at the forefront of addressing climate change. We are proud to be a signatory to the UN's Race to Zero campaign and we are delivering against all of our six carbon pledges. Our purpose drives us to make a real, positive contribution to the communities we serve through everything we do, and our investment programme plays a significant role in supporting the North West economy.

This excellent start to the delivery of our AMP7 plans provides a strong platform for us to play our full part in the economic recovery of the communities we serve as the country emerges from the COVID-19 pandemic.

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Maintaining excellent service to customers while supporting our employees

Our continued focus on delivering the best service to customers has never been more important. We delivered significant and sustainable improvements over AMP6 and we ended the period as a leading water and wastewater company. The way Ofwat measures customer satisfaction in AMP7 has changed, with C-MeX measuring household customer satisfaction and D-MeX measuring developer satisfaction. Despite a challenging operating environment, customer satisfaction remains high, earning us an outperformance payment for both C-MeX and D-MeX and positioning us in the sector upper quartile for all-round customer satisfaction.

The impact of COVID-19 has led to many customers facing increasing financial hardship. At the start of the pandemic we saw an increase in the number of customers needing affordability support and the initiatives we put in place in AMP6 enabled us to respond swiftly and effectively. We were the first water company to secure support and regulatory approval for an extension to the scale and scope of our social tariff, providing an additional £15 million to help a further 45,000 customers. We had to consider the appropriateness of continuing our normal billing and collection activities and the most suitable means of engagement. As part of our COVID-19 response, we proactively encouraged customers to contact us if they had been impacted financially by the pandemic. We carried out targeted activities aligned to specific customer segments and changes in customer behaviour to engage with customers, ensuring they knew they could talk to us about their water bill, and highlighting alternative ways to pay.

We could not have delivered such great service to customers during this time without highly engaged and motivated colleagues right across the organisation who demonstrate tremendous resilience and adaptability to deliver for a region hard hit by the pandemic. To keep employees safe, early on in the year we moved 60 per cent of our workforce to home working and the remainder continued working at our COVID-19 secure facilities. We have continued to work in this way in line with the government roadmap out of lockdown, while defining and shaping the way for future working. Our employee engagement score this year positioned us above the norm for UK high-performing companies – a remarkable score given the past year and testimony to the cohesiveness of the United Utilities team.

Transforming into a digital utility

Through our Systems Thinking approach we make use of technology, automation and machine intelligence to deliver better performance for customers and the environment.

Through implementation of Dynamic Network Management – an example of the most advanced form of Systems Thinking in the water sector – we are shifting from reactive management of our wastewater network to using a web of sensors that will provide near real-time performance information. This new digital capability will optimise performance in a predictive and preventative way, delivering greater efficiency, improved service to customers and helping to enhance the environment.

We recognise the benefits to be gained through building digital skills among our workforce, and our purpose-built technical training academy, established in 2014, has provided skills development and certification to over 2,800 colleagues. The focus on digital skills means that we have the in-house ability to develop and deploy breakthrough technologies at pace and efficiently.

We make extensive use of apps, many of which are developed in-house, to create digital capability for our field and customer- facing teams. Our new voids app, aimed at unbilled but

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occupied properties, has helped us to earn the maximum customer ODI outperformance payment on voids this year as well as securing future year benefits of a further £24 million over AMP7.

Delivering a robust financial performance

We have delivered another year of robust financial performance, supported by the strength of our balance sheet.

At £410.1 million profit after tax is £274.2 million higher than the profit after tax of £135.9 million reported in the prior year. This increase largely reflects a number of significant items that we incurred last year and we did not expect to recur in future years. These prior year items included non-cash impacts such as £82.6 million of accelerated depreciation on Bioresources assets and a £132.4 million deferred tax charge in relation to a change in tax rate. In addition to this, net fair value gains on debt and derivative financial instruments, which are subject to inherent volatility and can therefore vary significantly from year to year, were £147.9 million higher than the fair value losses reported in the prior year. These impacts have been partly offset by the expected decrease in allowed regulatory revenue in the first year of the new regulatory period, and an increase in infrastructure renewals expenditure due to planned work to optimise the performance of our network as well as a slight increase in the broader cost base.

Our balance sheet continues to be one of the strongest in the sector, with low customer debtor risk, net debt to regulatory capital value within our target range and a pension scheme that is fully funded on a low dependency basis.

Given the uncertainty created by the COVID-19 pandemic, the recoverability of household debtors has been a key area of focus. It has been an area of focus for us for most of the last decade, during which we have managed the position robustly. This manifests itself in the balance reducing from £115 million in 2016 to £78 million in 2021. Our net debtor balance as at 31 March 2021 is the lowest it has been for five years and is one of the best managed positions in the sector. Knowing this gives us added confidence as we emerge from the pandemic.

RCV gearing, measured as net debt to regulatory capital value, was 65 per cent. During the year, we changed our definition of net debt to exclude the impact of derivatives that are not hedging specific debt instruments. This provides a better reflection of the debt balances we are contractually obliged to repay and is more consistent with the approach taken by credit rating agencies and the regulatory economics. Our gearing policy is supportive of an A3 credit rating with Moody's and we have liquidity extending out to February 2023. This provides us with resilience and financial flexibility as we progress through AMP7 and demonstrates our prudent and responsible approach to financial risk management.

We have eliminated our pension funding deficit on a low-dependency basis and our pension position is in surplus on an IAS 19 basis. Having no pension funding deficit puts us at an underlying advantage versus most other companies in the sector, as well as against many companies in the Financial Times Stock Exchange (FTSE), that continue to make cash contributions into their pension schemes to achieve a fully-funded position. We are proud to have already achieved this, protecting employees past and present and shareholders from the risk of a large pension deficit.

In November 2020, we published our new sustainable finance framework, which allows us to raise financing based on our strong environmental, social and governance (ESG) credentials. This replaces the green funding we have previously secured through the European Investment

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Bank (EIB), which is no longer available post-Brexit. We issued our debut sustainable bond in January 2021 and were extremely pleased by the high level of interest. As a result, we secured not only our lowest ever coupon at that particular maturity, but also the lowest ever coupon for any UK corporate at that maturity, locking in financing outperformance.

Good start to the new regulatory period (AMP7)

We are performing well against the principal areas of our regulatory contract for AMP7 despite many targets getting tougher.

Our accelerated investment strategy and digital transformation is delivering value across the breadth of our customer ODIs. The £21 million outperformance payment earned this year is ten times the performance we delivered in the first year of AMP6. The net reward earned this year will be reflected in an increase to revenues earned in 2022/23. This provides a great platform for continued delivery against our customer ODIs for the remainder of the AMP and gives us the confidence to target a cumulative outperformance payment of around £150 million for the 2020–25 period. Thanks to our good performance in AMP6, we started AMP7 at a total expenditure (totex) run rate which supports delivery of our AMP7 scope within our final determination totex allowance. Since accepting our final determination, our investment plan has been extended by a further £300 million, which we expect to be fully remunerated through regulatory mechanisms, with this expenditure extending our environmental programme, accelerating our digital transformation and exploiting spend to save opportunities.

While we continue to seek efficiencies in the delivery of totex, as we have demonstrated through the £300 million extension to our totex plans, we will invest totex where we are confident we can deliver improved customer or environmental outcomes and better customer ODI performance.

On financing performance, 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 already locked in for AMP7 compare favourably with the price review assumptions.

ESG at our heart

Our purpose drives us to deliver our services in an environmentally sustainable, economically beneficial and socially responsible manner and what we do creates deep connection with the stakeholders we serve. We have a long-standing commitment to deliver against our ESG objectives and we have a strong track record of doing so. We are also looking to our supply chain partners to adopt these values and objectives via the United Supply Chain (USC) initiative, a fundamental step change as to how we engage with them in AMP7 and into AMP8.

Having achieved our climate change objectives up to 2020, reducing greenhouse gas emission by 73 per cent, we made six carbon pledges and have made good progress against them all. From October of this year, 100 per cent of our electricity will be sourced from renewable technologies and we have set ambitious science-based scope 3 emissions targets that have been submitted for endorsement by the Science Based Targets initiative (SBTi).

Our Catchment Systems Thinking (CaST) approach continues to mature. We have been working with the Environment Agency (EA) and other stakeholders to develop a North West natural capital baseline and once this process is complete, we will engage with other partners

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across the region to drive a consistent approach to delivering greater natural capital value. This year, we pledged a £300,000 CaST Fund, for which charities and community groups are able to bid, to boost the idea of working collaboratively to address the challenges facing the environment.

We are in a unique position to make a real, positive contribution to society and have an ambitious and innovative approach to addressing affordability and vulnerability. We have an extensive range of schemes available to help customers and around 200,000 are currently benefiting from that help. We are providing more customers than ever with access to Priority Services in times of need, with over 133,000 now on our register. We have committed to providing £71 million in financial support over AMP7, and have accelerated payments this year to provide much needed assistance to households struggling as a result of the economic impact of the pandemic. During the early stages of the pandemic, recognising the importance of cash flow to businesses, we took swift action to accelerate payment terms with suppliers, paying them within seven days where possible.

We want fantastic people from a range of different backgrounds and life experiences to enable us to deliver a great public service, and we are committed to creating a diverse and inclusive workforce, reaching and recruiting from every part of our community. We were delighted to be one of the top one per cent of 15,000 companies across Europe in the Financial Times' Statista Survey for Diversity and Inclusion Leadership and to achieve inclusion in the Bloomberg Gender Equality Index.

We operate in a manner that aims to maintain high ethical standards of business conduct and corporate governance. We have attained World Class status on the Dow Jones Sustainability Index for the 14th consecutive year. We were delighted to retain the Fair Tax Mark independent certification which recognises our commitment to paying our fair share of tax and acting in an open and transparent manner in relation to our tax affairs. We continue to focus on our long-term financial resilience, supported by our strong balance sheet and prudent approach to financial risk management, maintaining a responsible level of gearing and well-controlled pension position for many years.

Outlook

We started the new regulatory period as one of the sector's best performers and have delivered further improvements this year, giving us the confidence that we will continue to be able to meet our targets across AMP7. Our transformation to a digital utility is helping us operate more efficiently and deliver better service to customers while protecting and improving the natural environment. Although it remains uncertain how the country will emerge from the COVID-19 pandemic, we have proven to be resilient over this period and will continue to rise to the challenges that lie ahead, playing our part in the recovery of the North West economy.

Grateful to our stakeholders for their support

We would like to express our gratitude to our highly engaged and motivated employees and supply chain partners who have shown great resilience and adaptability in continuing to deliver excellent performance over such a challenging period, and we extend our thanks to customers and other stakeholders for their continued support.

Sir David Higgins
Chairman

Steve Mogford
Chief Executive Officer

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Our approach as a responsible business

The way we act as a business has a profound influence on the social, economic and environmental wellbeing of the region.

Responsible business is in our DNA

We have a strong track record leading on environmental, social and governance (ESG) matters. Over the past 20 years we have measured ourselves against national and international benchmarks of responsible business practice, often breaking new ground in the way the water sector approaches challenges such as catchment management schemes and support for vulnerable customers.

This long-standing commitment to responsible business has provided a solid foundation upon which to evolve existing programmes, develop new initiatives, and respond to the changing world in which we operate.

What is our approach?

We will only deliver our purpose and create and maintain value for our stakeholders if we act in a responsible manner. This comes from understanding what matters most to them and balancing these different perspectives in our decision-making.

Our approach isn't just about what we do, but how we do it. A key strength is our commitment to open, honest and transparent reporting about the continuity of our approach, underpinned by a clear purpose and strategic objectives.

Increasingly, stakeholders assess how companies approach responsible business through the lens of ESG. We believe there is a close relationship between ESG performance and investor value.

Demonstrating how we act responsibly and create value

Being a purpose-led business it is up to us to provide the evidence that we are providing great water and more for the North West. Our stakeholders are ultimately the ones who will judge whether we are delivering on our purpose.

Having tangible, externally recognised measures of our behaviour and performance helps retain the trust of those who take an interest in the way we do business. It enables us to demonstrate that we are operating in our stakeholders' interests. We collate, monitor and report on a wide range of performance measures, linked to what stakeholders tell us matter most, and align ourselves to recognised management standards and accreditations to give confidence in the way we are operating. We report these publicly so stakeholders can assess our progress.

Alongside this we actively participate in a range of global ESG ratings, indices and frameworks to benchmark our approach against best practice and emerging sustainability challenges.

As responsible business practice evolves we look constantly at how we can improve. For instance, we are currently exploring whether embedding multi-capital thinking (manufactured, financial, natural, social, human and intellectual capital) into business processes will add value and better inform our decision-making processes. This includes how we might report publicly against these capitals.

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Reporting responsible business performance

Evolving market expectations

The way we report on environmental, social and governance (ESG) issues is evolving as stakeholder interest grows.

There is increasing interest in how companies respond to sustainability challenges and growing expectations on how they disclose relevant information and data on their responsible business activities. For example, there is more interest in the disclosure of the ESG performance of companies and, last year, we published an investor guide to ESG at United Utilities in response to that trend: unitedutilities.com/globalassets/documents/pdf/united-utilities-esg-booklet-2020.pdf

The way in which we report has evolved over the past ten years to incorporate more ESG information and data through such action as moving to integrated reporting. We have looked to do this without making this report unnecessarily lengthy or difficult to read. Rather than adopt one specific framework, our approach is to use the framework of our purpose-led approach to disclose performance and data for each of the stakeholders we create value for. Many of the ESG indices in which we participate (see page 62) draw their data from this report.

However, we do recognise that some stakeholders prefer to have specific data provided in one place. The following indicates where further information on certain frameworks can be found:

World Economic Forum (WEF) International Business Council (IBC)

The WEF IBC has proposed a set of common metrics for the consistent reporting of sustainable value creation in mainstream annual reports. We already integrate many of these metrics in our annual report and to make this easier for those searching for the information we have collated them into one place on our website. unitedutilities.com/wef

Sustainability Accounting Standards Board (SASB)

SASB standards aim to standardise disclosure of material sustainability information mainly for companies based in the United States. As many of our shareholders are located in North America we are publishing comparable SASB data on our corporate website. This covers the main SASB data points for the water utilities industry of which we are part. unitedutilities.com/sasb

Taskforce for climate-related financial disclosures (TCFD)

TCFD sets out a framework for companies to provide stakeholders with an assessment of the financial implications of climate change and what this means for governance, strategy, risk and metrics. For the second year, we have included a TCFD section in our annual report. Read more on pages 63 to 83.

Sustainable Development Goals (SDGs)

We have identified six SDGs that are material to our business. More details can be found on page 62 to 63.

We also complete a variety of issue and stakeholder-specific rankings and benchmarks such as the Workforce Disclosure Initiative (WDI). Disclosure of these performance scores can be found on our website. unitedutilities.com/corporate/ responsibility/our-approach/cr-performance

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Our purpose, vision, strategy and values

Our purpose

Our strategic themes define the way we operate so we can deliver our purpose and work towards our vision, and our core values provide the cultural framework within which we operate.

Why we exist

To provide great water and more for the North West.

We are a purpose-led organisation and this drives us to deliver our services in an environmentally sustainable, economically beneficial and socially responsible manner, looking after the interests of the stakeholders with whom we interact.

Our vision

What we want to achieve

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.

How we deliver our purpose and vision

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.

At the lowest sustainable cost

In order to run a resilient business, it is important to ensure cost reductions are sustainable so that we can keep them down in the long term 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 through a holistic approach. 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.

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In a responsible manner

Our purpose drives us to deliver our services in an environmentally sustainable, economically beneficial and socially responsible manner, looking after the interests of the stakeholders with whom we interact. 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

Fundamental values that drive 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.

How we operate

Delivering clean water

We depend on water that we collect from the natural environment in rivers, lakes, open reservoirs and boreholes, but we need to do a lot of work before this water is safe and clean for customers to drink. We maintain covered reservoirs, water treatment works and thousands of kilometres of water pipes across the region in order to collect, treat, store and deliver billions of litres of reliable, clean drinking water to millions of customers 24 hours a day.

Removing wastewater

Once the water goes down customers’ drains, or surface water flows into the sewers, our job begins again as it requires separation and treatment before it is clean enough to return to the natural environment. We maintain wastewater treatment works and thousands of kilometres of wastewater pipes in order to collect, transport, treat and return water to begin the cycle again. We waste nothing, turning sludge by-product into compost for farmers and capturing gas to generate renewable energy.

Household retail

We deal with new connections, metering and billing for millions of household customers, and help vulnerable customers with our Priority Services and other assistance schemes.

Wholesale

For non-domestic customers in the North West, such as businesses, we provide a wholesale service to water retailers. Our wholesale activities include interactions with new appointments and variations, known as NAVs.

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Our Systems Thinking approach

Traditionally across the water industry, each asset or treatment works was operated, managed and assessed in isolation. Systems Thinking looks at the entire network, using enormous amounts of data from the telemetry backbone we have installed, to consider not just the individual asset but all its linkages, enabling us to find the best overall long-term solution. Our field engineers are linked by an Integrated Control Centre (ICC) at our head office, from which we plan, monitor and control our operations. From our ICC we process vast amounts of real-time data from across our network, factoring in other source data such as weather forecasts, and use artificial intelligence and machine learning to process this data and spot issues so we can resolve them before they impact customers.

Systems Thinking improves our asset reliability and resilience, reduces unplanned service interruptions, and helps us move away from the traditional reactive approach to address problems proactively before they affect customers. This pioneering approach helped us deliver operational improvements and cost savings during AMP6, and we have further developments planned for AMP7 and beyond, as Systems Thinking forms part of our long-term strategy to continue creating value for customers and stakeholders.

We serve the North West

We are committed to understanding the key factors that make our region unique.

Economic factors

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

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- 7.3 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 Lake District, Liverpool and coastal area

Social factors

We are leading the sector on affordability and vulnerability.

- 41 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
- 18 per cent of households are affected by water poverty, 20 per cent higher than the national average

Environmental factors

We have a large 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
- 29 designated bathing waters
- 830mm higher than average UK rainfall each year

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) regularly attends board meetings to provide its perspective.

The following pages detail how we engage with, and are influenced by, each of our key stakeholder groups. 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 19.

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.

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Our approach to engagement extends across all of our stakeholders, from those who influence what we do and benefit from the value we create, to those who just influence what we do.

Communities

Why we engage

Our work puts us at the heart of local communities, places where customers and employees live and work. We seek to support communities to be stronger based on mutual trust, respect and understanding the impact and contribution our work has on everyday life. We play a constructive role in tackling issues through engagement and investment, and by identifying what matters most to communities we can develop collaborative solutions.

How we engage

Much of our engagement is face-to- face, although over the past year we have adapted to using more digital means of engagement, such as our online consultation as part of the Haweswater Aqueduct Resilience Programme, alongside traditional methods, such as attending parish council meetings.

We engage through facilitated workshops and community partnerships, such as involving those communities affected by our construction work.

Issues raised by communities can present opportunities to improve what we do or to help others, while some can be complex and difficult to handle, especially where competing interests between different stakeholder groups are present, and require time and effort to work through.

Top three material issues

- Land management and access

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- Community investment
- Trust, transparency and legitimacy

Customers

Why we engage

To provide a great service in a way that customers value, we need to listen and engage with them to understand both short-term issues, and longer- term expectations of us as their water company. We are always interested to know what domestic and wholesale customers think about us so we can make our services better and address the issues that matter. As customer expectations change, we need to evolve our own services to ensure we meet those expectations.

How we engage

We interact with customers every day through our operational call centres, water retailers and increasingly via social media channels. We also get direct feedback through schemes such as the WOW awards.

Enhancements to our service such as Priority Services have been developed through engagement with customers and groups representing vulnerable customers, such as Age Concern and Autism Together.

Our current business plan was shaped by unprecedented levels of customer engagement. YourVoice, the independent customer challenge group, provided critical support and challenge, as well as contributing to shape our plans to 2025.

Top three material issues

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

Employees

Why we engage

It is essential we build productive relationships with our employees based on trust. Our employees are the face of the company and we simply could not deliver our services without them, including the 13,000 who form part of our supply chain in the North West. Employees know our business better than anyone, with a diverse range of views and experience, making them well placed to identify opportunities for improvement.

How we engage

Line managers play a vital role in supporting employees, with regular one-to-one meetings providing two-way engagement.

Every year our employee opinion survey provides an opportunity for employees to have a say about our company and to be open and honest with their views and opinions. The anonymous and confidential survey is managed by an independent consulting firm. Results are provided to all teams with greater than ten members for them to take action accordingly.

Our Employee Voice panel consists of 24 members from across the company, providing a means by which employee perspectives are heard by the board. We have several employee-led networks, including gender equality, multicultural and LGBT+ groups.

Top three material issues

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

Environment

Why we engage

We rely on the environment and play a key role in protecting and enhancing it across the region. Given the environment has no voice of its own, we engage with interested groups such as environmental regulators, non-governmental organisations, campaigners and local communities to find the best ways to tackle environmental issues, like climate change and land management.

How we engage

We have formal discussions with both national and regional representatives of environmental regulators to identify priority issues and solutions.

We conduct facilitated workshops with environmental stakeholders to understand their priorities and have undertaken a large number of customer research projects.

We work with other companies, including within the water sector, landowners and local and national environmental groups to explore where we have common interests and opportunities to collaborate and deliver more together through pilots and partnerships.

Top three material issues

- Resilience
- Environmental impacts
- Climate change

Investors

Why we engage

It is important that investors have confidence in the company and how it is managed, given their investment in our business. We provide regular updates to debt investors and equity investors of UUG so they can be assured that the company is being managed responsibly. Increasingly, this includes environmental, social and governance updates alongside financial and performance data as investors take a broader view of value and risk.

How we engage

UUG's AGM provides a chance for any shareholder to engage with our board of directors and hold them to account.

Through UUG's investor relations programme, we actively engage with shareholders and analysts who write reports on our company and industry. Regular engagement activities are supplemented by ad hoc events such as capital markets days.

Our treasury team has regular dialogue with the group's relationship banks and the EIB and credit rating agencies. Updates are provided to credit investors through a programme of meetings and mailings.

We supply information to several investor-led ratings and indices on ESG matters, such as the Dow Jones Sustainability Index.

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Top three material issues

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

Suppliers

Why we engage

Good relationships with suppliers help ensure that we get projects delivered on time, to good quality, at efficient costs and can identify and realise innovative approaches and solutions. Awareness of issues throughout the supply chain means we can address them together and become more resilient. We rely on suppliers to deliver our services and create value for all.

How we engage

Existing suppliers have regular discussions with our commercial team as part of our supplier relationship management (SRM) process. This helps to identify issues and opportunities to make our relationship flow smoothly.

When re-tendering goods or services, we engage with the market directly and through supplier databases such as Achilles, to get a broad view of best practice and market opportunities.

Through our United Supply Chain (USC) approach we engage suppliers on sustainable and ethical issues and performance. Suppliers can join USC by committing to our responsible sourcing principles.

Through memberships of organisations such as the Supply Chain Sustainability School and the Chartered Institute of Procurement and Supply we keep abreast of best practice.

Top three material issues

- North west regional economy
- Responsible supply chain
- Human rights

We maintain close relationships with three stakeholder groups that influence what we do and how we do it.

Media

Why we engage

It is through both traditional media and social media that many of our stakeholders receive their information about us and our activities. The media is influenced by the issues that matter most to those stakeholders as well as influencing them through what it reports. Given the nature of our services, it is important that coverage is fair, balanced and accurate. This requires effective two-way dialogue between the company and the media.

How we engage

Our media team are available 24/7 to respond to media enquiries and proactively engage media outlets providing digital content suitable for direct media broadcast.

Regular press releases on company activities help to maintain relationships with national, regional and local media outlets.

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We have a dedicated social media team who manage and respond to posts on our social media channels while driving proactive messages and articles. We monitor social media sentiment and issues related to the company so we can respond accordingly.

Top three material issues

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

Politicians

Why we engage

Politicians influence the long- term national water strategy and environmental priorities, matters that affect how all businesses operate, and champion issues raised by their constituents.

Local government, elected representatives and devolved administrations provide insight into shared social, environmental, economic and governance issues.

How we engage

We engage with regional and national politicians across the different political parties.

Open dialogue with regional MPs is maintained on specific issues and we regularly attend meetings at constituency offices. We have provided each MP in our region with a fact sheet with contact details and information about our activities in their constituency.

We take part in joint working groups with devolved administrations and local authorities on topics such as natural capital.

As part of our capital programme, we often attend local parish council meetings to make the case for our planning applications.

Top three material issues

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

Regulators

Why we engage

Through proactive, constructive engagement with economic, quality and environmental regulators, we agree commitments over specified time periods and finalise the expectations they have of our business planning and performance.

We actively engage to shape the policy and regulatory framework within which we operate, covering customer, economic, environmental, social and governance matters.

How we engage

We hold regular meetings with all of our regulators to discuss priorities and objectives which can change over time.

When they seek views through specific consultations we provide considered responses where we think there is value and we have something to contribute.

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We work together with regulators to find new solutions through projects such as Natural Course, which aims to build capacity to protect and improve the water environment of the North West.

Top three material issues

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

Managing our material issues

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 below.

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

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

Our assessment of the level of interest to stakeholders is based on a balance of views obtained from communities, customers, employees, investors, regulators, and subject matter experts from the company on an ongoing basis, as well as the extensive insights gathered for the regulatory price review process. We will be undertaking a thorough review of our material issues and matrix in the next 12 months.

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

Material issues matrix

We consolidated feedback from our various stakeholder groups, as detailed above, which resulted in 26 material issues. Due to the impact and ongoing nature of the COVID-19 pandemic we have included this as a new material issue. These issues are impacted by factors that may be external, internal or both; for example, the material issue of a diverse and skilled workforce has an external dimension of skills and diversity within the region, whereas the training and culture within the company are internal factors. The 27 issues are plotted on the matrix below, from lower to higher in terms of level of interest to stakeholders and how much it can affect our ability to create value.

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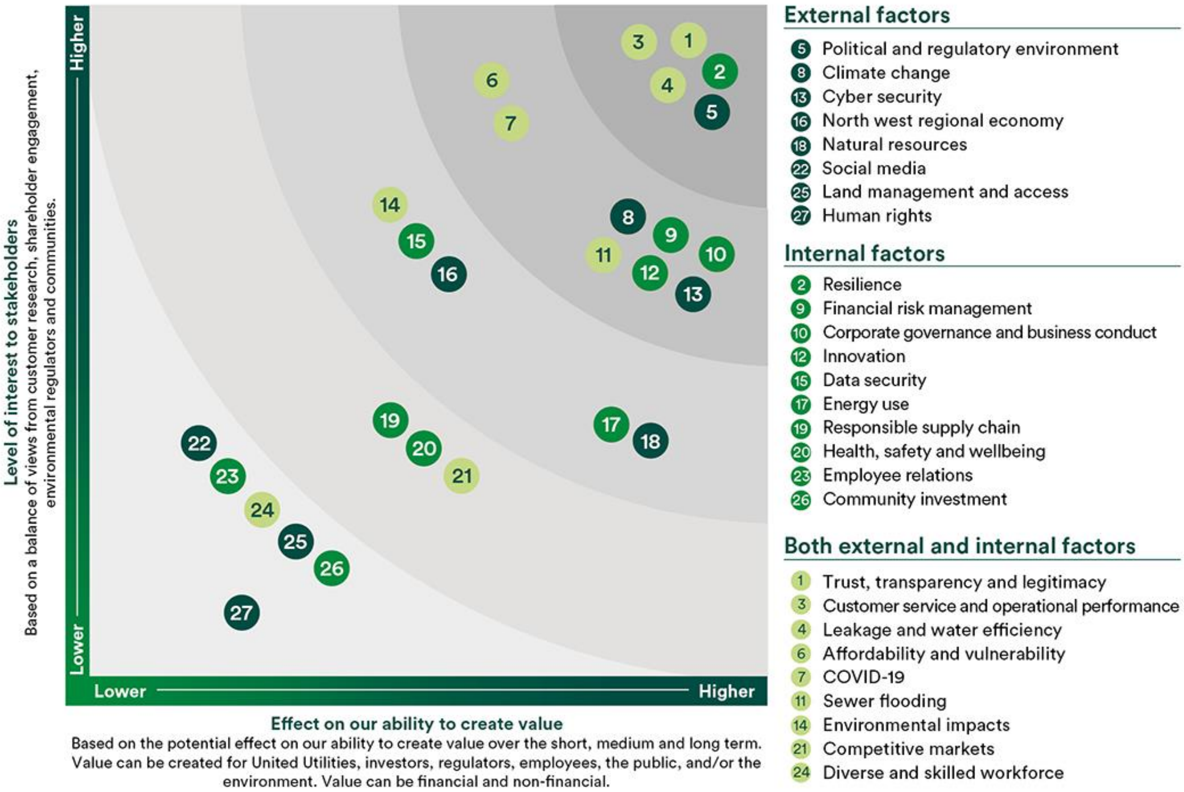

S172(1) Statement

Introduction

Throughout this annual report, 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 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 (among other matters) to factors (a) to (f) S172(1) Companies Act 2006, in the decisions taken during the year ended 31 March 2021.

Our key decisions during the year to 31 March 2021 were:

Green recovery

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In July 2020, Defra commenced an initiative through which water companies (among others) could propose to accelerate investment to deliver 'green' initiatives that would both benefit the environment and support the economic recovery from the COVID-19 pandemic. The requirements for such proposals were further clarified by Ofwat, Defra, the Consumer Council for Water, the Environment Agency and the Drinking Water Inspectorate in November 2020 and January 2021.

The board's view

The board believed that the draft investment proposed would help to contribute to the Government's green recovery plans and bring forward benefits for customers and the environment, but it would not present a significant risk to our financial resilience nor compromise our ability to deliver the remainder of our AMP7 plan. The board believed that our proposals were: of high quality; represented strong outcomes for customers and the environment; offered good value for money; could be implemented alongside existing regulatory and statutory commitments; and would be most likely to promote the long-term success of the company for the benefit of its members as a whole. If our regulators confirm they are supportive, the board will further review its position.

Scope 3 emissions

We had already committed to achieving science-based targets to reduce our emissions in line with the UK's commitment in the 2008 Climate Change Act (see pages 63 to 77). As part of our carbon strategy the board has made a series of pledges to deliver these targets and to setting further targets across our full value chain, including transitioning to using 100 per cent renewable energy by 2021 and a 100 per cent green fleet by 2028.

The board's view

During the year, we have made a further commitment by setting science-based targets for scope 3 emissions. First, we will reduce our absolute emissions by 25 per cent from the 2020 baseline by 2030, thereby aligning the group to a trajectory needed to limit global warming to 'well below' 2ºC. Secondly, we have set the target that 66 per cent of our construction services suppliers should set their own science-based target by 2025, thereby helping to escalate a carbon focus in the construction services sector. The board believed that committing to our pledges and delivering against the targets set would be most likely to promote the long-term success of the company for the benefit of its members as a whole.

Dividend deferral for year ended 31 March 2021

In January 2020, alongside the announcement of the acceptance of the PR19 Final Determination for the 2020-25 regulatory period (AMP 7), the company's dividend policy for AMP7 was approved. The announcement confirmed the group's capital structure target and credit ratings targets for AMP7, in particular, aiming to maintain long-term credit ratings for the company of A3 with Moody's, BBB+ with Standard & Poor's and a senior unsecured debt rating of A- with Fitch. In light of the uncertainties of the COVID-19 pandemic, the board concluded in May 2020 that it was not appropriate for the company to pay a dividend during 2020/21 and that the payment of the 2020/21 'base' dividend of 4 per cent (nominal) on the actual equity portion of the shadow regulatory capital value, would be deferred until prevailing uncertainties had been determined.

The board's view

In May 2020, in the early stages of the pandemic, there were many uncertainties as to its longer-term effect on businesses and the economy, particularly in relation to inflation. Furthermore the company's business planning scenarios reflecting the potential impacts of the pandemic suggested mitigating action was required to improve the company's gearing and associated credit ratios. The board concluded that the deferral of the 2020/21 base dividend was a responsible approach to maintaining the financial resilience of the company in light of the uncertainties prevailing at the time, and 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 10 to 11, 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 44 to 54), include data in relation to the areas of disclosure required by s414CB(1).

The composition of the UUW Board mirrors that of the UUG Board and therefore the non-financial information statement should be read in conjunction with the UUG 2021 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 UUW Annual report and financial statements

Reporting requirement	Information necessary to understand our business and its impact, policy, due diligence and outcomes	Policies, guidance and standards which govern our approach (some of which are only published internally)
Environmental matters	Reflecting the needs of the environment:	• Waste and resource use policy
	• Natural resources – see page 34	• Environmental policy
	• Natural environment – see pages 25 and 26	• Water Resources Management Plan – see page 48
	• Reducing our carbon footprint – see pages 86 to 99	• Emissions target – see pages 86 to 99
Employees	Reflecting the needs of our employees:	• Health and safety policy
	• Competitive base salaries and benefits – see UUG Annual report page 173	• Equality, diversity and inclusion policy
	• Health and safety – see page 61	• Flexible working arrangements
	• Mental wellbeing – see page 59 to 60	• Agency worker policy
	• Gender pay report 2020 – see UUG Annual report page 139	• Mental wellbeing policy
	• Engagement – see pages 5, 24, 59, 61 and 194	• Human rights policy – see page 41
	• Board diversity – see UUG Annual report page 132 to 133	• Board diversity policy - see UUG Annual report page 132 to 133
Respect for human rights	Reflecting the needs of our stakeholders:	• Employee data protection policy
	• Suppliers – see page 25	• Slavery and human trafficking statement
	• Diversity within our workforce – see UUG Annual report pages 42, 59 to 62, 132 to 133, 137 to 140	• Human rights policy – see page 41
Social matters	Reflecting the needs of our stakeholders:	• YourVoice – see page 22
	• Customers – see page 24	• Charitable matched funding guidance
	• Communities – see page 24	• Volunteering policy
	• Environment – see page 25	• United supply chain – see pages 41 and 73
	• Suppliers – see page 25	• Commercial procurement policy
	• Regulators – see page 26	
Anti-corruption and anti-bribery	Reflecting the needs of employees and suppliers:	• Anti-bribery policy
	• Employees – see pages 59 and 155	• Fraud investigation and reporting processes
	• Suppliers – see page 71	• Whistleblowing policy
		• Internal financial control processes
		• Commercial procurement policy

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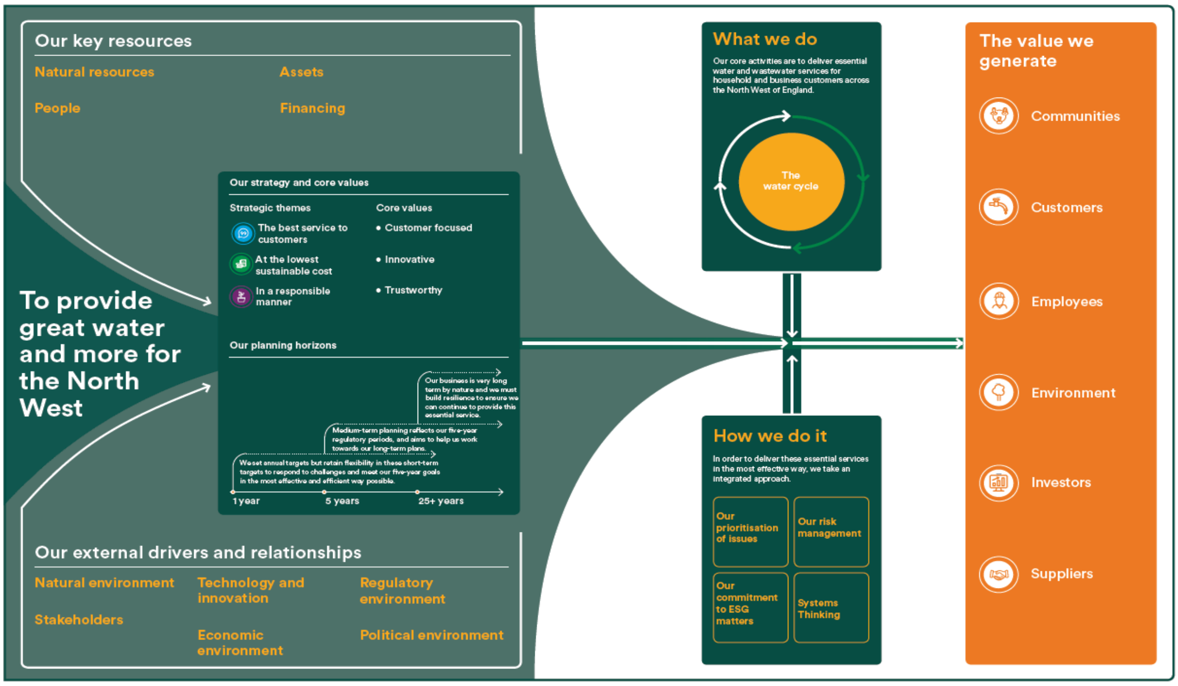
Our business model



Our purpose is to provide great water and more for the North West.

Our key resources

Natural resources

We rely on natural resources to supply water and take back wastewater after treatment, as well as to generate renewable energy. We own and manage large areas of land.

People

We rely on skilled and engaged employees and suppliers to deliver our services, and must ensure skills are maintained across the generations through training and development.

Assets

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

Financing

Financing allows us to preserve intergenerational equity for customers while funding long-term capital investment, and we maintain access to a range of markets to seek good value.

Our external drivers and relationships

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.

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Technology and innovation

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

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

Regulators' priorities drive our five-year commitments, and we must actively engage to influence and prepare for future market reforms in the industry.

Political environment

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

Our strategy and core values

Our strategy sets out how we deliver our purpose, and is broken down into three strategic themes, which govern everything we do.

Our core values – to be customer-focused, innovative and trustworthy – provide the cultural framework within which we operate.

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

Our planning horizons

We undertake long, medium, and short-term planning, taking into account our external drivers and what matters to stakeholders.

1 year

We set annual targets but retain flexibility in these short-term targets to respond to challenges and meet our five-year goals in the most effective and efficient way possible.

5 – 10 years

Medium-term planning reflects our five-year regulatory periods, and aims to help us work towards our long-term plans.

25+ years

Our business is very long term by nature and we must build resilience to ensure we can continue to provide this essential service.

Our key resources

Natural resources

We rely on natural sources of water, such as reservoirs, rivers and boreholes, from which abstraction licences permit us to take water in a safe and sustainable way to be treated and supplied to customers. We rely on natural watercourses to take wastewater back into the environment after extensive cleaning. We generate renewable energy from the sun and wind, and extract bioresources from wastewater that we break down into biogas (which is used to

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generate renewable energy) and biosolids (which are treated to provide a high-quality fertiliser for farmers).

Coping with severe dry periods requires action in relation to supply (ensuring we have resilient water resources and infrastructure to move water efficiently around the region) and demand (encouraging and supporting customers to use water more efficiently). In periods of heavy rainfall we need to deal with excess surface water drainage and minimise the risk of sewer flooding, pollution and spills.

How we manage this key resource

Much of the water we abstract originates on land before running off into the bodies of water. We own and manage large areas of this land, much of which is managed by tenant farmers, or in partnership with other organisations, such as the RSPB and Wildlife Trusts, and we focus on ensuring it is well managed to improve water quality and help protect habitats and species that live there.

Our Systems Thinking approach is central to how we manage water supply. We have an integrated supply zone covering most of our region, our West-East Link Main allows us to transfer water between Manchester and Liverpool, and where there is a potential shortfall we can bring more supplies online to meet demand. Forty-six per cent of households in our region now have water meters installed, and we encourage customers to save water by raising awareness, sharing tips, and providing free water-saving devices.

Traditional interventions to flooding, such as storage tanks and enlarging sewers, are costly and subject to space constraints. We are innovating with new sustainable drainage solutions by working with partners to transform hard grey areas into living planted places. We use integrated catchment solutions, working with others to improve the lakes, rivers and coastal waters in our region, and often using the natural environment as part of the solution. We manage our own woodland in a sustainable way to protect water quality, conservation, access, recreation and timber.

Our activities produce various wastes, including sludges, which we manage in a sustainable way with more than 97 per cent going to beneficial uses such as recycling and application to land as a fertiliser. We use recycled products where practical, and are working to reduce our use of plastics and raw materials to minimise our environmental impact.

Link to principal risks:

- Water service
- Wastewater service
- Health, safety and environmental

People

Our people are the face of our company and essential in delivering our purpose. We believe the most effective decision-making comes from a diverse range of people who feel encouraged to share their views, and that having a skilled, engaged and motivated team of employees, suppliers and contractors is fundamental to the performance we deliver.

Rewarding employees well has been shown to enhance quality of work, increase employee retention, and reduce absenteeism, as well as providing societal benefits. Employee retention helps ensure efficient and effective training and higher levels of performance.

How we manage this key resource

We support thousands of jobs in the North West, including graduate and apprenticeship programmes, helping to secure a legacy for the future in our region. We are an accredited Living Wage Foundation employer, providing our employees with competitive salaries and benefits, an

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attractive pension offering, and the opportunity to join the employee healthcare scheme and our share incentive plan.

We provide comprehensive training and development opportunities, including digital skills to help with our Systems Thinking approach and enable remote working where practical, which has been more important than ever this year with restrictions as a result of the COVID-19 pandemic.

We promote diversity and equal opportunity to drive a comprehensive and balanced skill set, and we recruit and promote employees on the basis of merit. We are committed to being an inclusive workplace, supporting employees to reach their full potential whilst feeling valued and included. Employee networks, representing certain groups of employees that may face specific challenges, are overseen by an executive sponsor and support employees through their career progression. Read more about diversity and inclusion on pages 49 to 50 and pages 138 to 140 of the UUG Annual report and financial statements.

We are committed to protecting the health, safety and wellbeing of our people, and have been awarded the workplace wellbeing charter.

We measure employee engagement through an annual survey, and regularly achieve results higher than the UK norm.

We monitor and measure employee performance through annual reviews, and employees at all levels of the company participate in the bonus scheme, so they benefit from company success. The bonus performance measures are the same for all employees as those for the executive directors, and can be found on pages 132 to 134.

Link to principal risks:

- Resource
- Health, safety and environmental

Assets

Our network assets and treatment works are essential to delivering our services for customers and protecting public health, and our energy assets enable us to generate renewable energy, which helps reduce costs and minimise our environmental impact. It is important we have the right systems and procedures in place to monitor and control our assets efficiently and effectively.

Many of our assets are very long term in nature, such as our impounding reservoirs that can last hundreds of years. We must invest to maintain these assets in good condition so they can continue to provide for customers in the long term. We need to make improvements to ensure we can meet the needs of a growing population, and increasingly high quality standards and tighter environmental consents driven by our quality and environmental regulators.

How we manage this key resource

Since privatisation, the significant investment we have made in our assets has provided substantial benefits to customers, including reduced supply interruptions, reduced sewer flooding incidents, and improved water quality, and we expect to continue with a substantial investment programme for the foreseeable future as current environmental legislation requires continued investment. We plan for the long term to help us understand where and when we need to invest in our assets, and we monitor the condition, performance and health of our assets.

We manage our assets in a holistic way that seeks to minimise whole life costs, and we embrace new technology and innovation, which is at the heart of our Systems Thinking approach. This helps us deliver efficient total expenditure (totex) without compromising on quality of service or long-term resilience, saving future operating costs and reducing future customer bills.

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We saw in AMP6 the benefit of accelerating our investment to deliver improvements sooner, and we plan to take the same approach in AMP7, bringing forward £500 million of our capital expenditure into the first three years of the five-year period.

Our assets and infrastructure projects can affect people who live nearby. We consult with these communities in the planning stage and work hard to minimise odours from our wastewater treatment works and other impacts.

Link to principal risks:

- Water service
- Wastewater service
- Resource

Financing

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

It is important that we are able to raise finance when needed to preserve adequate liquidity, and that we manage financial risks such as our exposure to movements in interest rates and inflation, to ensure we maintain long-term financial resilience.

How we manage this key resource

We maintain a robust capital structure, with a responsible mix of equity and debt financing. We monitor our performance against required thresholds for key credit ratios to help us maintain strong and stable investment grade credit ratings. This gives us efficient access to debt capital markets across the economic cycle.

We maintain relationships with a diverse range of banks and access to a broad and diverse range of sources of financing in a number of markets, across which we seek the best relative value when issuing new debt. We periodically refresh our euro-medium term note (EMTN) programme to enable efficient debt issuance under pre-agreed contractual terms, and the board delegates authority to the CFO, allowing us to respond quickly to attractive financing opportunities. This helps us to consistently raise efficient financing at a cost cheaper than many of our peers. This year we published our new 2sustainable finance framework, allowing us to raise debt based on our strong ESG credentials.

We aim to avoid a concentration of refinancing in any one year, and fund long term where possible. Our debt portfolio has a very long average life, and we monitor liquidity forecasts with a policy of having resources available to cover the next 15–24 months of projected cash flows to ensure forward funding needs are met. We have clear and transparent hedging policies covering credit, liquidity, interest rate, inflation and currency risk, and these are aligned with the regulatory model.

Link to principal risks:

- Finance

Our external drivers and relationships

The way we work is impacted by a number of factors external to our business that we must consider and manage.

Natural environment

The natural environment is constantly changing, and we must adapt and prepare for future impacts such as climate change and population growth. We can help mitigate climate change by

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minimising our own emissions and environmental impact. Our use and return of water to the environment is a continuous cycle, and returning water cleanly and safely, as well as managing our catchment land effectively, allows this cycle to begin again from the best starting point.

Link to challenges:

- Protecting and enhancing the natural environment
- Adapting to a changing climate

Stakeholders

The nature of our work means we are at the heart of communities in our region, and have an impact on a large variety of stakeholders. We own and manage huge areas of land in areas of natural beauty that are valued by locals and tourists alike. It is important, therefore, that we give consideration to what matters to those stakeholders, and we build relationships and consult with them in developing and executing our plans.

Link to challenges:

- Securing long-term operational resilience

Technology and innovation

New technologies and innovative ideas present opportunities for us to make things faster, better, safer and cheaper. These can come from a huge variety of places – across different industries and different countries as well as ideas from within our business. We encourage innovation externally and internally at all levels of the business, from our Innovation Lab to our annual CEO Challenge. Technology can also create risks, and this is why our approach to cyber security is so important.

Link to challenges:

- Delivering a reliable service in a changing world

Economic environment

We are impacted by market rate movements, such as interest rates and inflation, but we seek to manage these prudently to reduce risk as far as practical. As well as these direct impacts on the company, the economic climate impacts our customers and their ability to pay their bills. We operate in an area with high levels of extreme deprivation, so helping vulnerable customers is particularly important for us.

Link to challenges:

- Protecting corporate and financial resilience
- Helping customers with affordability and vulnerability

Regulatory environment

Sustainable business means preparing for future market reforms as well as meeting current regulatory commitments. We place great value on our relationships with economic, quality and environmental regulators. We engage actively and regularly, both on progress with our ongoing plans, and on consultations for future reforms where we offer our views and influence where we can.

Link to challenges:

- Securing long-term operational resilience
- Maintaining trust and confidence

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Political environment

Political decisions have the potential to significantly impact on our operations. As a responsible business, we ensure that we abide by the directions set by government, and stay flexible to adapt according to political and policy developments. Therefore, we engage closely with politicians and other policymakers from the government and other parties on a constituency, regional and national level, to understand the development of policy which will affect our business, and to communicate the economic, social and environmental value that United Utilities delivers in the North West, and the UK as a whole.

Link to challenges:

- Maintaining trust and confidence

Our industry and market

To provide great water and more for the North West we must first consider our economic, quality and environmental regulation, and the particular characteristics of our region.

Customers in England and Wales are served by 10 large licensed water and wastewater companies and smaller companies providing water-only services. United Utilities Water Limited, is the second largest, based on the size of our Regulatory Capital Value (RCV), which represents the 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. As a monopoly provider of essential services, we are regulated by various bodies as set out below.

Our economic regulator (Ofwat) sets the price, service and incentive package that companies must deliver in five-year periods, known as Asset Management Plan periods (AMPs). These packages are based on Ofwat's methodology and priorities, and consideration and scrutiny of company business plans. We must therefore engage constructively with Ofwat on its future priorities and methodology consultations, 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 first year of AMP7, covering the 2020–25 period, and our focus has been on delivering and trying to outperform our final determination through:

- delivering higher customer satisfaction than the other companies in our industry;
- beating the outcome delivery incentive (ODI) targets for operational performance;
- delivering our AMP7 scope within our final determination total expenditure (totex) allowance; and
- raising debt finance at a cost below the industry allowed cost of debt.

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 has allowed a further £51 billion across the industry to deliver even more improvements.

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. The latter two, which were in place at the start of AMP6, are included in our operational key performance indicators (KPIs). Our vision is to be the best UK water and wastewater company, so we regularly benchmark our

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performance against these peers. As well as assessment against our water peers, we benchmark our customer service performance against other leading service providers in our region.

Our regulators

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

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 timeframe 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.

How we respond to challenges

Overview

Addressing the short, medium and long-term challenges we face is key to delivering a resilient service. How we respond to these can be seen in the material issues and risks identified below.

Challenge: Delivering a reliable service in a changing world

In an increasingly digitised and instant economy, customers expect more from services now than ever before. This includes the water sector, with high expectations for the reliability of services, the water we supply and the assets we operate.

Many of our assets are ageing compared to other utilities. To meet the expectations of customers and regulators, it is critical that we combine modern technology into our networks and

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management of customer service. Quick response to issues raised by stakeholders, often through digital means such as social media, is part of this growing expectation.

Ensuring a reliable service in the face of a growing population, changing climate and increasing expectations of service requires integrated long-term thinking and targeting investment to ensure both short and longer-term reliability.

How we respond

Our culture of innovation and Systems Thinking approach drive us to adapt our assets and the way we operate to use modern technology and the best new ways of working. Examples include sensors across our network that allow remote monitoring and control from our integrated control centre, and our fleet of alternative supply vehicles (ASVs) that can inject treated water directly into supply while we undertake repairs. We have a substantially enhanced social media presence to respond quickly to stakeholders.

Over one million customers now engage with us digitally, whether this is through our website, our mobile app or on social media. Customers rate us 4.7 out of 5 on the App Store and 4.2 out of 5 on Google reviews.

We monitor the performance and health of our assets, with the help of sensors across the network, and this allows us to be proactive. For example, by monitoring pressure in the water network we can spot issues and fix them before we get a burst, saving costs and sparing customers the impact.

Link to strategic themes

We are installing over 100,000 sensors across our networks to proactively manage issues and sort them before customers are impacted.

We balance our capital and maintenance expenditure to ensure affordability and reliability over the short, medium and long term.

We are targeting a 15 per cent reduction in leakage over the 2020–25 period to further protect the reliability of service and water resources.

Our future plans

We have a number of challenging targets for the 2020–25 period that will help improve the reliability of our service, including helping and encouraging customers to use less water. Further deployment of Systems Thinking will deliver further improvements in the reliability of services.

Challenge: Securing long-term operational resilience

It is vital to our operational resilience that we have plans in place to manage future challenges and maintain the provision of our essential services to customers. Our assets must be prepared to cope with a growing population, and comply with increasingly challenging environmental constraints in areas such as water abstraction and wastewater treatment levels. We must build increased resilience to cope with the anticipated impacts of a changing climate in the long term, including reducing the risk of sewer flooding.

Balancing the risk of service interruptions against investment for the future is a constant challenge for water companies. Understanding what matters to stakeholders to plan our investment programme requires in-depth engagement and analysis, especially in the context of longer-term challenges that span more than five years.

How we respond

It can take many years and require substantial investment to increase the resilience of existing assets or build new ones, which is why our long-term planning is so important. We have detailed plans in place to anticipate future challenges and understand what we need to do to address these, and we build these needs into our business plans for each five-year regulatory period to

Strategic report

ensure we can agree the funding we need to act at the right time. We invested an additional £250 million over 2015–20, from the outperformance we earned over that period, to improve our operational resilience further.

Where possible, we design our assets to work in tandem with the natural environment, which provides more sustainable and efficient solutions, such as our innovative Catchment Systems Thinking approach.

Link to strategic themes

Through innovative approaches we are improving the reliability and resilience of our assets, helping to reduce unplanned service interruptions, and enabling us to be more proactive.

By monitoring the health and performance of our assets we can ensure we invest at the right time in solutions that offer the lowest whole life cost.

We invest in training centres to build technical skills and promote future skills through our education programmes.

Our future plans

Systems Thinking provides opportunities for us to increase our resilience further. Our Haweswater Aqueduct Resilience Project (HARP) will be progressed through direct procurement for customers in AMP7 and AMP8, addressing our biggest operational risk in a critical pipeline that transports water from the Lake District to Greater Manchester.

Link to material issue

- Political and regulatory environment
- Resilience
- Customer service and operational performance

Link to principal risks

- Supply chain and programme delivery
- Resource

Challenge: Protecting and enhancing the natural environment

The UK Government’s current goal is to be the first generation to leave the environment in a better state than we found it. Water management is a key part of this and our industry has a leading role to play. However, the cost of solutions has an impact on customer bills and so we need to balance this goal with the need to maintain affordability and avoid bill shocks.

Environmental regulators set stringent consents for our activities to ensure the environment is protected. We take these obligations seriously and work hard to maintain compliance. This requires striking a balance with environmental impacts, such as the use of natural resources and emissions of greenhouse gases.

Our region is fortunate to have some of England’s finest countryside and wildlife, much of it legally protected being designated as National Parks and Sites of Special Scientific Interest. There is growing realisation, brought further to the fore by the COVID-19 pandemic, of the physical and mental health benefits that access to green space has for people and communities.

How we respond

The EA assesses water companies’ performance across a basket of measures, and we are one of the best-performing company over the last five years.

Strategic report

Our regulatory framework shapes the way we manage natural resources and our interaction with the environment, and we work with our environmental regulators to agree long-term plans.

A phased, long-term approach to address all of the concerns and interests of our many stakeholders, including environmental regulators, ensures that the necessary work can be delivered without placing too much pressure on customer bills by spreading some of the spend over several years. We work with partners to improve the quality of rivers and bathing waters in our region, providing access to the recreational benefits of the natural environment and boosting the local tourism industry.

Our catchment land is open to the public with millions of visits a year. National lockdowns have increased the popularity of many of our sites and made managing visitor numbers at certain sites difficult. We have worked with local interest groups and local MPs to manage these issues when they arise.

Link to strategic themes

Customer engagement tells us that they value the natural environment in our region and want us to protect and enhance it, while maintaining affordable bills.

We use pioneering catchment projects that combine multiple partners and access to other sources of funding to achieve more together for less.

We provide free public access to our land, many of which are in areas of outstanding beauty, with over nine million visits every year.

Our future plans

We are expanding our Catchment Systems Thinking approach, using more natural solutions to create more value for the environment, and we are reviewing our approach to land management to enable multiple benefits from a targeted approach.

Link to material issue

- Natural resources
- Environmental impacts
- Land management and access

Link to principal risks

- Health, safety and environmental
- Political and regulatory

Challenge: Helping customers with affordability and vulnerability

The socioeconomic situation in the UK is still very challenging and water poverty is an important issue. The COVID-19 pandemic, national lockdowns and slowdown of the economy will only make this more difficult for many customers. How we respond will be crucial to securing and maintaining customers' trust and confidence in the sector in the years ahead.

Our region suffers high levels of extreme deprivation. Eighteen per cent of households in the North West are affected by water poverty, higher than the national average, and research indicates that many customers who are behind on water charges are behind on other bills and many have a pay-day loan. Our stakeholders are interested in how we provide support for customers in vulnerable circumstances beyond just financial distress, such as disability, first language not being English, or temporary vulnerability brought on by illness or a life event.

Strategic report

How we respond

We have a leading approach to affordability and vulnerability, with the sector's widest range of assistance schemes. We are helping over 200,000 customers through our affordability schemes, and through our assistance schemes 71,000 customers became water debt free this year.

Customer support has been at the forefront of our activities throughout COVID-19, such as increasing the number of customers eligible for our social tariff, 'Back on Track', and providing the option to request a three- month payment holiday without affecting credit scores.

We led the sector in establishing our Priority Services scheme, with dedicated teams providing additional support to customers with physical, mental health, or financial difficulties during an incident. This scheme is now accredited by the British Standards Institute (BSI), and over 128,000 customers are now registered for this support, with more joining every day.

Link to strategic themes

We have a wide range of schemes that help customers struggling with affordability concerns and other vulnerable circumstances.

Initiatives such as our affordability schemes help us to manage our household bad debt expense.

Through the charity FareShare we have provided support that has enabled 600,000 meals for struggling families in the North West.

Our future plans

Through bill reductions and financial support we will help move over 300,000 customers out of water poverty by 2025, extend our Priority Services offering to over 210,000 customers, and improve the quality and scale of the support we provide.

Link to material issue

- North west regional economy
- COVID-19
- Affordability and vulnerability

Link to principal risks

- Retail and commercial

Challenge: Adapting to a changing climate

The biggest anticipated impact on our natural environment comes from climate change. We must plan well into the future to understand what changes we are likely to experience in our region as a result of climate change, and continually adapt to meet the risks and opportunities this presents.

The main opportunity is the potential for water sharing, as our region typically receives more rainfall than the comparatively drier south.

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

We need to ensure we have access to resilient water resources, reduce leakage, and encourage less water use in the future to protect this critical resource. We need to ensure our infrastructure can cope with increased surface water to reduce the risk of flooding.

Strategic report

How we respond

Our response to climate change risk involves mitigation (minimising our greenhouse gas emissions) and adaptation (ensuring our services are resilient to a changing climate). Where practical, we generate renewable energy on our sites through solar panels, wind turbines, and the use of bioresources at wastewater treatment works, helping to reduce our emissions. We have reduced our carbon footprint considerably since 2005/06 and have set ambitious science-based targets as part of our continued efforts to reduce emissions. We have committed to six pledges to help us achieve significant further reductions in emissions. Read more about our approach to climate change on pages 63 to 83.

We have detailed plans that set out how we will adapt to meet the challenges of climate change, and we are targeting a 15 per cent reduction in leakage over AMP7.

We work with third parties to encourage sustainable drainage solutions to help cope with surface water in periods of heavy rain and are finalising a Drainage and Wastewater Management Plan with key authorities across the region.

Link to strategic themes

We help customers to use less water, with advice and free water saving gadgets, saving them money as well as protecting this resource.

Our renewable energy generation helps to reduce our reliance on purchasing energy and therefore save costs.

We have reduced our carbon footprint significantly in recent years and are committed to further reduce our emissions.

Our future plans

We have a detailed 25-year Water Resources Management Plan, Drought Plan, and we plan to publish our third adaptation report in 2021 setting out how we aim to adapt to meet the challenges of climate change. Read more at unitedutilities.com/corporate/about-us/our-future-plans

Link to material issue

- Climate change
- Resilience
- Leakage and water efficiency

Link to principal risks

- Water service
- Wastewater service

Challenge: Maintaining trust and confidence

Strong relationships are based on trust. Being open, honest and transparent is key to building and maintaining trust and legitimacy. As well as reporting openly this means setting out commitments and delivering on them. Our stakeholders want to know that we are treating employees fairly, protecting customer data, and paying our fair amount of tax.

The increasing pace of globalisation means many customers feel disconnected from many large businesses. This has led to growing calls for companies to demonstrate how they are contributing to society as a whole and operating in the public interest.

In recent years the UK water sector has faced challenges to its legitimacy, amplified by some specific issues at a small number of companies. Consequently, trust has been eroded and questions raised about the ownership structure of the sector, and Ofwat has called for further

Strategic report

transparency and disclosure around board leadership and decision-making processes, as well as starting discussion on companies' contribution to public value.

How we respond

We have open and transparent reporting around all of our equity and debt financing arrangements, do not use offshore financing vehicles, and we have secured the Fair Tax Mark independent certification for the past two years.

We have updated our human rights policy which can be found on our website, with links to other related policies, including our modern slavery policy and whistleblowing policy.

Cybercrime has been on the increase and, as the holder of customer information, it is a threat we take very seriously through our policies and dedicated data protection team.

We work with suppliers and contractors whose principles, conduct and standards align with our own. Our key suppliers have committed to United Supply Chain. We are a signatory to the Prompt Payment Code, and fully comply with rules on reporting payments to suppliers.

Link to strategic themes

We engage on a continual basis with customers to understand their expectations in relation to service and behaviour, through activities like our quarterly brand tracker.

We maintain a stable credit ratings with key agencies which helps us retain efficient access to the debt capital markets.

We set qualitative and quantitative performance targets across all of our stakeholders to evidence how we are delivering on our purpose.

Our future plans

Operating in a responsible manner is a key driver of trust with our stakeholders. Our continued compliance with the corporate governance requirements of a listed company helps ensure the transparency of our reporting and behaviour.

Link to material issue

- Cyber security
- Corporate governance and business conduct
- Trust, transparency and legitimacy

Link to principal risks

- Security
- Conduct and compliance

Challenge: Protecting corporate and financial resilience

We believe the most resilient and effective companies have a diverse, engaged and motivated workforce, who can bring their different ideas and perspectives to help us find solutions.

The availability of skilled engineers depends on economic and social conditions, and we need to ensure an appropriate pipeline of skills in younger generations too, especially in the areas of science, technology, engineering and mathematics (STEM). As the world becomes increasingly digital, we need to have the right people and skills to manage our business in the modern world.

Long-term financial resilience starts with a robust balance sheet and management of financial risks. Companies have to be aware of their own financial situation and make sure that they understand the financial resilience of others, such as suppliers and former employees.

Strategic report

How we respond

We support employees to achieve their full potential and feel valued and included, regardless of their gender, age, race, disability, sexual orientation or social background.

We build skills resilience internally through training and development, including digital skills.

We have graduate and apprentice schemes, and ambassadors that work with schools and education institutes to encourage the younger generation to pursue STEM careers.

We maintain good relationships with employees, and employee representatives, to ensure an engaged and motivated workforce, and we continually strive to build diversity across all types of role and all levels within our business. We have a Gender Equality Network that helps by providing role models, mentoring and opportunities. Women are represented at all levels of our company, and 38 per cent of our combined board and executive team is female, as can be seen below.

We consistently adhere to the highest levels of governance, accountability and assurance. We have a strong balance sheet, a secure pension position, and take a prudent approach to financial risk management, which delivers long-term predictability and resilience to financial shocks. Our clearly articulated policies, covering a variety of market risks, help us reduce our exposure to the economic and regulatory environment, providing more predictable returns.

Link to strategic themes

As we did in AMP6, we are accelerating our capital programme into the early years of AMP7 to deliver service improvements for customers earlier.

Our robust capital structure and relatively low gearing provide long-term financial resilience and future financial flexibility.

We have award winning training centres, the only ones in the water industry approved to run Ofsted accredited programmes.

Our future plans

Creating strong relationships with employees and suppliers will help build a resilient value chain, and our focus on good corporate governance and prudent financial management ensures we have a basis for long-term success.

Link to material issue

- Financial risk management
- Corporate governance and business conduct
- Diverse and skilled workforce

Link to principal risks

- Resource
- Finance
- Conduct and compliance

Strategic report

(1) Group board as at 31 March 2021
(2) Executive team excludes CEO and CFO, who are included in group board figures
(3) As at 31 March 2021, there were eight male and three female employees appointed as statutory directors of subsidiary group companies but who do not fulfil the Companies Act 2006 definition of 'senior managers'
(4) Wider employees as at 31 March 2021

How our responsible approach has helped us make a difference during the COVID-19 pandemic

How we responded

We serve some of England's most socioeconomically deprived communities, many of which have been severely impacted by COVID-19. We have prioritised supporting customers, the wider communities and our colleagues during this difficult time. Recognising the importance of water for public health and sanitation, especially with the emphasis placed on washing hands, we have maintained water supplies and wastewater services throughout the pandemic, keeping our employees safe while they carried out their duties.

Our communication with stakeholders during this time has been more important than ever, whether that has been encouraging customers to get in touch if they have been impacted financially by the pandemic or issuing guidance reinforcing government guidelines to protect employees, suppliers and customers. Our consultation for the Haweswater Aqueduct Resilience Programme (HARP) was stopped in its tracks by COVID-19. We changed approach, developed a virtual consultation, and as a result we have seen better engagement than our traditional approach.

Board oversight

COVID-19 has changed ways of working for everyone and our board has been no exception. We have continued to hold scheduled board meetings in a virtual format to ensure that the board's oversight has remained effective. We were able to hold a number of events during the year, including a board strategy day, conducting external board evaluation and providing UUG's major shareholders with the opportunity to virtually meet with the Chairman.

Outlook

Lessons we have learnt from the pandemic will shape how we deliver for stakeholders in the future. We now have an even better understanding of our customers and how we can support them. We have been challenged to think more creatively about how we engage with our stakeholders.

The pandemic has accelerated our digital strategy and changed our ways of working in such a way that we do not see a return to how we worked before.

Although there remains a degree of uncertainty as to how the UK and the economy will continue to recover after the pandemic, it has taught us that our sustainable and responsible approach to business means we can tackle future challenges as they emerge.

Communities

How we responded

We have continued to support young people in our region throughout the pandemic.

Recruitment of apprentices and graduates has continued uninterrupted and we are supporting the Kickstart Scheme, offering training and meaningful work placements, with the support of our supply chain partners, to an initial 250 young people.

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This year, as part of our ongoing charitable donations, we supported the FareShare charity in delivering 600,000 meals to struggling families via local foodbanks and replaced one of the charity's delivery vans, helping to ensure meals get to families in need over the next eight years.

During school closures our education team created a Home Learning Hub, providing teachers and children with home schooling material.

Customers

How we responded

Recognising affordability has been even more important during the pandemic, we took swift action and were the first company to secure support and regulatory approval for an extension to our social tariff, with an additional £15 million available to help customers keep out of debt.

We are committed to providing over £71 million of financial support over AMP7, and we have accelerated payments this year to provide much needed assistance to struggling households.

We have increased the extensive financial assistance we already provide, for instance by widening eligibility for our 'Back on Track' social tariff.

Employees

How we responded

We facilitated home working for over 3,000 of our employees with the remainder of our workforce continuing to work at COVID- secure facilities.

A huge focus has been on the wellbeing needs of our colleagues, in particular mental health support. We have delivered initiatives to help build resilience across our workforce, including e-learning and bitesize webinars.

We have not furloughed any employees, but, recognising that our employees and their families have not been immune to the hardships as a result of changing circumstances, we created a Staff Outreach Scheme to provide one-off grants through a confidential application process.

Environment

How we responded

As we emerge from the pandemic, we are determined to play our part in supporting a green recovery in the North West. We have accelerated investment plans, spending more over the early years of AMP7 than our original business plan. This will support recovery to build a greener, more sustainable future, all while helping the region to recover from the economic impact of the COVID-19 pandemic.

Our new investment plans include delivering environmental improvements in rivers, protecting habitats, combating invasive species, enhancing water quality, drainage and reducing pollution. This investment will generate lasting benefits for the environment, for customers and for communities.

Investors

How we responded

Throughout the pandemic we have maintained regular contact through calls and video calls with both existing and new investors of UUG. This year we offered major shareholders the opportunity to meet, albeit virtually, with the Chairman as part of UUG's active investor relations programme.

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Suppliers

How we responded

We have continued to work closely and actively engage with our supply chain during the pandemic. Looking out for the health, safety and wellbeing of our suppliers has been as important to us as that of our employees.

We continued with the majority of our construction programme throughout the national lockdowns, supporting our supply chain partners.

We acted swiftly at the beginning of the pandemic to accelerate payments from 14 days down to seven days to help with cash flow and offered a range of payment options.

How we plan for the future

Our approach and short, medium and long-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, to stakeholders and to 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, so we can ensure resilience in order to continue to fulfil our purpose.

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.

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 long-term challenges and opportunities.

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

This involves looking at a lot of current and predictive data from various sources, such as economic forecasts, expectations for population growth in certain areas, 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 our risk management process.

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

- Climate change;

Strategic report

- 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 the challenges ahead and how we will focus our resources and talents in order to meet them: unitedutilities.com/corporate/about-us/our-future-plans

This includes our 25-year Water Resources Management Plan (WRMP) covering the 2020–45 period, which was developed and published in 2019 following consultation with stakeholders, and our Drought Plan, which was published in 2018 with an amendment appendix in 2018/19. 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, and the actions we will take to manage the risk of a drought. In 2023 we will publish an update to our WRMP and, for the first time, publish a Drainage and Wastewater Management Plan (DWMP).

We create long-term value for stakeholders by:

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

Medium-term planning (5-10 years)

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

The business plans we submit focus mainly on the subsequent five-year AMP period whilst providing a high-level view of the following AMP. This provides medium- term planning visibility of between five and ten years at any one point in time.

It is important that our ambitions align with those of our regulator, therefore we carefully evaluate all consultation and methodology publications from Ofwat and engage with them to put forward our views and help ensure a balanced approach that creates value for all stakeholders.

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 FD, which sets the price (in terms of total expenditure and customer bills), level of service, and incentive package that we must

Strategic report

deliver over the five-year period, and an allowed return we can earn (expressed as a percentage of Regulatory Capital Value). When we receive the FD, we refine our company business plan for any changes, such as in allowed expenditure or performance level targets, and we must decide whether to accept the FD.

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 totex proposals we put forward.

We made a flying start to our 2020–25 plans by investing an additional £130 million in 2019/20, helping us deliver a strong start to this new period. 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 years one to three of the five-year period. Our total expenditure for this period will be extended by £300 million, with this expenditure extending our environmental programme.

Our strategy of delivering the best service to customers at the lowest sustainable cost in a responsible manner 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 is made up of the base allowed return and any outperformance/underperformance, on an annual and cumulative basis for each five-year period.

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.

Before the start of each financial year, we develop a business plan for that year, which is reviewed and approved by the board. This sets our annual targets, designed to help deliver further improvements in service delivery and efficiency, and to help move us towards achievement of our five-year goals. Performance against these annual targets determines annual bonuses for executive directors and employees right through the organisation, who are remunerated against the same bonus targets as the executive team.

To avoid short-term decision-making and ensure management is focused on the long-term performance of the company, as well as these annual targets executive directors are remunerated through long-term incentive plans that assess three-year performance, measured during the current period through total shareholder return, sustainable dividends and customer service.

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

It is vital that we retain flexibility within this short-term planning so we can adapt to meet challenges that may arise during each year, and deliver high quality and resilient services to customers in the most effective and cost-efficient way possible. This may involve bringing enhancements forward to deliver improvements for customers early, investing further into the business to maintain service, or delaying projects to occur later in the regulatory period in order to prioritise expenditure and allow our people to spend their time dealing with any unexpected challenges that arise.

The challenges presented by COVID-19 are a clear example of why this flexibility is crucial. We enacted our robust contingency plans, enabling us to quickly and efficiently move thousands of

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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 are critical for public health at this time. Read more about our response to the challenges of COVID-19 on pages 38 to 40.

How we measure our performance

To measure progress on delivering our purpose and creating value for all our stakeholders, we monitor and measure our performance against each stakeholder group.

Our key performance indicators

Overview

During the 2015–20 period, we reported against a range of operational KPIs that were aligned to our strategic themes to demonstrate how we realise our purpose and deliver on our vision.

Our purpose drives us to create long-term value for all our stakeholders, so between 2020 and 2025 we are measuring our performance by reference to the value we create for each of our stakeholder groups.

Operational KPIs

Our operational KPIs include one main metric for each stakeholder group, based on the top material issues identified through stakeholder engagement. A description of these operational KPIs, our targets for each, and our performance against these targets can be seen on pages 44 to 54.

Our executive bonuses and long-term incentives are closely aligned to financial and operational KPIs, as highlighted in the remuneration report on pages 132 to 134.

Financial KPIs

Our financial KPIs assess both profitability and sustainability of our business from a financial perspective. They are largely the same as the 2015–20 period, with the addition of having low dependency defined benefit pension schemes with nil deficit.

This recognises the increasing importance of this strong and secure position for our people, representing a significant driver of relative value.

A description of these financial KPIs and our performance against our targets can be seen on pages 55 to61.

Our other performance indicators

Overview

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

As discussed on pages 13 to 19, we engage with a variety of stakeholders and this gives us a view of what matters most to them.

We report on a selection of other metrics on pages 44 to 54 of this report, based on the measures shown to be of highest interest to our stakeholders.

For example, for customers our KPI is Ofwat's measure, C-MeX, but on page 57 of the UUG Annual Report and financial statements we report on Ofwat's D-MeX measure, the level of customer complaints, vulnerability support, customers lifted out of water poverty, and the impact of water efficiency measures.

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On environmental performance, our KPI is the overall assessment by the Environment Agency and on page 65 of the UUG Annual Report and financial statements we report on more specific environmental performance indicators, such as leakage reduction, climate change, proportion of waste going to beneficial use rather than landfill, and measures of natural capital.

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

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)

Overview

Performance against our regulatory contract is monitored and assessed each year, and reported within an Annual Performance Report (APR), as required by Ofwat for all water companies since the start of the current regulatory period in 2015/16, replacing the previous 'regulatory accounts'.

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

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

Our APRs for previous years are available on our external website, and the APR for 2020/21 will be published in July 2021.

Find our more information on our external accreditations

In addition to our KPIs and regulatory targets, we monitor our performance against an assortment of ESG metrics that are of interest to our many stakeholders.

We report against these within this report on page 62 and on our website at **unitedutilities.com/corporate/responsibility/our-approach/cr-performance**

Operational performance

Our performance at a glance

Communities

Our work puts us at the heart of local communities in the North West of England, where customers and employees live and work. We understand the impact our work can have on everyday lives across our region, and we seek to play an active role in tackling the issues that matter most to these communities through active engagement and investment, developing strong relationships and building partnerships where we work together to generate solutions. We also look after beautiful landscapes and open our land to the public, which supports the regional tourism industry and offers physical and mental health and wellbeing benefits for communities through access to relaxation and recreation.

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 between 2010 and 2020.

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The average investment between 2010 and 2020 was £2.56 million per annum and in 2020/21 we supported communities through direct community investment of £2.15 million (calculated using the B4SI method). This is slightly lower than we were targeting to invest, mainly as a result of much lower community activity as a result of the impact of COVID-19. However, we contributed an additional £2.7 million from our Trust Fund to help those struggling to pay their bills and a further £15 million was made available to help customers reduce their water bill to an affordable amount through extending our social tariff. As we emerge from the pandemic, and events can safely recommence, we expect our community investment to increase.

Helping young people

We are committed to supporting the Government's 'Kickstart' programme by providing 250 placements to young people, working with our supply chain. Our new employees will have a dedicated placement manager as well as a Kickstart Skills Coach, and will also receive job-related and employability skills training to enhance their CVs in order to help secure employment in the future. We work with local schools and training facilities to promote skills for the future, including youth programmes that support young people not in education, employment and training (NEETs) to help improve social mobility in our region and break down barriers in bringing people from all backgrounds into employment. It is estimated this programme has generated over £9 million of social value through avoided welfare costs and new employment. During the school closures brought about by the pandemic lockdowns, our education team created a home learning hub that supported teachers and children across the region, and even extending overseas, with materials for home schooling. Recruitment of apprentices and graduates has continued uninterrupted, with the help of some online challenges, skills sessions and live streamed assessments while face to face interaction was limited. We have continued to create our early careers pipeline welcoming 67 apprentices and graduates in 2020/21.

Social mobility

In October we hosted the sector's first Social Mobility Summit, an online event at which more than 100 organisations joined us for the launch of our Opportunity Action Plan – another first for the sector – which aims to identify and share best practice and leading edge thinking from businesses that are successful in promoting social mobility, including case studies from our own employees reflecting the progress we have already made.

Charitable support

Our ongoing charitable support, including a voluntary salary reduction by Board members at the height of the COVID-19 pandemic, has helped provide support to local communities. One of our donations to the FareShare charity has supported them in delivering 600,000 meals to struggling families across the North West via local foodbanks, and will replace one of the charity's delivery vans, helping to ensure 6.4 million meals get to families in need over the next 8 years.

Community engagement

We build trust with local communities through effective engagement, whether that is around large capital projects or day to day management of our landholdings. Our consultation for the Haweswater Aqueduct Resilience Programme (HARP) was stopped in its tracks by COVID-19, half way through the traditional face to face exhibitions. We changed approach, developed a virtual consultation, with accessible content advertised through letters and social media, and, as a result, we have seen better engagement. We received over 100 per cent more feedback compared with the traditional approach with over 8,000 hits to the specific HARP section of the website. 69 per cent of all feedback has been supportive of the plans. Given the success of this approach, we will continue with virtual consultations for other aspects of this project.

Access to our land for recreational use

As a result of COVID-19 restrictions, there has been a marked increase in the number of visitors to our catchment land to enjoy the countryside and benefit from open spaces. While the majority of visitors have respected the countryside, sadly a small minority have not. Our teams have worked hard to address this anti-social behaviour through a variety of methods, including

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targeted social media campaigns on issues such as moorland fire risk, improved site signage and the creation of local stakeholder groups. We are currently testing several ideas to better connect visitors to the land and to encourage them to behave responsibly.

Customers

We put customers at the heart of everything we do. This relentless focus drove us to deliver significant and continuous improvements over AMP6, ending the period as a leading water and wastewater company. Despite the challenging environment we have continued to operate in during the pandemic, customer satisfaction has remained high. Reliable access to clean water has been more important than ever before, and we have continued to provide a robust service for customers throughout the year. Serving the most economically deprived areas in the country, we are always mindful of the need to help customers who struggle to pay their bills. We reduced typical household bills by 5 per cent this year in real terms, have committed to provide £71 million in financial support to customers over AMP7, and have an extensive range of schemes offering financial assistance and tailored support for customers struggling with affordability and vulnerability. We are delighted to have received a positive recommendation for continued certification to BS 18477:2010 which is the accreditation for our Priority Services scheme and one of our customer ODI measures looking at the quality of services provided to vulnerable customers.

Our key performance indicator to measure customer satisfaction over AMP7 is Ofwat's C-MeX measure, in which we target being in positive reward territory.

At the end of the year we are ranked 5th out of 17 companies, the highest listed company, achieving a reward of £2.1 million for C-MeX performance in the first year of AMP7. While our written customer complaints performance for the year has fallen below our targets, in part reflecting the higher level of complaints during the dry spring in 2020 and our focus on collecting cash from those customers who are able to pay, but choose not, we still expect our relative performance to be upper quartile compared with the other water and wastewater companies.

Customer service

We have significantly increased the availability and performance of our digital channels with over 1 million customers engaging with us digitally, driving both service improvements and cost efficiencies. Customers rate us 4.7 out of 5 on the App store and 4.2 out of 5 on google reviews.

We have been proactive and used targeted communications with customers to offer support to those impacted financially by the pandemic and struggling to pay. We have achieved all of our reputational performance commitments, most notably continued certification to BSI standard for our Priority Services scheme that supports over 133,000 customers, and we were recognised as providing the best customer support initiative at the Utilities and Telecoms Awards for the support provided to customers during the pandemic. We are one of only 14 brands in the UK with the Institute of Customer Service Accreditation with distinction.

For developers, customer experience is measured in AMP7 by D-MeX, of which there are two elements: quantitative (service level agreement performance); and qualitative (customer satisfaction survey). For 2020/21, we are ranked first in the sector for our quantitative performance, with final qualitative results expected later in the year. We estimate our overall industry position to be fourth. This strong performance reflects the transformation programme we are delivering in this area that continues to deliver tangible and much improved results, benefiting all developers who are building in the North West.

Operational performance for customers

Our AMP7 business plan includes 46 customer commitments, delivering the outcomes that are important to customers and measured through customer ODIs.

Our performance has been strong across the broad range of our activities with us having met or exceeded over 80 per cent of our performance commitments for the year. We have delivered particularly strong performance in the areas of hydraulic flood risk resilience and pollution where

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we have delivered another year of sector leading performance with no serious pollution incidents for the second consecutive year. We were also able to deliver leakage at its lowest ever level and have more than halved supply interruptions to customers – outperforming our targets on both these key service delivery measures.

We entered AMP7 knowing that our biggest challenge would be against our internal flooding ODI and this is the measure that has yielded the largest penalty this year. As part of the £300 million extension to our AMP7 totex plans, we will be investing around £100 million in Dynamic Network Management (DNM) – a ground breaking application of Systems Thinking using state of the art sensors and predictive machine intelligence to move to a more proactive management of our wastewater network. This new digital capability is expected to improve service to customers and improve performance against our internal flooding ODI.

We work hard to encourage customers to save water through water efficiency programmes, helping them to preserve this precious resource and save money on their bills. More customers have spent more time at home during the pandemic and used more water for sanitation, increasing per capita consumption (PCC) measures for 2020/21. Recognising that the long term impact of COVID-19 remains uncertain and that there may also be a variety of drivers of changes in behaviour, Ofwat has proposed to assess company performance for this customer ODI at the end of the AMP when fuller facts and evidence of absolute and relative company performance are available.

We have our own in house app development capability and this is paying dividends in creating digital capability for our field and customer facing teams with agility, flexibility and at low cost. Our new voids app which helps us to easily identify unbilled but occupied properties has contributed to a 93,000 reduction in the number of void properties in the year, helping us earn maximum customer ODI reward on voids this year and underpins a further £24 million reward over the AMP.

Haweswater Aqueduct Resilience Programme (HARP)

In November 2020, we successfully completed the replacement of the Hallbank section of the Haweswater Aqueduct, part of a critical asset that delivers around a third of our total water production to 2.5 million people in Cumbria, Lancashire and Greater Manchester. Work to replace the majority of the aqueduct is expected to be undertaken using a direct procurement for customers (DPC) approach and we have been preparing for a DPC tender in 2021/22. If the tender process proceeds as planned, contract award is anticipated in 2023, with construction to begin later in the AMP.

Cash collection

Despite the impact of COVID-19, our overall cash collection has performed well throughout the year. We are encouraged by the continued growth in our direct debit volumes, now at 72 per cent and one of the highest across the industry. Overall, the proportion of customers on a payment plan has continued to increase to 82 per cent despite the challenging economic environment and providing a high level of collection certainty for a significant proportion of the household customer base.

We are recognised as a leader in credit management and collections across all industries, not just water. In the year we have won three external awards for our credit services, most recently winning the Utilities and Telecoms Team of the Year at the 2020 Credit Awards. Our industry leading approach to collections and innovative affordability offerings have ensured we were well placed to respond to the challenges brought about by the pandemic.

In the current year, we have enhanced our credit reference sharing process to include another agency with a greater high street focus. This has further extended our footprint and will facilitate improvements in our collections activity, and is just one example of our comprehensive approach to collections activity, supporting our ability to collect cash from customers who have the ability to pay, but attempt to avoid doing so.

Affordability

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When the country first went into lockdown we saw an increase in demand for affordability support. The initiatives we delivered over AMP6 enabled us to respond efficiently and effectively, with our Payment Break scheme giving over 8,000 customers the breathing space they required.

The nature of the pandemic and the significant impact it is having on customers' lives has meant we have had to consider the appropriateness of continuing our normal billing and collection activities and the most suitable means of engagement. While as an industry we took steps to pause collection activity, our COVID-19 response encouraged customers to contact us if they had been impacted financially by the pandemic and found themselves struggling to pay. We carried out targeted activities aligned to specific customer segments and changes in customer behaviour to engage with customers, actively promoting our range of affordability support, ensuring customers knew they could talk to us about their bill, and highlighting alternative ways to pay. Over the course of the year we sent over 5 million proactive customer communications, a 30 per cent increase on the previous year.

We have an extensive range of schemes available to help customers and around 200,000 are currently benefiting from that help. Recognising affordability has been even more important during the pandemic, we took swift, proactive action and were the first water company to secure support and regulatory approval for an extension to the scale and scope of our social tariff, allowing us to support a broader range of customers whose income has been affected by COVID-19. This augments our support schemes this year with an additional £15 million to help customers keep out of debt and was intended to support an additional 45,000 customers who have been furloughed, are claiming through the self-employed income support scheme (SEISS) or are now unemployed, by reducing their water bill to an affordable amount. Through efficient use of the additional £15 million funding secured we were able to support 73,000 customers – 62 per cent more than originally estimated - preventing customers from falling into debt. This additional support meant that in the year we supported 160 per cent more customers via our Back on Track scheme than the previous year. We promoted the new scheme directly to customers, via partner organisations and the Hardship Hub to increase overall awareness. The £71 million financial support we have committed to provide over AMP7 is the largest of any water company, and we have accelerated payments this year to provide much needed assistance to households struggling as a result of the economic impact of the pandemic.

We continually innovate to further enhance our affordability processes, and we are piloting a first-of-its-kind real-time income verification tool to streamline eligibility for reduced-rate social tariffs. We're proud to be the first water company in the UK to roll out an Open Banking solution for social tariff applications, modernising our income verification. In March 2021 we were the first water company to begin data sharing with the DWP, leveraging the new provisions under the Digital Economy Act, to assist people living in water poverty. We're excited to be able to use these new provisions to continue to proactively provide lower bill support to customers.

Employees

Our people are critical to the success of our business and it is important we give them the opportunity to develop their skills and knowledge and support them with the most effective technology. We have continued to invest in skills training throughout the pandemic and have accelerated our digital strategy to support new ways of working. The health and wellbeing of our employees is paramount and keeping them safe remains our primary concern. During the initial lockdown in 2020, we moved 60 per cent of our workforce to home working and the remainder continued working at our COVID-secure facilities. Around 80 per cent of our employees were designated as key workers, delivering our essential services to customers. We have largely continued with business as usual, operating within COVID guidelines and in line with the Government roadmap out of lockdown, while defining and shaping the way we will work post-COVID based on the changes in the last year.

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.

This year we achieved 89 per cent engagement, which is five per cent above the UK High Performance Norm and is the highest engagement score we have achieved while comparatively

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tracking engagement over the last six years. It is also a five per cent increase from 2020 engagement levels and is 15 per cent better than the UK Norm and nine per cent better than the Utilities Norm. We are rated 4.5 out of 5 by former and current employees on Glassdoor and 92 per cent of our employees would recommend United Utilities to a friend as a great place to work. We are delighted to be in the top one per cent of 15,000 companies across Europe, and the highest placed water company, for our overall approach in the Diversity Leaders ranking. The survey, by Statista and the Financial Times, surveyed employees on their employers' efforts to promote diversity.

Protecting colleagues through the COVID-19 pandemic

During the pandemic, we have facilitated home working for over 3,000 of our employees and are providing support for employees' health, safety and wellbeing whilst temporarily working at home in extraordinary circumstances. As well as facilitating home working for more than half of our employees, we have introduced a range of measures to ensure those who are still working on sites and in the field are able to do so in a COVID-secure way. We conducted over 390 COVID-secure risk assessments across all our operational sites and carried out a number of control measures to ensure they met the Government's requirements for COVID-secure workplaces. This included temperature checking stations, extra sanitation provisions, safe desks and one-way procedures in offices to ensure social distancing can be maintained. Additional personal protective clothing has been provided and we have adapted new ways of working for our front line field employees. We adapted the way we carry out our mandatory health surveillance checks to virtual assessments and more recently COVID-secure face-to-face assessments.

With the involvement of over 200 trained mental health supporters and wellbeing champions across the business, we have supported the wellbeing needs of our colleagues, delivering initiatives to help build resilience across our workforce. This includes delivery of several bitesize webinars on topics such as mental health, stress control, and managing change to around 2,000 people over 20 webinars. We have been encouraged by the take up of the zero suicide alliance e-learning module which now includes a specific module on COVID-19 and isolation, and have produced new resource packs and initiatives to help our workers through winter. Crucially, we engage regularly with managers, providing awareness of the support services available and how to make best use of them and the widely introduced Wellness Action Plans, in order to enable managers to have wellbeing conversations with their teams.

We have not furloughed any employees, but we are aware that our employees and their families are not immune from the hardships caused by the economic impacts of COVID-19. Therefore, we have established a staff outreach scheme that provides financial support to employees whose families are struggling financially as a direct result of the pandemic.

Committed to equality, diversity and inclusion

We want fantastic people to enable us to deliver a great public service now and into the future, so we are determined to make sure we are reaching and recruiting from every part of our community. We are supporting employees to achieve their full potential and feel valued and included, regardless of their gender, age, race, disability, sexual orientation or social background. Our employee diversity networks, including LGBT+; GENEq; ability and multi-cultural groups have a growing membership of 730 people, and play a pivotal role in providing insight, raising awareness and giving support to colleagues. We are committed to creating a diverse and inclusive workforce and so we are delighted to be one of the top one per cent of 15,000 companies across Europe in the Financial Times' Statista Survey for Diversity and Inclusion Leadership.

We are working hard to improve how we attract women into the industry, and developing women within our existing workforce. We are seeing good progress with increasing numbers of female graduates and apprentices in our talent pipeline and 96 per cent of our current female workforce recommend United Utilities as an employer. Following our 2021 Annual General Meeting (AGM), the measurable targets of 33 per cent female representation on the board and one director of non-white ethnicity will be met. We achieved inclusion in the Bloomberg Gender Equality Index, recognising our commitment to gender equality and transparency.

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Training and development

Our technical training academy established in February 2014 has provided skills development and certification to over 2,800 people to date, including programmes for those individuals not in education, employment or training (NEETs). Many people have received multiple training opportunities such that in total, around 11,000 technical training sessions have been delivered over that period. We are the only water company currently governed by Ofsted (Office for Standards in Education), with a “good” overall rating.

Ensuring everyone goes home safe and well

Over the last couple of years our health, safety and wellbeing agenda has centred on behaviours and the part they play in accidents and the culture across our organisation. Having spent a number of years focusing on site standards, asset condition, training and personal protective equipment, it was clear from our root cause analysis that behaviours play a key part in many of the accidents we have had. We delivered our Home Safe & Well Behavioural Safety programme to everyone in the company and we are embedding a culture of looking after ourselves and each other, to ensure we all go home safe and well.

We are seeing improvements in a number of important performance measures, including the number of accidents, the severity of accidents and an increase in hazard and near miss reporting. Our employee accident frequency rate for 2020/21 was 0.094 accidents per 100,000 hours worked, representing a 15 per cent improvement on performance from the prior year. Our contractor accident frequency remained broadly consistent despite an increased workload at the start of AMP7, with 0.087 accidents per 100,000 hours worked, compared to 0.083 last year. Our aim by 2030 is that no one will be harmed while working on our behalf, and we will actively promote, support and improve their wellbeing.

Environment

We are fortunate to have many areas of natural beauty within our region, and these are important in offering health, fitness and wellbeing benefits to local communities and drivers for tourism in the area, as well as being essential for us to deliver our services to customers. It is of great importance we continue to protect and enhance the environment across the North West, and manage our land responsibly to improve the environment in our region for future generations. We delivered a number of environmental improvements over AMP6, including improving 338.5 kilometres of rivers, significantly reducing our carbon footprint, increasing our renewable energy production and ensuring zero emissions energy usage. We have agreed an environmental improvement programme to be delivered in AMP7 that will continue to improve the river, bathing and shellfish water quality for the benefit of customers and visitors to the North West as well as society as a whole. Our investment in AMP7 is expected to result in an improvement in water quality in 1,315km of rivers in the North West. Having completed the first year of the period, we remain on track for the improvements we have committed to.

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 within the water industry each year.

In the assessment for 2020, we expect to be awarded the maximum 4 stars, meaning we would be classed by the Environment Agency as an “industry leading company”.

Leakage reduction

We have beaten our leakage target for the 15th consecutive year and we are now at the lowest ever level of leakage reported in the North West. Our leakage performance improvement has been achieved through a combination of techniques. Alongside satellite technology to geo-locate potential leaks in our network and sniffer dogs to accurately locate the leak, we have deployed 66,000 acoustic loggers since 2019 with a further 29,000 being installed over the next year. We have recruited around 20 per cent additional leakage detection resources, further supported this year by our first intake of apprentices on a bespoke two year technical training scheme, mitigating the risk of a national shortage in leakage technicians. Over AMP7, we plan to reduce

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total leakage by at least 15 per cent, with a delivery plan that continues to make best use of available technologies and is flexible to ensure that we can embrace the heightened level of innovation in this area.

Pollution performance

In 2020, we had no serious pollution incidents for the second year running, and have reduced total pollution incidents by almost a third. Here, we are seeing the benefits of delivering the action developed as part of our Pollution Incident Reduction Plan which covers a range of interventions, and for the first time we had no Wastewater Treatment Works classed by the Environment Agency as “failing works”, which is something that has only ever been achieved across the sector once before.

Greenhouse Gas Emissions and Climate Change

Carbon reduction (“mitigation”) and climate resilience (“adaptation”) have influenced both our strategic and operational decisions for over two decades. We have achieved substantial progress over recent years and we have ambitious plans and commitments to go much further.

Carbon reduction - We are signatories to the UN Race to Zero campaign and we are contributing to the UK water industry’s commitment to achieve carbon net-zero by 2030. In May 2020 we announced six carbon pledges including a new carbon emissions reduction target by adopting a science-based approach. We have successfully reduced our operational emissions by over 70 per cent in recent years, primarily by investing in our own renewable energy generation capabilities within the wider United Utilities group and purchasing green energy from the national grid. We continue to deliver on our commitments to peatland restoration and woodland creation, recently establishing two tree nurseries in the North West. We are also committed to delivering our green fleet strategy and have introduced more low carbon vehicles and charging.

Climate resilience - In AMP6 we invested an additional £250 million targeted to increase resilience against climate change, and we continue to invest across our business to protect and enhance the climate resilience of our assets, processes and customer services. We are working to further mature our already advanced level of climate risk understanding. We will soon be publishing an overview of our climate risks and plans in our new adaptation report. This will be released in draft for open consultation and engagement before we finalise our submission over the months ahead. Our latest annual statement in support of the recommendations of the Taskforce for Climate-related Financial Disclosures (TCFD) provides an update on our performance this year.

Natural Capital and Biodiversity

We continue to develop our approach to natural capital and improve our understanding of the full value of our activity to better inform investment decisions. We have a natural capital ODI in AMP7, which encourages assessment of the added natural capital value we deliver by pursuing nature based and catchment solutions. Understanding this value will help us drive partnership working and our Catchment Systems Thinking (CaST) approach which seeks to understand the broader needs of a catchment and deliver outcomes across multiple stakeholders. As part of this approach we have worked with stakeholders to develop a North West natural capital baseline to understand the natural assets the North West has, the benefits they provide and the value of them. Once completed, we will engage with other partners across the North West to drive a consistent approach in order to drive greater natural capital value. To facilitate this we are seeking to establish a North West governance group for natural capital.

Biodiversity is a key pillar of natural capital and plays an important part in our CaST approach. As the largest private land owner in the UK, and an organisation delivering significant development in the North West we have committed to no net loss on biodiversity and delivered significant investment in improving the condition of habitats on our land. We are actively reviewing our approach to how we can best manage and enhance biodiversity.

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Investors

Our investment strategy and digital transformation, underpinned by our pioneering Systems Thinking approach, is delivering significant performance improvement and efficiency. This has been our best year of operational performance for customers and the environment, manifesting itself in a net reward against our customer ODIs for the year of £21 million. Since accepting our AMP7 Final Determination, we have increased our totex plan by a further £300 million, all of which we expect to be remunerated through regulatory mechanisms, and we continue to accelerate our overall AMP7 investment programme to deliver benefits sooner and boost the regional economy as we emerge from the worst effects of COVID-19. We have delivered another year of robust financial performance and we are raising finance effectively, locking-in rates favourable to the price review assumptions and leveraging our strong ESG credentials.

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.

2020/21 reported RoRE was 4.5 per cent on a real, RPI/CPIH blended basis, mainly comprising 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), financing outperformance of 1.2 per cent and customer ODI outperformance of 0.3 per cent as a result of our year 1 net reward o.

Our totex performance of -0.3 per cent represents the year 1 impact of the £300 million additional totex which provides benefits that are not all reflected in RoRE.

Retail performance of -0.3 per cent reflects a small overspend this year in adapting to the effects of COVID-19 and tax performance of -0.5 per cent reflects the Government's reversal of the planned reduction in the rate of corporation tax from 19 per cent to 17 per cent from 1 April 2020 (which will be recovered through the tax sharing mechanism), and the tax impact of our strong financing outperformance.

Our underlying RoRE is higher at 4.8 per cent and is adjusted for the tax impact that will be recovered through the tax sharing mechanism and the additional totex that drives better outcomes against future customer ODIs.

Total expenditure (totex)

Our AMP7 business plan was assessed by Ofwat as being amongst the most efficient in the sector. Thanks to the strong performance we delivered in AMP6, we started AMP7 at the target totex run rate and we are confident that we can deliver our AMP7 scope within our Final Determination totex allowance. Our investment strategy delivers long-term sustainable performance improvements and efficiency and our AMP7 totex plans will be extended by around £300 million, which we expect to be be fully remunerated through regulatory mechanisms, with this investment extending our environmental programme, accelerating our digital transformation and exploiting spend to save opportunities.

In this first year of AMP7, we have invested £617 million in net regulatory capital expenditure (excluding infrastructure renewals expenditure (IRE)), representing the continued acceleration of our AMP7 investment programme and early expenditure against the £300 million extension to our original totex plans. This represents a good start to the delivery of our AMP7 programme, benefitting from the early start and transition investment we made in 2019/20 and our ability to continue working, where it was safe to do so, during the COVID-19 pandemic. As a consequence, 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.

While we continue to seek efficiencies in the delivery of totex, as we have demonstrated through the £300 million extension to our totex plans, we will invest where we are confident we can deliver improved customer or environmental outcomes and better customer ODI performance.

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Customer outcome delivery incentives (ODIs)

Our digital transformation and investment strategy are delivering improved performance and we have made a strong start to AMP7, achieving a £21 million net customer ODI rewards for 2020/21. This is ten times the net reward we achieved in the first year of AMP6 and is particularly pleasing in light of the tougher targets we have set.

The “Customer” section above provides more detail on the customer ODIs where we are performing well and others where the targets for AMP7 are challenging. We see opportunities across a number of ODI targets, and our Systems Thinking approach, including new digital capability driven by DNM, increased use of data and analytics within our retail function, coupled with early investment have and will continue to help us drive performance improvements.

Unlike AMP6, ODI rewards and penalties in AMP7 will be adjusted in revenues on a two-year lag, therefore any net reward earned this year will be reflected in an increase to revenues earned in 2022/23 through allowed increases in the rates charged to customers in that financial year, in accordance with the regulatory mechanism. Overall, we are targeting a cumulative net ODI reward over the 2020-25 period of around £150 million, a significant improvement on the £44 million achieved in the previous regulatory period.

Financing

On financing performance, 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 already locked-in for AMP7 compare favourably with the price review assumptions.

In November 2020, we published our new sustainable finance framework, allowing us to raise finance based on our strong ESG credentials and replacing the green funding that we have previously secured through the European Investment Bank (EIB), which is no longer available post-Brexit. In January 2021, we issued our debut sustainable bond generating a huge amount of interest for the company and our ESG credentials and delivering a coupon of 0.875 per cent. This is not only our lowest ever coupon at this maturity, locking-in financing outperformance, but also the lowest ever coupon for any UK corporate at this maturity.

ESG performance

We perform well across a broad range of ESG indices and for 2021 we attained World Class status on the Dow Jones Sustainability Index for the 14th consecutive year. In April 2021, we were ranked 6th out of 613 global utilities in the Sustainalytics’ ESG Risk Rating assessment, positioning us as the leading water utility in the index. We achieved a score of A- from the CDP which evaluates how companies assess climate change related financial risks and opportunities, including their approach to transparency and disclosure. We were assessed by the Environment Agency (EA) as the best performing company on pollution for the second year in a row with no serious pollution incidents and we expect to be awarded industry leading 4 star status in the EA’s Environmental Performance Assessment for 2020. From an employee perspective, we achieved a significant improvement in the Workforce Disclosure Initiative, scoring well above the overall average and receiving special recognition in the 'COVID-19 transparency' category at its Workforce Transparency Awards.

Suppliers

Our activities support around 17,700 jobs in the supply chain, and the acceleration of around £500 million of capital expenditure into the first three years of AMP7 will play a part in helping to generate jobs and income for the North West economy at a critical time as the country emerges from the worst effects of the COVID-19 pandemic. Suppliers play an important role in maintaining supply for key parts of our business, and contractors, as well as direct employees, act as the face of our business for many customers and communities. The pandemic has shown the importance of our relationship with our supply chain partners. We have continued to work

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closely with our supply chain and issued guidance reinforcing Government guidelines to protect employees, suppliers and customers while maintaining delivery of critical services.

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.

For 2020/21, in excess of 99 per cent of invoices were paid within 60 days, the average number of days taken to pay our suppliers was 13 days which is reflective of our efforts to accelerate payment to suppliers by 7 days during the COVID-19 pandemic and which was particularly welcomed by the small businesses we engage with. We act fairly and transparently with all our suppliers and are a signatory to the Prompt Payment Code, fully complying with the reporting requirements.

'Better together' through our United Supply Chain

In November 2020 we successfully launched our new approach to responsible supply chain management for AMP7 called United Supply Chain (USC). USC recognises suppliers as an extension of the United Utilities family and suppliers are asked to become a signatory to our Responsible Sourcing Principles as a minimum. Those suppliers who are integral to our operations we encourage to become leaders and to work jointly with us to deliver improvements across environmental, social and governance areas and improve value to customers. At the end of March 2021 we had signed 38 per cent of our targeted suppliers to our Responsible Sourcing Principles and continue to pursue the remaining suppliers to reach our target of 100 per cent. Via our partnership with Supply Chain Sustainability School we have been able to offer both our commercial colleagues and supply chain partners free resources to learn more about the Responsible Sourcing Principles.

Innovation in action

Our Innovation Lab programme is designed to "look for ideas where others aren't looking" – in other sectors, other countries and with suppliers that are often small, start-up businesses, just starting on their idea development or business growth journey. It does all this whilst being fully compliant with procurement legislation – allowing for rapid idea testing and idea adoption / contract award – an obstacle that most regulated companies struggle with. The open, collaborative nature means that feedback is given more frequently and ideas get tailored for United Utilities adoption faster than traditional product testing. We have worked with 23 suppliers in this way – and our highest profile success is FIDO (tackling leakage detection in our Lab 2 programme.) They are becoming known as a disruptor in the global water sector with United Utilities having first mover advantage on new developments.

We are part-way through our third Innovation Lab programme; we have published four high level problems and encouraged innovative solutions from around the world. Over 120 supplier applications have been reviewed by our experts and we have selected eight suppliers with high potential ideas; with our help, they could offer a performance step-change across a range of areas from helping us to reduce our carbon footprint and be more self-sufficient on energy, to predicting asset failures before they occur. All ideas support our Systems Thinking ambitions, most are digitally-centric, and half are new entrants to the UK water sector.

Financial performance

Financial KPIs

	Year ended 31 March 2021	Year ended 31 March 2020
Revenue	£1,797.6m	£1,849.9m
Operating profit	£601.7m	£626.8m
Profit before tax	£505.7m	£327.4m
RCV gearing	65%	67%
Interest cover	6.3	2.6

Revenue for the year to 31 March 2021 was down 2.8 per cent on last year, largely reflecting the typical customer bill reduction we have delivered for this first year of the new AMP7 regulatory period. Although COVID-19 changed patterns of demand for our services, changes in consumption between different customer groups have broadly offset each other in total. Household cash collection and our bad debt position have remained robust, and we have provided further financial assistance to customers who are struggling in this difficult time.

We continue to invest in our assets, bringing forward capital expenditure and seeing an increase in infrastructure renewals expenditure (IRE) in the period. Our financing performance remains strong and we have benefitted from lower short-term inflation reducing our net finance expense.

Our balance sheet remains one of the strongest in the sector, with a robust customer receivables position, an industry-leading, fully funded pension scheme on a low dependency basis, and RCV gearing supporting a stable A3 credit rating with Moody's.

Revenue

	£m
Year to 31 March 2020	1,849.9
Wholesale revenue forecast incentive mechanism (WRFIM*) adjustments	12.5
Regulatory revenue changes – 5.5 per cent real typical household bill reduction and 1.5 per cent uplift in line with CPIH inflation	(79.5)
Non-household consumption decrease	(46.7)
Household consumption increase	46.8
Innovation fund increase	6.2
Other	8.4
Year to 31 March 2021	**1,797.6**

* Annual regulatory adjustment for volume differences – Wholesale Revenue Forecasting Incentive Mechanism

Revenue was down £52 million, at £1,798 million, largely reflecting the £80 million reduction from the new pricing regime in this, the first year of AMP7, incorporating a 5.5 per cent real reduction in typical household bills and a 1.5 per cent CPIH-linked increase.

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The impact of the COVID-19 pandemic and related lockdown periods has seen non-household revenue decrease by £47 million, with an increase in household revenue of £47 million as a result of more time spent at home and the hot, dry weather in spring 2020.

Revenue in 2020/21 includes £6 million in relation to the Innovation in Water Challenge Scheme. This is a new scheme introduced by Ofwat in AMP7, and therefore did not apply last year, and is intended to fund industry-wide innovation projects. In 2020/21, we have provided for £6 million of offsetting costs with the balance of revenue and costs as the scheme matures in future years dependent upon how successful companies are in bidding for funds.

Operating profit

	£m
Year to 31 March 2020	626.8
Revenue decrease	(52.4)
Infrastructure Renewals Expenditure increase	(21.8)
Property rates increase	(13.6)
Innovation fund increase	(6.2)
Other operating costs increase	(5.1)
Depreciation and amortisation decrease	60.9
Allowance for expected credit losses – trade and other receivables decrease	13.1
Year to 31 March 2021	**601.7**

Operating profit at £602 million was £25 million lower than last year. This principally reflects the £52 million reduction in revenue, and also a £22 million increase in IRE as a result of ongoing work to optimise the performance of our network. Property rates are £14 million higher this year largely reflecting a rates refund received last year. We have accrued £6 million of costs in 2020/21 in relation to the Innovation in Water Challenge Scheme mentioned above, along with £13 million of extra COVID-19 related costs (including a £5 million increase in the bad debt charge). This is partly offset by depreciation being £61 million lower, principally reflecting £83 million of accelerated depreciation in the prior year relating to bioresources assets that were taken out of use and a £13m reduction in allowance for expected credit losses on trade and other receivables. In the near term we would expect depreciation to flatten out reflecting the lower AMP7 capex programme.

Household bad debt is 2.2 per cent of regulated revenue, representing a marginal increase of £5 million on the underlying bad debt cost in the prior year, reflecting the ongoing uncertainty associated with the third lockdown and taking into account expected cash collection into the future, as government support unwinds in the coming months.

Strategic report

Profit before tax

	£m
Year to 31 March 2020	327.4
Operating profit decrease	(25.1)
Net finance expense decrease	203.4
Year to 31 March 2021	**505.7**

Profit before tax was £506 million, £178 million higher than last year. This reflects the £203 million decrease in net finance expense (including fair value movements), partly offset by a £25 million reduction in operating profit.

- Net finance expense

Net finance expense of £96 million was £203 million lower than last year, principally reflecting a £150 million increase in the fair value gains on debt and derivative instruments, from a £76 million loss in the prior year to a £74 million gain in the current year, and lower inflation applied to our index-linked debt. The indexation of principal on index-linked debt amounted to a net charge in the income statement of £53 million, compared with a net charge of £101 million last year.

Profit after tax

	PAT £m
Year to 31 March 2020	135.9
Profit before tax increase	178.3
Underlying tax decrease	95.9
Year to 31 March 2021	**410.1**

Profit after tax of £410 million was £274 million higher than last year principally reflecting the £178 million increase in profit before tax and a £96 million lower underlying tax charge largely as a result of a £133 million deferred tax adjustment for the change in tax rate reflecting the Government's reversal of the planned reduction in the rate of corporation tax recognised in the prior year partially offset by the pension deficit repair payment we made last year.

- 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 we were delighted to have retained the Fair Tax Mark independent certification for a second year.

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 5,000 strong workforce. As in the prior year, the total payments for 2020/21 were circa £250 million and included business rates, employment taxes, environmental taxes and other regulatory service fees such as water abstraction charges as well as corporation tax.

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In 2020/21, we paid corporation tax of £73 million, which represents an effective cash tax rate on profits of 14.5 per cent. This is lower than the headline rate of corporation tax 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.

As well as the payments we also received a repayment of corporation tax of £27 million following agreement of routine prior years' UK tax matters.

The current tax charge was £78 million in 2020/21, compared with £43 million in the previous year. There were current tax credits of £nil in 2020/21 and £11 million in 2019/20, following agreement of prior years' UK tax matters.

For 2020/21, the group recognised a deferred tax charge of £17 million, compared with £149 million for 2019/20. Of the deferred tax charge for 2019/20, £133 million related to the Government's reversal of the planned reduction in the rate of corporation tax from 19 per cent to 17 per cent from 1 April 2020. Excluding the above change in tax rate related deferred tax adjustment in the prior year, the total effective tax rate was around 19 per cent for both the current year and the prior year. Subject to any legislative or tax practice changes, we would expect the total effective tax rate to be in line with the headline rate of corporation tax for the medium-term.

In 2020/21, there are £29 million of tax adjustments taken to equity, 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.

An increase in the headline rate of corporation tax to 25 per cent from 1 April 2023 was announced in the Chancellor's Budget on 3 March 2021. This change has been enacted in May 2021, and will result in a future deferred tax charge currently estimated at around £380 million.

Cash flow

Net cash generated from continuing operating activities for the year to 31 March 2021 was £941 million, marginally higher than the £822 million last year. The group's net capital expenditure was £638 million, principally in the regulated water and wastewater investment programmes. This excludes infrastructure renewals expenditure which is treated as an operating cost. Cash flow capex differs from regulatory capex, since the latter is based on capital work done in the period, rather than actual cash spent.

Pensions

As at 31 March 2021, the group had an IAS 19 net pension surplus of £531 million, compared with a net pension surplus of £579 million at 31 March 2020. This £48 million decrease is predominantly due to the unwinding of a spike in credit spreads at 31 March 2020 due to COVID-19 that resulted in a temporary decrease in the valuation of liabilities. 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 and is hedged for inflation and interest rates. Any inflation and credit spread movements are therefore not expected to have a material impact on the pension liabilities calculated on a scheme specific funding basis.

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

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Financing

Net debt	**£m**
At 31 March 2020	8,013.0
Cash generated from operations	(1,122.8)
Fair value movements	(7.5)
Net capital expenditure	638.1
Dividends	-
Interest	136.2
Indexation	52.6
Tax	45.7
Other	7.9
At 31 March 2021	**7,763.2**
Adjustments	**(98.4)**
At 31 March 2021 (new definition)	**7,664.8**

The group's gross borrowings at 31 March 2021 had a carrying value of £8,715 million. The fair value of these borrowings was £10,120 million. This £1,945 million difference principally reflects the significant fall in real interest rates compared with the rates at the time we raised a portion of the group's index-linked debt. This difference has increased from £470 million at 31 March 2020 due primarily to a decrease in credit spreads.

Cash and short-term deposits at 31 March 2021 amounted to £649 million.

Net debt at 31 March 2021 was £7,665 million, compared with £8,013 million at 31 March 2020. This comprises gross borrowings of £8,715 million and derivative liabilities of £115 million net of cash of £639 million and derivative assets of £425 million. This is then adjusted to exclude derivatives with a net liability of £98 million under our revised definition of net debt to exclude the impact of derivatives that are not hedging specific debt instruments and therefore gives a fairer reflection of the amount we are contractually obliged to repay. This approach is more consistent with that taken by the credit rating agencies and better reflects the regulatory economics.

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

Gearing, measured as group net debt divided by shadow (adjusted for actual spend) regulatory capital value, was 65 per cent at 31 March 2021, compared with 67 per cent as at 31 March 2020.

- Cost of debt

As at 31 March 2021, the group had approximately £3.0 billion of RPI-linked debt at an average real rate of 1.3 per cent, and £1.1 billion of CPI or CPIH-linked debt at an average real rate of (0.2) per cent.

The group has fixed the interest rates on its non index-linked debt in line with its 10-year reducing balance basis for the 2020-25 regulatory period.

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- 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) 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 €7 billion euro medium-term note (EMTN) programme. The EMTN programme does not represent a funding commitment, with funding dependent on the successful issue of the notes.

In total over 2020-25, we expect to raise around £2.4 billion to cover refinancing and incremental debt, supporting our five-year investment programme. In 2020/21 we have raised £900 million, taking advantage of the attractive rates available and extending our liquidity position out to August 2023.

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.

In January 2021, we issued our debut sustainable bond raising £300 million, maturing in October 2029 and subsequently swapped to CPI-linkage.

We remain one of the sector leaders in the issuance of CPI-linked debt in response to Ofwat's decision to transition away from RPI inflation linkage. At 31 March 2021, we have increased the CPI-linkage in our debt portfolio to £1,015 million with a further £50 million of CPIH-linkage, and therefore a perfect match for the regulatory regime.

Since 31 March 2020, we have renewed £50 million of revolving credit facilities with a relationship bank for a further five-year term, and extended £100 million of revolving credit facilities for a further three years, and £250 million of revolving credit facilities for a further year.

- 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 2021, approximately 39 per cent of the group's net debt was in RPI-linked form, representing around 26 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 9 per cent of UUW's RCV, with an average real rate of (0.2) 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. To manage exposure to medium-term interest rates, the group fixes underlying interest costs on nominal debt out to ten years on a reducing balance basis.

Historically, this has been supplemented by fixing substantially all remaining floating rate exposure across a forthcoming regulatory period around the time of the price control determination. Recognising Ofwat's intention to apply debt indexation for new debt raised during the 2020-25 regulatory period, we have retained the hedge to fix underlying interest costs on

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nominal debt out to ten years on a reducing balance basis, but have not supplemented this with the additional 'top up' fixing at the start of the new regulatory period.

- Liquidity

Short-term liquidity requirements are met from the group's normal operating cash flow and its short-term bank deposits and supported by committed but undrawn credit facilities. Our €7 billion EMTN programme provides further support.

At 31 March 2021, we had liquidity out to February 2023, comprising cash and short-terms deposits (enhanced by new finance raised in the period), 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.

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.

OUTLOOK

We have responded well to the challenges presented by COVID-19 and delivered another year of strong operational performance, building on the improvements we delivered in AMP6. We are leading the way on customer satisfaction and have made a strong start to our AMP7 customer ODIs delivering net outperformance of £21 million this year. We have extended our AMP7 totex plans by £300 million to underpin the delivery of long-term sustainable performance improvements and efficiency and we continue with our strategy of accelerating investment to bring forward benefits for customers and the environment and contributing the economic recovery of our region.

This is a great start to the new regulatory period and provides a strong platform to deliver further good operational performance for the benefit of all stakeholders. This gives us the confidence to target cumulative net outperformance of around £150 million against our customer ODIs for AMP7.

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Being a responsible business

Our ESG credentials

Through our purpose, vision and strategic themes, responsible business is a core part of who we are as a business and has been for many years.

We actively participate in a range of global ESG ratings, indices and frameworks to benchmark our approach against best practice and emerging sustainability challenges.

Index/rating	Description	Performance
Dow Jones Sustainability Index	The Dow Jones Sustainability Index ranks the sustainability approach of the top 10 per cent of the world's biggest companies based on long-term economic, environmental and social criteria.	**For 2020, our overall performance was 79 per cent and we attained World Class status for the 14th consecutive year. We were awarded SAM Bronze Class in the Sustainability Yearbook 2021.**
FTSE4Good Index	The FTSE4Good Index measures the performance of companies who demonstrate strong ESG practices against globally recognised responsible business standards.	**United Utilities Group PLC has been included in the FTSE4Good Index Series since 27 June 2001. Latest review June 2020.**
ISS	ISS ESG's Corporate ESG Rating provides investors with comprehensive portfolio company research on social, environmental and governance factors to help identify and mitigate ESG risks and to capitalise on investment opportunities	**In the annual review of November 2020 our status was assessed as Prime.**
MSCI ESG	Provides ESG ratings on an AAA to CCC scale according to exposure to industry specific ESG risks and ability to manage those risks relative to peers.	**As of February 2021, United Utilities Group PLC received an MSCI ESG rating of AA.**
Sustainalytics	Sustainalytics, a Morningstar company, is a leading independent ESG research, ratings and data firm. Its ESG Risk Ratings measure a company's exposure to industry-specific material ESG risks and how well a company is managing those risks.	**In April 2021, United Utilities received an ESG Risk Rating of 13.0 and was assessed by Sustainalytics to be at low risk of experiencing material financial impacts from ESG factors. United Utilities is a Sustainalytics ESG Industry Top Rated Company for 2021.**
Vigeo Eiris	Vigeo Eiris (V.E), an affiliate of Moody's, is a global leader in ESG assessments, data, research, benchmarks and analytics. Leveraging their extensive proprietary database, they equip market players with the ESG insight they need to manage risks and better understand and address their social and environmental impact. The Euronext ESG indices serve as a benchmark for investors to incorporate ESG considerations into their investment strategies.	**We received an overall Advanced ESG score by V.E of 65 and United Utilities Group PLC has been confirmed as a constituent of the Euronext UK 20 and Europe 120 Indices in year 2020**

Alignment to wider global goals

The Sustainable Development Goals (SDGs) comprises 17 global goals to be achieved by the year 2030, and were adopted by a summit of the United Nations (UN) in 2015. They are designed to be the blueprint to achieve a better and more sustainable future for all. Our approach to responsible business aligns quite naturally with the goals and we have identified six that are most material to our business and where we contribute the most.

We contribute to the delivery of a wider selection of the SDGs through our investment projects and these are described in our sustainable finance framework.

Clean water and sanitation – Part of our purpose is to provide great water and is the reason we exist, ensuring customers in the North West have safe, resilient and affordable water and wastewater services.

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This includes avoiding wasting water, and we promote water efficiency through campaigns, advice, education and free water saving gadgets for customers.

We protect and enhance water-related ecosystems across our region through initiatives such as our Catchment Systems Thinking approach.

Decent work and economic growth – Our daily operations provide direct, indirect and induced employment for 22,700 people, and we are a big contributor to the North West economy.

We provide training and development opportunities in safe, secure working environments, graduate and apprentice opportunities, programmes for young people experiencing difficulties securing employment, offer equal opportunities to all and value diversity among our employees.

Industry, innovation and infrastructure – We invest heavily in infrastructure, including plans for over £4 billion between 2020 and 2025 to improve the performance and resilience of our assets and operations to impacts such as those arising from climate change.

We embrace innovation, especially in an increasingly digital world, to ensure the region where we operate has reliable, sustainable and resilient infrastructure, now and into the future.

Sustainable cities and communities – We use our understanding of customer needs and priorities to deliver services that meet their expectations and engage with communities to enhance participation in what we do. We plan at least 25 years into the future to prepare for increases in the population and new housing that will need connections for water and wastewater services. We are exploring ways to do this using natural solutions to manage water and wastewater, such as Sustainable Drainage Systems (SuDS).

Climate action – Responding to the climate emergency is an imperative for us all.

Reducing our greenhouse gas emissions, delivering against our six carbon pledges and ensuring that we, and the region we serve, are resilient to the impacts that a changing climate might bring, are key to our long-term planning.

Peace, justice and strong institutions – We run our business in a responsible manner, and being trustworthy is one of our core values.

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

Our approach to climate change

Task Force on Climate-related Financial Disclosures

Overview

Weather is fundamental to how we deliver water and wastewater services so climate change has been, and always will be, of strategic and operational importance.

With advances in climate science, our understanding of climate change and how we respond is ever evolving, as is the external policy environment in which we operate.

Incorporating climate into long-term planning

Building on our long-standing approach to climate change mitigation and adaptation, we now integrate consideration of climate- related risks and opportunities directly into our business planning to influence strategy and behaviours throughout the organisation.

This year, we've enhanced our understanding of the sensitivity of our business risks to climate change and applied Systems Thinking to embed physical and transitional risks into both operational planning and long-term strategy development.

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We now have a good understanding of the controls required to adapt to a changing climate, and are building our confidence to recognise and manage cascade impacts where multiple weather events in a short time frame can have a cumulative impact.

Scenario analysis

To support strategic planning, we developed three comprehensive scenarios exploring how multiple drivers of change might evolve and interact over time, compared to a baseline scenario. Each one is aligned to a specific emissions pathway, enabling us to test out scenarios where there is: an effective transition to a low carbon world; a climate crisis due to suboptimal climate change mitigation efforts; and a central case where more moderate impacts of climate change are experienced after slow initial progress is followed by a step change in de-carbonisation.

Pledges and commitments

We have made good progress on our six carbon pledges (see page 74), which include science-based emission reduction targets and four specific pledges on how those reductions will be achieved.

Pledge 1 is to reduce our scope 1 and 2 emissions by 42 per cent by 2030. We are on track to achieve this pledge although progress will not be linear year-on-year while we work to reverse the pressures that are driving growth in emissions.

Pledge 2 Over 94 per cent of the electricity we used in 2020/21 came from renewable technologies. From October 2021, we will meet our pledge for 100 per cent.

Pledge 3 commits us to 100 per cent green fleet by 2028. We have deployed 27 electric vehicles at operational sites, and are trialling a 44-tonne biogas-powered HGV.

Pledge 4 commits us to 1,000 hectares of peatland restoration by 2030. We have proposed five sites for green recovery catchment peatland restoration.

Pledge 5 commits us to 550 hectares of woodland creation by 2030. We have planted 9,783 woodland carbon code compliant trees, established two tree nurseries and identified hundreds of potential sites for new and 'replanted' woodlands.

Pledge 6 commits us to set a science- based target for our scope 3 emissions, which we have done (see page 74).

An important element of our approach is to encourage others to contribute by making public commitments. We joined the global movement of 'Business Ambition for 1.5°C: Our Only Future', with a commitment to setting science-based targets aligned with limiting global temperature rise to 1.5°C above pre-industrial levels. We are signatories to the UN Race to Zero campaign and we are proud to be contributing to the UK water industry's commitment to be net zero from 2030.

Achievements

- On track to deliver our climate change mitigation pledges and our public commitments.
- Science-based targets covering all emission scopes set and submitted for validation by the Science Based Target initiative (SBTi).
- Three 'alternative' scenarios, each one aligned to a specific emissions pathway, developed and used to support strategic planning.
- Impact of climate change now specifically considered as part of corporate risk framework.

Successes

- CDP is a global disclosure system for environmental reporting. Our CDP climate change rating improved from B to A- in 2020, demonstrating leadership-level reporting and

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disclosure. We are one of only two companies in the UK water sector achieving leadership level.

- The Sustainability Reporting Performance report by EcoAct measures how businesses are acting and reporting on climate- related sustainability. We have been ranked in the top 20 FTSE 100 list, improving from 17th to 11th position in 2020, and are the highest ranking water company.

Transparency and disclosure

We have published carbon and climate change disclosures in our annual report and CDP's Climate Change Programme assessment for over a decade. We report in adherence with the Greenhouse Gas Protocol Corporate Accounting and Reporting Standards (2015) and the 2019 UK Governmental Environmental Reporting guidelines.

We have signed the Statement of Support for the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) which was published in June 2017, and we report in line with its recommendations across its four thematic areas.

Corporate Citizenship Review

Corporate Citizenship, a leading sustainability consultancy, reviewed this disclosure and provides an ISAE assurance against the Principles of Effective Disclosure to ensure that it accords with Task Force on Climate-related Financial Disclosures recommendations.

Read more at fsb-tcfd.org/ recommendations

TCFD recommendations

This table shows progress this year towards meeting the TCFD recommendations and the areas we will focus on in the future. The table includes cross-references where there is more material within this annual report and financial statements.

Governance	**The organisation's governance around climate-related risks and opportunities**	
Progress this year	Future focus	Further information
▪ Implemented enhancements required to reach overall 'leadership level' in the 2020 CDP assessment. ▪ Included special report on climate-related risks in board-level risk review. ▪ Created long-term strategy team with primary focus on climate change adaptation and mitigation.	▪ Further inclusion of climate-related risks and opportunities into all investment decisions, processes and governance. ▪ Continue to demonstrate leadership in climate-related disclosure, for example CDP assessment.	Our **corporate responsibility committee report** on pages 156 to 159 of the UUG 2021 Annual report and financial statements provides a summary of committee discussions on climate change. A summary of the **board and its management committees** can be found on page 120 of the UUG Annual report and financial statements.
Risk management	The process used by the organisation to identify, assess and manage climate-related risks	
Progress this year	Future focus	Further information
▪ Enhanced analysis of risks arising from the climate change we are already experiencing and the extent to which that might affect operations. ▪ Completed a robust review to identify which corporate risks are vulnerable to climate change and quantified the impact and time sensitivity.	▪ Further fomalisation of climate-related physical and transitional risks into risk management systems. ▪ Embed identification of climate-related risk and opportunities throughout the organisation as business as usual.	Read more **about the process for identifying, assessing and managing climate risks** on page 66.. Read more about **our risk management framework** on page

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		83.
Strategy	The actual and potential impacts of climate-related risks and opportunities of the organisation's businesses, strategy and financial planning.	
Progress this year	Future focus	Further information
Metrics and targets	The metrics and targets used to assess and manage relevant climate-related risks and opportunities	
Progress this year	Future focus	Further information
▪ Completed comprehensive review of all scope 3 emissions and set ambitious science-based targets (currently being validated by SBTi). ▪ Achieved A- rating in 2020 CDP assessment of targets and emission-reduction initiatives. ▪ Updated drought plan triggers to minimize the impact on customers and improve our resilience to periods of prolonged dry weather.	▪ Secure SBTi validation for science-based targets for all three emission scopes. ▪ Implement data improvements for scope 3 emissions so more are supplier and product-based factors rather than spend based. ▪ Analysis to understand cascade impacts and our resilience to them where multiple extreme weather events can occur in a single short time frame.	Read more about **metrics used to assess climate impacts to our key risks** on page 73. Read more about **setting our science-based targets** on page 74. Read our **energy and GHG emissions report** on pages 77 to 83.

Governance

Chief Executive Officer Steve Mogford has ultimate responsibility for the group's preparedness for both adapting to climate change and driving our mitigation strategy. As climate change is a significant causal factor for the group's principal risks (see page page 103 of UUG Annual report and financial statements), the executive team is tasked with managing the risks and mitigating actions, for example by ensuring the company has the necessary financial resources and people with the required skills to achieve its climate- related objectives.

Chief Financial Officer 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.

The group audit and risk board (GARB) reviews the effectiveness and performance of the governance processes along with the identification of emerging trends, including climate change. The work of the GARB feeds into the information and assurance processes of the audit committee and into the board's assessment of risk exposures and strategies to manage these risks.

There is further board oversight of climate- related issues through the corporate responsibility committee (see pages 156 to 159 of the UUG Annual report and financial statements). Mitigation and adaptation are priority topics for the committee, which plays an important role in challenging and encouraging consideration of climate- related issues. It initiated the review of the company's carbon strategy and endorsed the mitigation policy, defining our corporate ambition and objectives. This led to the development of our mitigation strategy and the establishment of an executive-level steering group. This group has delegated responsibility to embed climate-related issues throughout business planning, to bring consistent focus to the delivery of our climate-related commitments, such as the six carbon pledges, and to provide updates to the board and corporate responsibility committee.

Risk Management

We have a strong track record of risk management and of climate change disclosure. We continually mature our capacity and capability to manage risk and uncertainty to build and maintain long-term resilience across the corporate, financial and operational structures of the group.

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Our company risk management framework follows an enterprise-wide approach and covers all principal risk areas such as water service, supply chain and programme delivery.

Climate-related risks are identified, assessed and managed in the same way as any other risk through our embedded risk management framework which is described on pages 83 to 87. Having been identified, each business risk is assessed in two ways. First, we consider the likelihood of the event occurring based on multiple causal factors; secondly, we examine the full range of potential impacts and their severity should the event occur, from a minimum (best case) to a maximum (worst case) scenario.

We take a variety of approaches to identify and assess risks, including using risk breakdown structures and tools such as PESTLE to formalise horizon scanning, as well as complex modelling of the physical impacts of climate change on our water resources and wastewater management.

Horizon scanning such as tracking legal and regulatory changes, emerging technologies and comparison of our strategies with other companies is particularly useful when considering transitional risks. We have found risk breakdown structures and detailed modelling are better suited to acute or chronic physical risks.

Risks sensitive to climate change

Climate change has been identified as a critical cross-cutting driver, so all our 100 event-based risks in our business risk profile were reviewed for their exposure to climate change. Last year we identified seven risks most sensitive to climate change in that their likelihood or the impact will increase with global warming. We have further analysed these risks and now have a good understanding of the controls required to adapt to a changing climate. This is set out on pages 68 to 73. This exercise highlighted a further risk in the potential for cascade impacts where multiple weather events in a relatively short time span can have a more challenging impact.

Looking ahead, we will explore how innovation can help us learn more about the profile of risk events, their causes and consequences and the capacity and capability of our company to manage them. By understanding this, we have the opportunity to be proactive and better prepared by prioritising issues.

By incorporating longer-term climate change impacts more explicitly in our corporate risk framework, we have raised the profile of climate change adaptation, providing the board enhanced insight to consider our risk appetite and capacity from within existing risk management processes and with the same thresholds for materiality.

We have identified where climate risks are not well enough understood or where existing controls might be inadequate to manage the risk in the long term.

Strategy

Planning horizons

Our planning horizons are illustrated on pages 40 to 43. Climate-related risks are manifesting themselves in the short to medium term and in common with the rest of the water industry, we are also vulnerable to physical climate risks in the long term (ten to 25 years and beyond) as our assets typically have long, even very long, lifespans. Many of our services are based on legacy infrastructure which was designed decades ago to deliver water and wastewater services for the climate we had rather than the one that is ahead of us.

Already seeing climate change in the North West

Five of the top ten wettest years for the North West since 1880 have occurred since 2000, and all of the ten hottest years have occurred since 2002. A top ten coldest year has not been recorded since 1963. These trends, and their impact on local weather conditions, are impacting our climate sensitive risks already.

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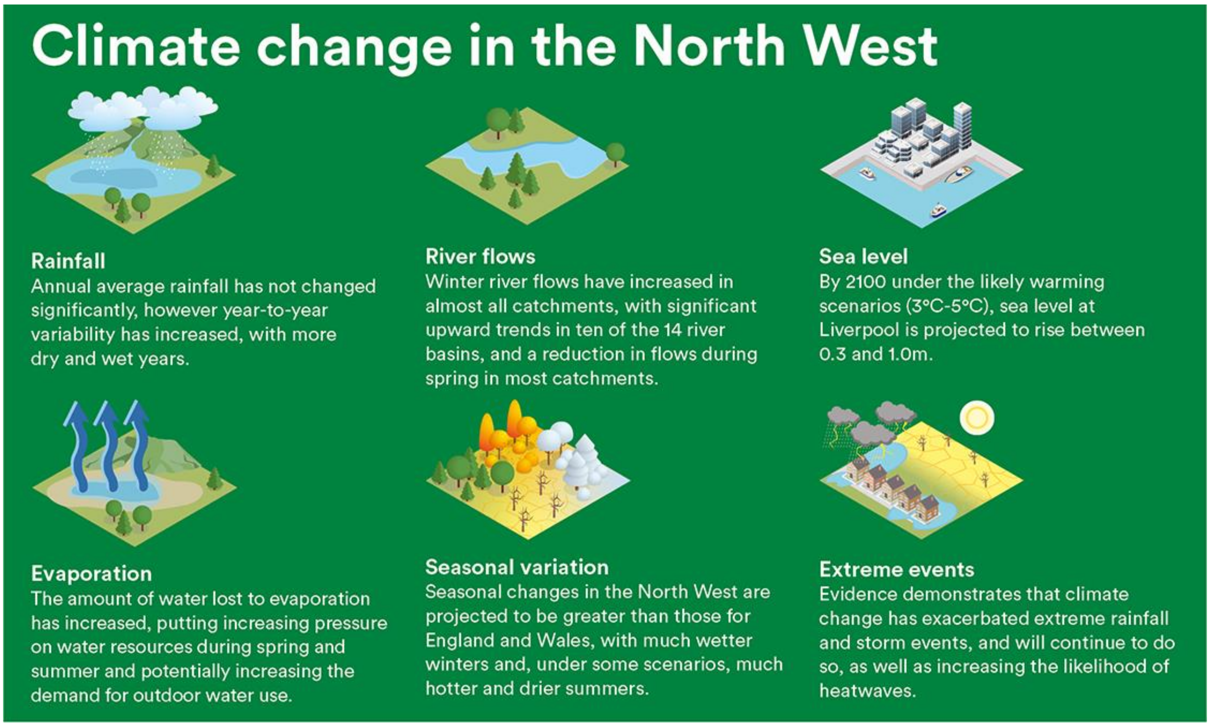
For example, changes in precipitation and temperature have contributed to changing patterns of river flow in our water supply catchments. There has been an increase in winter flows in almost all catchments, with significant upward trends in ten of the 14 river basins, and a reduction in flows in most catchments in spring, most notably for the strategic Vyrnwy catchment where there has been a significant downward trend over the last 20 years.

Annual average rainfall has not changed significantly, although the year-to-year variability has increased (with more dry and wet years) and some research shows an increase in the probability of heavier rainfall events. The greatest change in seasonal rainfall trends is an increase in winter rainfall, due to an intensification of heavy rainfall events, which leaves us increasingly susceptible to a range of key risks, including sewer flooding, asset flooding and land quality deterioration.

Annual and monthly temperatures in the North West are already higher than those experienced before 1900, largely due to anthropogenic activity, with the rate of warming accelerating.

Application of temperature-based estimates show an increase in potential evapo-transpiration in our region. This may influence the water balance, particularly in spring and summer, leading to a sensitivity to drought, and potentially water network failure and water sufficiency events.



Physical risks

All seven of the risks identified as being sensitive to climate change are physical risks, so we set about quantifying that vulnerability.

Predicting the effects of climate change is complex, with a large amount of uncertainty involved. Focusing on the predominant downsides, we assessed the potential implications for the seven risks in 2050 and 2100 compared to today, using the latest climate research, the Met Office UK Climate Projections 2018 (UKCP18). This has four pathways to 2100 depending on concentrations of greenhouse gases in the atmosphere and we have used what is widely accepted as the most likely pathway, RCP 6.0, which is consistent with peak emissions occurring in 2080. Best and worst case scenarios will be considered in due course.

The outcomes of the risk assessment were the topic of a special report prepared for a board-level risk review which took place in April 2021. They are presented on pages 69 to 73, together with a summary of assumptions, climate sensitivity and existing controls. In each case the

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downside effect is quite significant relative to the baseline, and four risks in particular stand out as having the most significant increases in likelihood: water sufficiency event; water network failure; recycling of biosolids to agriculture; and risk of inadequate land management.

Transitional risks

We are also vulnerable to risks associated with the transition to a low-carbon economy. Changing policies, regulation and legislation to address mitigation and adaptation requirements can increase operating costs due to, for example, enhanced emissions reporting.

Environmental requirements to meet water quality standards can lead to increased fuel or chemical consumption and legislation such as the Industrial Emissions Directive will result in operational and strategic planning interventions.

One likely consequence of changing legislation is potential asset redundancy, where the case to move to lower carbon technologies might result in the consolidation of assets on a fewer number of sites.

Opportunities

We are a relatively energy-intensive business, typically using around 800 GWh of electricity each year. As well as the risks associated with this dependency we see opportunities in the way we manage energy and have developed an approach to use less, generate more and use our assets and resources smarter while maintaining security of supply.

We have already invested in innovation and research to minimise the total amount of energy we consume, for instance in pioneering UV LED water treatment. We have increased renewable generation through bioresources, solar and wind, increasing the amount of self-generated energy from 108 GWh in 2012/13 to 205 GWh in 2020/21.

We aim to develop more successful innovation projects and that by meeting more of our own energy demands we can rely less on imports from the grid and mitigate the risks of future energy price fluctuations and uncertainty, as well as bolstering our own security of supply.

Resilience of our organisation to a changing climate

The main climate-related risks to the resilience of our operational assets are uncertainty of the health of ageing infrastructure and the increasing challenges presented by predictions for climate change and population growth over the long term.

Our Water Resources Management Plan 2019 is an example of how our strategy, to achieve a long-term, best value and sustainable plan for water supplies in the North West, has been developed to ensure that we have an adequate supply to meet demand over the 25 years from 2020 to 2045. This will ensure that our supply system is resilient to drought and other hazards, including climate change (using 'stochastic weather' and scenarios from the latest UK climate projections, UKCP18) and demand (population growth, economic trends and patterns of water use).

Climate sensitive risks overview

Below is the outcome of a special risk assessment on the risks identified as sensitive to climate change.

Likelihood and impact are as predicted at 2050 and 2100 using the accepted most likely emission pathway RCP6.0.

Water sufficiency event

When temperatures rise, higher water usage, evapo-transpiration and lower average summer rainfall from associated dry periods, causes supply pressures. The most likely impact assumes weather patterns similar to 2018 happening twice in five years at 2050, and four times in five years by 2100.

		Likelihood (%)	Impact (NPV £m)
Baseline		10%	£66m
2050		40%	£265m
2100		80%	£530m

Controls

- Development of new sources of water, particularly boreholes.
- Water trading between different regions of the UK. Leakage reduction.
- Encourage and inform customers about using less water.
- Installation of more meters on domestic properties.

Failure of wastewater network (sewer flooding)

Increased rainfall (storm) events can result in severe sewer flooding. The frequency of such events is forecast to almost double with climate change. For a storm with a return period of one in 50 years or greater, 15 per cent of our region is currently at risk of internal flooding. By 2050 it is expected 20 per cent of our region would be impacted, rising to 29 per cent by 2100. The cost of an internal flooding incident is assumed to stay constant.

	Likelihood (%)	Impact (NPV £m)
Baseline	40%	£210m
2050	53%	£278m
2100	77%	£404m

Controls

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

Land management

Deterioration in the quality of land due to climate change will increase the frequency and impact of weather events on our owned land. Such events have led to more fire, flood, subsidence and landslip events which in turn have associated impacts on: health, safety and environmental issues; access to operational and capital activities; corporate reputation; missed opportunities; legal liability and additional unplanned spend associated with invasive species.

	Likelihood (%)	Impact (NPV £m)
Baseline	20%	£31m
2050	50%	£76m

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2100	100%	£153m

Controls

- Proactive land management action to protect quality, including through
- nature-based solutions.
- Provide net gain in biodiversity from our construction projects. Directly restore peatland and woodland.
- Work in partnership with farmers, the Environment Agency and others to improve upland watercourses.

Failure to adequately treat wastewater

Extreme rainfall events cause overflows and variation between high rainfall and drought periods causes further susceptibility. Likelihood of failure to adequately treat wastewater is expected to remain at one in two years but the most likely impact expects six more failing works (above 2020 baseline) and uses the current ODI penalties as the impact magnitude.

	Likelihood (%)	Impact (NPV £m)
Baseline	50%	£75m
2050	50%	£95m
2100	50%	£114m

Controls

- Enhancements linked to no deterioration funded through price review.
- DWMP investigations into increased dilution.
- Infrastructure investment to increase resilience to extreme events.

Failure of above-ground water and wastewater assets (flooding)

Average winter rainfall is projected to increase by 6 per cent by 2050, and by 12 per cent by 2100, increasing the likelihood of extreme events where sites are flooded from sea, river or surface water sources.

The impact is estimated based on three modelled events (of likelihood 1:1000, 1:100 and 1:30) each having a 10 per cent annual increase in frequency every 20 years.

	Likelihood (%)	Impact (NPV £m)
Baseline	8%	£45m
2050	12%	£117m
2100	15%	£142m

Controls

- Install permanent flood defences at most flood-prone sites.
- Improve flood forecasting capabilities.

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- Build better network connectivity so that supplies can be maintained from elsewhere if a treatment works is flooded.
- Invest to ensure sites can bounce back quickly once flooding subsides.

Water network failure

Warmer, milder winters will decrease the likelihood of cold snaps/freeze thaws that result in burst pipes. However, these milder winters will result in more precipitation and flood events, causing a risk to assets close to, or crossing, rivers. Increased summer temperatures may result in considerably more heatwaves, which cause a higher peak demand. Such events can result in low pressure and no water for some customers.

	Likelihood (%)	Impact (NPV £m)
Baseline	13%	£2.1m
2050	24%	£28m
2100	32%	£41m

Controls

- Already increased the size of our fleet of alternative supply vehicles
- (ASVs), and introduced a new 24/7 logistics capability.
- New Network Maintenance Services contracts with key third-party suppliers include elements to ensure all can respond effectively in an incident when required.
- Leakage reduction.
- Encourage and inform customers about using less water. Installation of more meters in domestic properties.

Recycling biosolids to agriculture

Climate change is expected to increase persistent rainfall. The resultant water logging will limit spreading biosolids to land for a greater part of the year and uncovered sludge stores and stockpiles will be more vulnerable in persistent wet, winter weather.

The impact calculation assumes the sludge that cannot be spread to land will be sent to restoration and the impact is the associated ODI and EA fines.

	Likelihood (%)	Impact (NPV £m)
Baseline	20%	£2.3m
2050	37%	£12m
2100	52%	£27m

Controls

- Increased sludge storage capability.
- Utilise covered storage.
- Increased distance travelled for disposal of sludge.

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Our WRMP proposals include enhanced demand management activities to offset upward pressures on water suppliers and will enable us to reduce the frequency of needing drought permits to augment supply by 2025.

As well as targeted scenario analysis, 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', are plausible narratives, with associated metrics, of a 2050 future for water and wastewater services in the North West.

The scenarios recognise climate change as one of the most critical uncertainties and use RCPs 2.6, 4.5 and 8.5 (GHG concentration pathways adopted by the IPCC) to describe how well climate change has been mitigated in each case.

The 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.

Climate change mitigation strategy

Before agreeing our strategy, we developed a matrix to assess and compare our mitigation capabilities with other water companies and brands, to explore principles, priorities and define our objectives. The matrix began with the premise that great carbon management is more than just a number and that our strategy should cover four themes: vision and visibility; ambition and commitment; demonstrating action; and beyond here and now. See figure on page 76.

We already have a strong track record of sustainability reporting and disclosure, having reported our GHG emissions for nearly 20 years. Through this TCFD section, and improvements in our CDP response, we want our carbon reporting to be open and transparent and recognised as among the best in the UK.

Other aspects of our climate mitigation strategy can be summarised as:

- integrating carbon into strategic and day-to-day business planning;
- improving our carbon reporting and climate-related disclosure;
- setting ambitious and comprehensive commitments and greenhouse gas emissions targets to contribute to limiting global temperature rise;
- reducing emissions across water and wastewater processes, sludge process and disposal, fleet management, fuel use, land use, and waste and resources; and
- collaborating to drive innovation and challenge standards to deliver a low- carbon future.

Playing our part

Pages 63 to 66 and 94 to 95 of the UUG Annual report and financial statements illustrate and describe how there are climate-related risks and opportunities throughout our organisation. Our approach to managing those risks, and taking advantage of the opportunities, involves all our stakeholders across our value chain

Metrics and targets

Metrics to assess climate risks

The metrics which determine the magnitude of our climate risks and opportunities relate mainly to the weather, for instance measures such as temperature and rainfall by season.

To manage our climate risks effectively we must track and understand patterns of weather, and weather events, and learn how they can affect us operationally, so we can put into place appropriate controls such as those in the risk tables on pages 69 to 73.

We monitor several measures that can affect transitional risks. These include energy pricing (electricity, natural gas, diesel and alternative fuels, such as compressed natural gas and

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hydrotreated vegetable oil) and carbon pricing through purchasable credits, offsets and certificates (such as REGOs not bundled with electricity). We monitor the marketplace for the availability and pricing of alternative fuelled vehicles, battery storage and for emerging technologies to reduce process and fugitive emissions.

Operational metrics and targets

We have key metrics that assess the effectiveness of the controls for our principal risks and therefore determine our capability to adapt to a changing climate and ensure the resilience of our service. For these operational metrics we have set ambitious targets. For instance, to give us headroom in our water supply demand balance we have set short and long-term targets for leakage and per capita consumption (how much customers use) to reduce the demand for water in all climate scenarios. Recognising the need to maintain service to customers, even in extreme weather events, we have also set targets for supply interruptions, sewer flooding and pollution incidents.

Metric	2020	2025	2045
Per capita consumption	140	135	115
Leakage	-	15% reduction	40% reduction
Network interruptions	-	50% reduction	
Sewer flooding	-	20% reduction	70% reduction
Pollution incidents	-	37% reduction	64% reduction

Climate commitments and targets

We have made several climate-related public commitments, on our own and with other organisations. Having exceeded the emissions targets we set in 2015, last year we made six pledges to reduce our carbon footprint. Central to these is to set and meet science-based targets for all emission scopes (see figure of greenhouse gas emissions by scope on pages 78 to 80) and we have joined the global movement of 'Business Ambition for 1.5˚C: Our Only Future' and the UN Race to Zero campaign.

Science-based targets

Science-based emission reduction targets are set in line with what climate science says is enough to limit global temperature rise to well below 2°C or 1.5°C above pre-industrial levels. This requires emissions to halve from 2010 levels by 2030 and to hit net zero by 2050.

The Science Based Target initiative (SBTi) defines and promotes global best practice in science-based target setting. We have applied the 'SBTi Criteria and Recommendations' guidance to our policies and greenhouse gas accounting standards and have applied for our targets to be validated.

Pledge 1 is to meet our science-based target to reduce scope 1 and 2 emissions by 42 per cent by 2030 (from the 2019/20 baseline). This ambition is based on the Paris Agreement's highest level of ambition, to limit global temperature rise to 1.5°C above pre-industrial levels. We have a longer-term science-based target for a 100 per cent reduction from the 2019/20 baseline (net zero without purchased offsets) by 2050.

Pledge 6 committed us to set a science- based target for scope 3 emissions and we describe how this was achieved on page 96 of the UUG Annual Report and financial statements.

Net Zero 2030 Routemap: Unlocking a net zero future

In November 2020 the UK water sector launched the 'Net Zero 2030 Routemap: Unlocking a net zero future', understood to be the world's first sector-wide plan for net zero. We have committed to contributing by stating our ambition that our water emissions (scope 1, 2 and a small selection

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of scope 3) will be net zero from 2030.This routemap allows companies to offset residual emissions (using agreed offsetting principles) whereas science-based targets require absolute emission reductions. This explains the difference between our science-based target to achieve a 42 per cent reduction by 2030 and being net zero from 2030 in line with the water industry ambitions.

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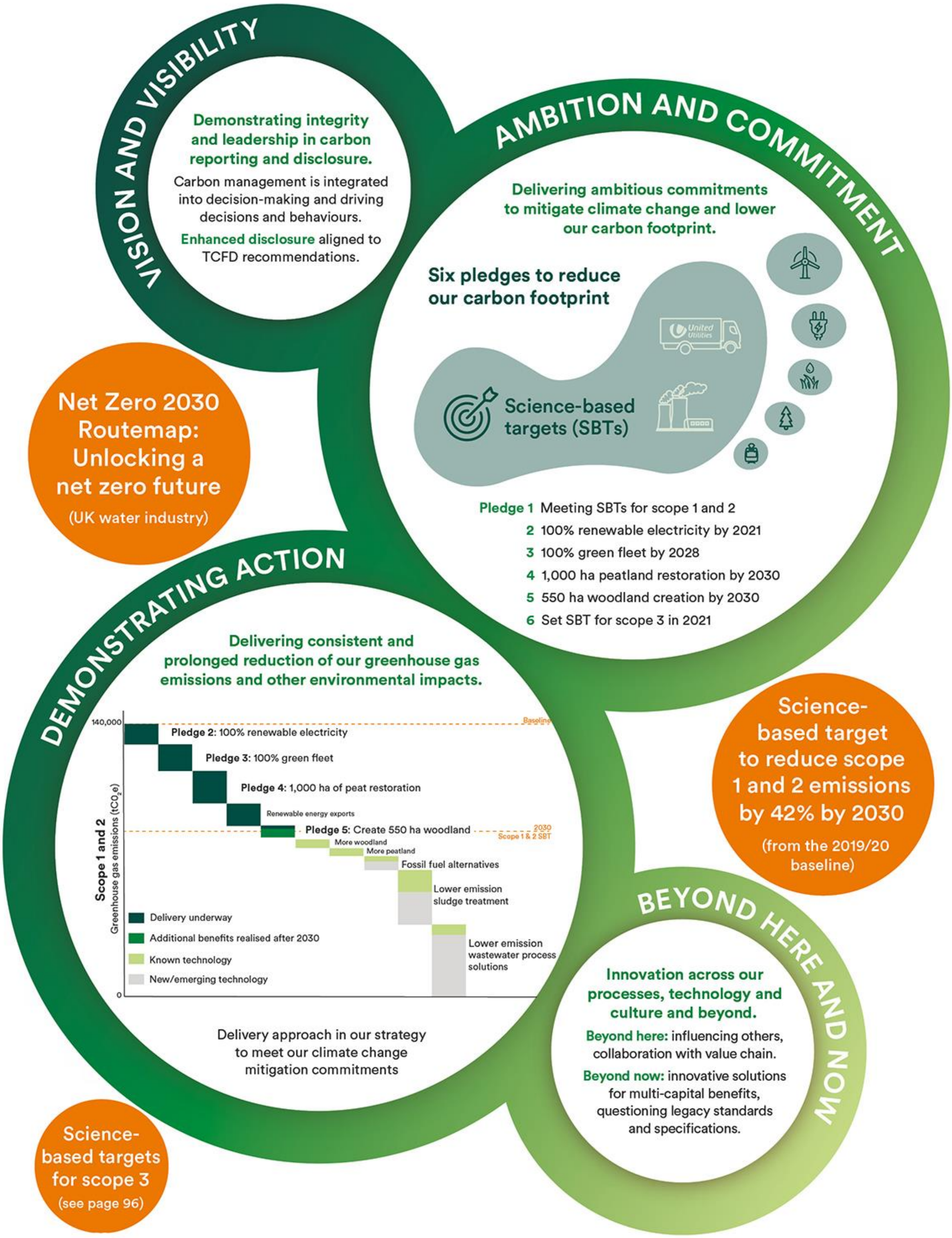
Our approach to climate change mitigation

A collaborative strategy for a low carbon future: embedding carbon commitments across our processes, technology, culture and beyond.



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Energy and carbon report

Reporting and assurance

We measure and report the greenhouse gases that result from all United Utilities' activities. We have used the financial control approach so our energy and greenhouse gas emissions reports are aligned with the consolidated financial statements for United Utilities Group PLC. This includes its subsidiaries listed in the UUG Annual report and financial statements section A8 on page 260.

Our measurement and reporting is aligned to the GHG Protocol Corporate Accounting and Reporting Standard (2015) and the recommendations of the TCFD. As required, we report under the Companies Act 2006 (Strategic Report and Directors' Reports) Regulations and we apply the 2019 UK Government Environmental Reporting Guidelines, including the Streamlined Energy and Carbon Reporting Guidance (SECR). Our reporting is compliant with the international carbon reporting standard (ISO 14064, Part 1) and assured by the Carbon Reduce programme previously known as Certified Emissions Measurement and Reduction Scheme (CEMARS). We hold a Platinum status certificate as we have demonstrated emission reductions over ten years.

How we measure our greenhouse gas emissions

A carbon footprint is calculated by converting all emissions of Kyoto Protocol gases into a carbon dioxide equivalent (tCO_2e). Emissions are categorised as direct, indirect or avoided emissions.

Direct emissions (scope 1 emissions) are those from activities we own or control, including those from our treatment processes, company vehicles, and burning of fossil fuels for heating.

Indirect emissions, known as scope 2 and 3 emissions, result from operational activities we do not own or control. These include emissions produced as a consequence of electricity we purchase to power our treatment plants (scope 2) and other indirect emissions such as products and services we buy and travel on company business (scope 3).

Avoided emissions are reductions from the purchase, or export, of renewable energy. Gross emissions are the sum of all three scopes. Net emissions are the gross emissions minus reductions from avoided emissions and removals.

The GHG Protocol recommends using two methods to quantify emissions - the 'location-based' method which uses average grid electricity emissions factors and the 'market-based' method which is specific to the actual electricity purchased. Following the GHG protocol recommendation we report results using both methods and use the 'market-based' figures to report our headline emissions.

Greenhouse gas emissions and energy performance in 2020/21

Our investment in renewable energy generation has resulted this year in a further increase to 205.3 GWh, equivalent to a quarter of the electricity we consumed.

Our net scope 1 and 2 greenhouse gas emissions for 2020/21 were 127,173 tCO_2e, 1.5 per cent more than last year. This is due to an increase in fossil fuel use, the volume of wastewater being processed and the subsequent amount of wastewater sludge being produced.

Our scope 3 emissions, covering our new comprehensive inventory, have increased by 4 per cent, due to increased spend in the value chain on goods and services. In the coming years we plan to reduce the reliance on spend-based emissions calculations and will incentivise use of lower emission products, services and suppliers.

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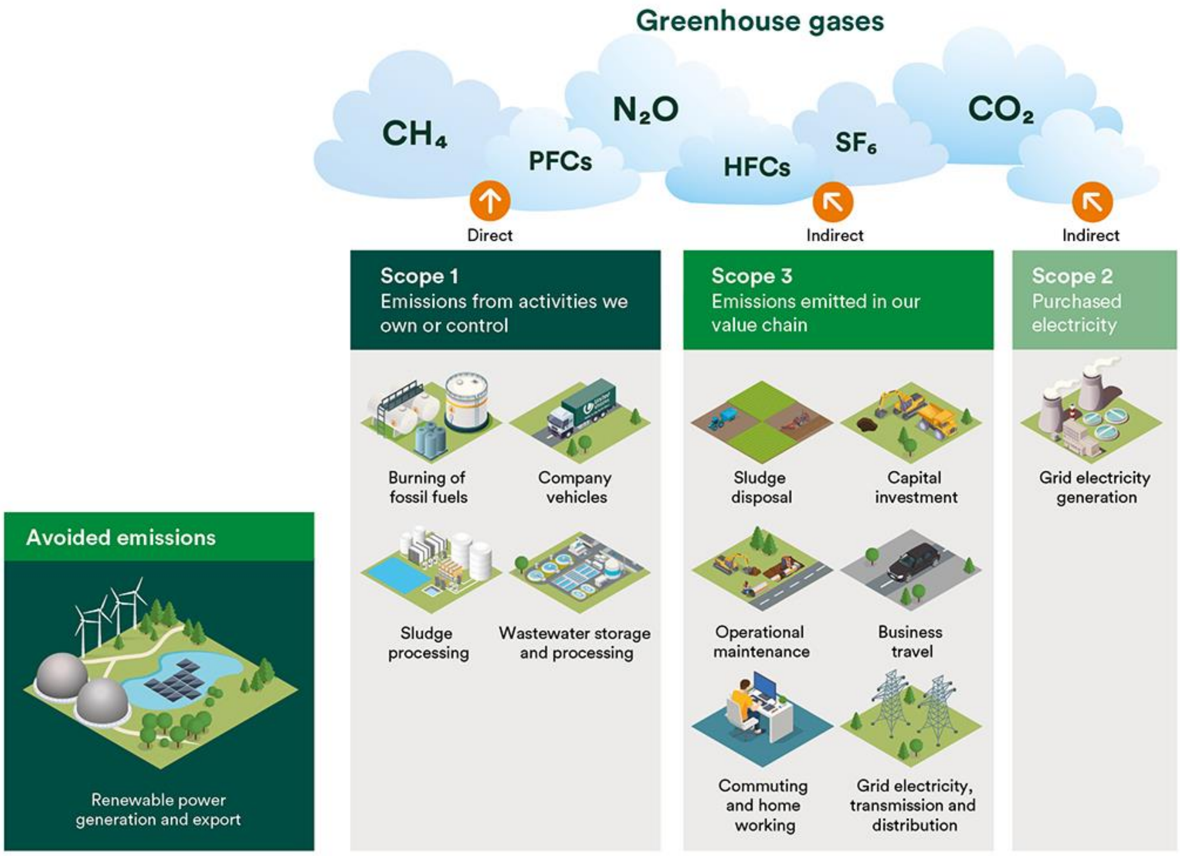

Our approach to climate change

Greenhouse gas emissions and energy

The greenhouse gas emissions for the financial year 2020/21 are presented in the table below. Emissions have been estimated using the water industry Carbon Accounting Workbook v15 (CAW v15) which incorporates the UK Government GHG conversion factors for company reporting. 2019/20 data has been restated using CAW v15 to reflect the significant changes from the previous version of the workbook, including improvements to the accounting for biogas and renewable electricity generated and used on site and an increased emission factor for wastewater process emissions (following the recommendation in UK Water Industry Research project report 'Quantifying and reducing direct greenhouse gas emissions from waste and water treatment processes – Phase 1' (20/CL/01/28)).

Scope 1, 2 and 3 emissions have been separated to align with the boundaries of our science-based targets. We now disclose all the scope 3 emissions categories described in the Corporate Value Chain (scope 3) Accounting and Reporting Standard that are deemed relevant to United Utilities. This change in scope 3 emissions reporting boundary has significantly increased our emissions in this area. The increase over the past year is due to variation in supply chain spend on goods and services.

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		Current CAW v15 2020/21 tCO2e	SBT baseline CAW v15 2019/20 tCO2e(2)	CAW v13 2020 2019/20 tCO2e	CAW v13 2020 2018/19 tCO2e
Scope 1 Direct emissions					
Direct emissions from burning of fossil fuels		17,371	15,247	17,129	16,809
Process emissions from our treatment plants – including refrigerants		98,569	96,186	84,048	88,136
Transport: company owned or leased vehicles		16,634	15,739	15,739	14,409
Scope 1 Total		132,575	127,172	116,916	119,354
Scope 2 Energy indirect emissions					
Grid electricity purchased – generation	Market-based(1)	8,507	11,789	11,789	18,503
	Location-based	149,030	164,521	164,521	187,171
Scope 2 Total		**8,507**	**11,789**	**11,789**	**18,503**
SCOPE1 AND 2 GREENHOUSE GAS EMISSIONS (GROSS)	**Market-based**	**141,082**	**138,961**	**123,705**	**137,857**
Avoided emissions from renewable energy		-4,184	-3,979	-3,979	-3,434
Renewable electricity exported					
Biomethane exported		-9,725	-9,302	-9,302	-8,446
Avoided emissions Total		-13,909	-13,281	-13,281	-11,880
SCOPE1 AND 2 GREENHOUSE GAS EMISSIONS (NET)		**121,173**	**125,680**	**115,424**	**125,977**
Scope 3 Other indirect emissions					
Purchased goods and services		271,871	213,442	-	-
Capital goods		95,968	128,286	-	-
Fuel and energy-related emissions	Market-based	42,599	45,262	1,007(2)	1,577(2)
Upstream transportation and distribution (sludge transport)		1,119	3,374	-	-
Waste generated in operations (including slide disposal to land)		26,333	27,936	27,410(3)	26,186(3)
Business travel (public transport and private vehicles)		1,226	3,508	1,123(4)	2,236(4)
Emissions from sludge and process waste disposal		4,108	4,231	-	-
Scope 3 Total	**Market-based**	**443,223**	**426,039**	**n/a**	**n/a**

SCOPE 3 GREENHOUSE GAS EMISSIONS (excluding capital goods)					
Science based targets	**Market-based**	**347,255**	**297,753**	**n/a**	**n/a**

(1) Market-based figures for electricity purchased on a standard tariff have been calculated using specific emissions factors from published generator fuel mix disclosures, shown in energy use table. Location-based figures use average grid emissions and are shown in blue.

(2) Well-to-tank emissions were not included in previous scope 3 inventory. We include well-to -tank emissions for electricity, natural gas and all liquid fuels.

(3) Sludge-to-land and grit and screenings only, other business waste was not included in the previous scope 3 inventory.

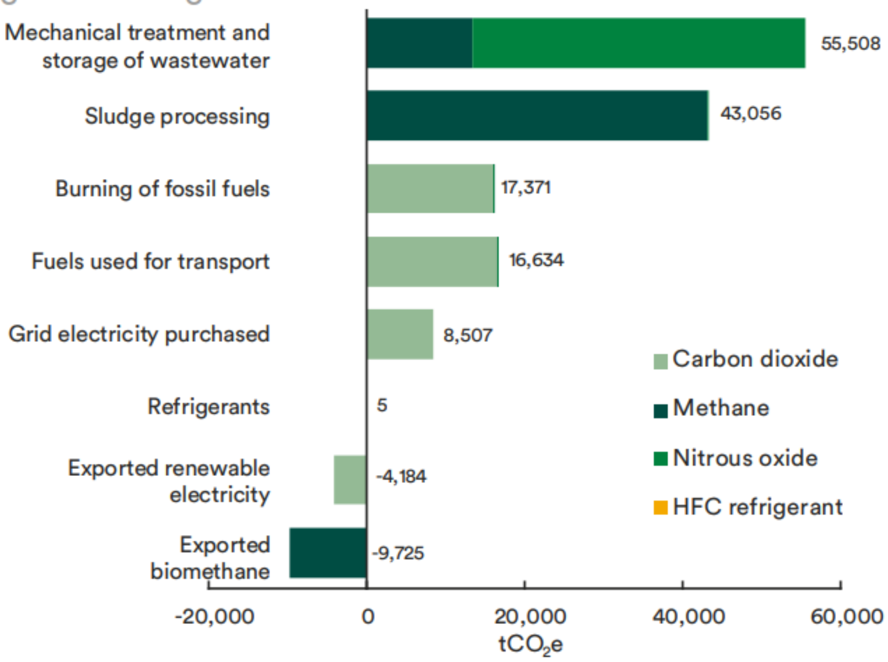
(4) Hotel accommodation, other travel services and outsourced transport were not included in the previous scope 3 inventory.

United Utilities' greenhouse gas emissions intensity

As in previous years we state our emissions as tonnes CO2e per £million revenue. We include scope 1 and 2 emissions only in this measure. We also report the regulated emissions tonnes CO e per megalitre treated (using the location-based method as calculated in the CAW v15), as these are common metrics for our industry. The methodology for this calculation changed from CAW v13 so the figure is not available for 2018/19.

		2020/21	2019/20	2018/19
Scope 1 and 2 greenhouse gas emissions (gross) per £m revenue	tCO2e	**78.0**	74.6	75.8
Scope 1 and 2 greenhouse gas emissions (net) per £m revenue	tCO2e	**70.3**	67.6	69.3
Regulated emissions per megalitre of treated water	kg tCO2e/Ml	118.51	131.98	n/a
Regulated emissions per megalitre of sewage treated	kg tCO2e/Ml	152.26	168.51	n/a

Scope 1 and 2 emissions – breakdown by activity and greenhouse gas



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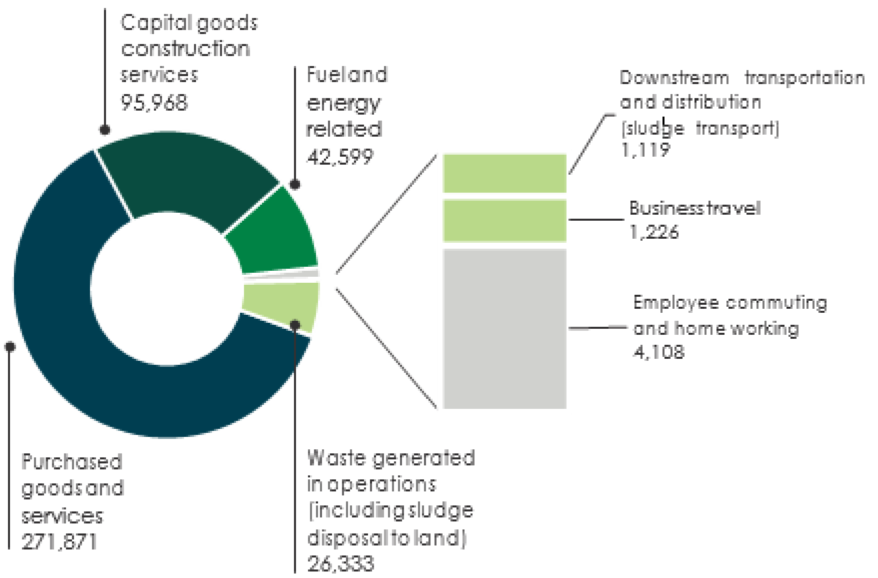
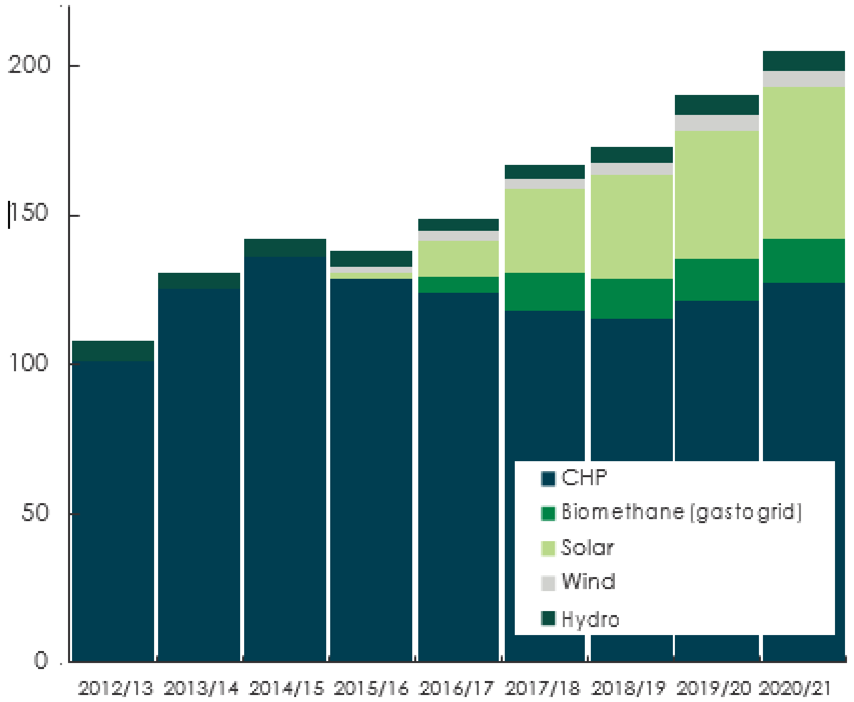
Scope 3 emissions by GHG Protocol category



Renewable energy generated



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Energy use, generation and export

	2020/21 GWh	2019/20 GWh	2018/19 GWh
Energy use			
Electricity	807.3	801.3	807.8
Gas	40.0	38.3	33.0
Other fuels(1)	104.0	144.4	135.0
Total energy use	**951.3**	**984.0**	**975.8**
Electricity purchased			
Renewable Tariff(2)	591.4	602.9	601.5
Supplier Standard Tariff (3)	47.8	40.8	59.7
Total electricity purchased	**639.2**	**643.7**	**661.2**
Renewable energy generated			
CHP	127.6	121.5	115.7
Solar	50.7	42.6	34.6
Wind	5.3	5.7	4.8
Hydro	6.9	6.8	4.6
Biomethane(4)	14.8	14.2	13.2
Total renewable energy generated		**190.8**	**172.9**
Renewable energy exported			
Electricity	22.4	18.1	13.0
Biomethane(4)	14.8	14.2	13.2
Total renewable energy exported	**37.2**	**32.3**	**26.2**

(1) Other fuels includes liquid fuel purchased for processing and transport plus business mileage in private vehicles converted to GWh using 2020 UK Government GHG Conversion Factors for Company Reporting.

(2) Electricity purchased on a renewable tariff had 0 CO2e/kWh emissions.

(3) Electricity purchased on our standard tariff had 289 CO2e/kWh emissions in 2019/20 and 178 CO2e/kWh emissions in 2020/21.

(4) Biomethane generated and exported to grid is expressed as an electricity equivalent.

Energy use and emissions

Our energy management strategy aims to achieve an appropriate balance between managing energy consumption, use of renewables and self-generation and being smart about how we operate our assets to get best value while maintaining security of supply. We are a relatively energy-intensive business, consuming 951 GWh in 2020/21. We have increased the amount of energy generated from renewable sources, such as hydro, solar photovoltaics, wind, biomethane and sewage sludge powered combined heat and power (CHP) generators. In 2020/21 we generated the equivalent of 205 GWh of renewable electricity, an increase of 14 GWh on 2019/20. We exported 37.2 GWh back to the national electricity and gas grids, 4.9 GWh more than the previous year. Overall we reduced our electricity purchase by 4.5 GWh.

Energy efficiency action taken

Our energy management programme brings together management processes, asset optimisation and data analytics. We have focused on optimisation of existing operations

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alongside realising opportunities through our capital programme to improve our use of pumps and how we manage wastewater treatment processes.

A focus area for 2020/21 has been our use of pumps. At Watchgate water treatment works, performance analysis of two key pump types led to the tactical refurbishment of the worst performing pumps and changes to the control philosophy – resulting in better efficiency, saving an estimated £40,500 per year, and a longer asset life.

At Heronbridge water treatment works, analysis of pump operation identified an opportunity to operate two pumps at minimum speed rather than a single pump at maximum speed. Running pumps closer to their best efficiency point reduces energy use and costs and should save approximately £45,000 per year.

Principal risks and uncertainties

Our risk management framework

We have a robust risk management 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 management 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.

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. These include an update to risk appetite statements, greater focus and analysis

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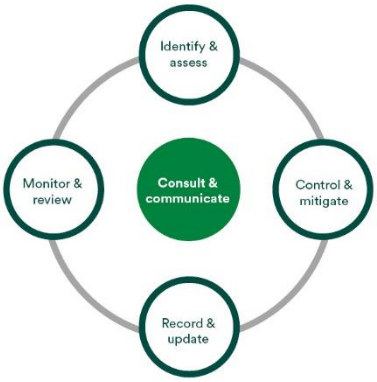
of cross-cutting themes and improved escalation of data from operational risk management systems.

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 determines 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 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.

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, and emphasises the most significant event-based risks 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. 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.

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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 consists of approximately 100 event-based risks, each of which relates to one of ten inherent risk areas, which we regard as our principal risks due to their potential to affect the performance, future prospects or reputation of the company. The allocation of event-based risks to principal risks enables the company to consider risks in the context of systems and production lines, in line with our Systems Thinking approach.

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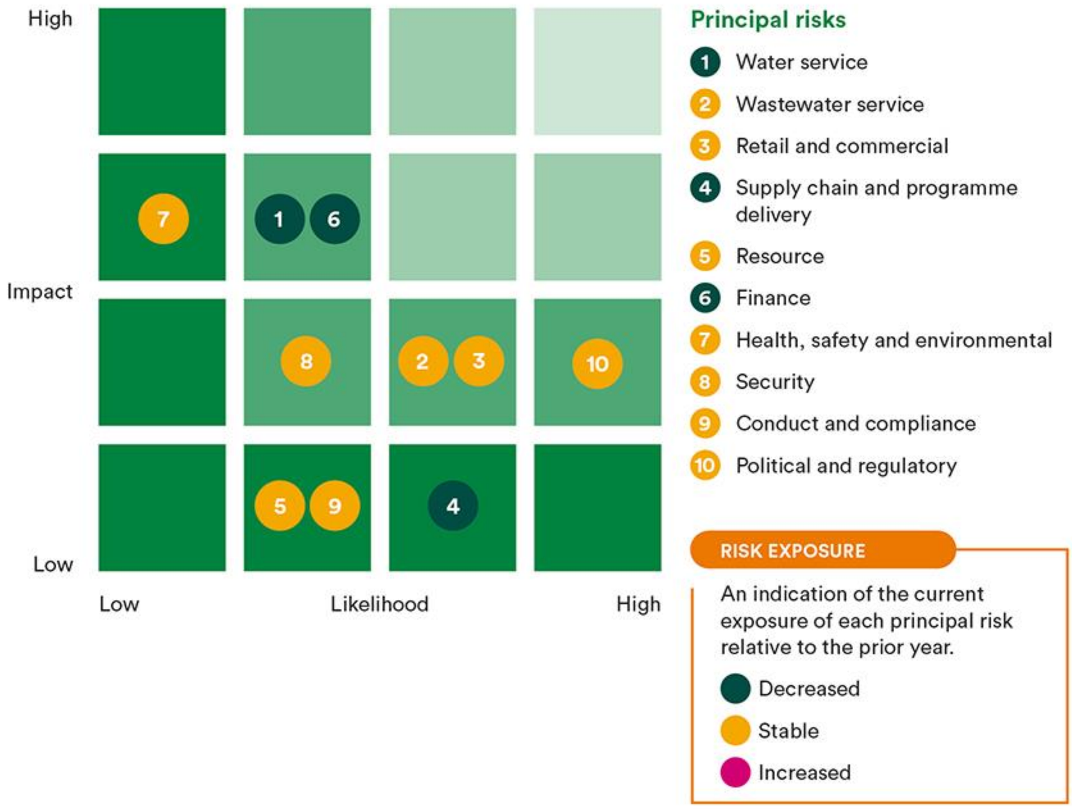
Principal risk heat map



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

Seven of the ten principal risks have remained relatively stable in the last 12 months. Water service, Supply chain and programme delivery and Finance have reduced due to the replacement of a section of the Haweswater Aqueduct, the trade deal with the EU and improvement in the economic outlook, respectively.

Common themes

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 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 to enable a more integrated, Systems Thinking approach to risk mitigation. Analysis of the control environment indicates the strengths, weaknesses and gaps in the mitigation of risk, as well as the interdependencies across the business to manage risk as part of the integrated approach.

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

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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).

- ***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: the anticipated post-Brexit changes in law bring an element of uncertainty; and the introduction of competition, whilst positive to customers and markets, can affect ongoing revenue and the asset base.

- ***Economic conditions:*** Macro events, such as the financial crisis in 2008 and more recently COVID-19, 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, culture cuts across the majority of risks in the profile. Our embedded corporate culture of innovation, customer service and behaving in a responsible manner provides an established platform, however, this is an area of ongoing focus to maintain high performance in an increasingly challenging business environment 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:

- ***Customer:*** 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 sizable 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.

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Our principal risks

Core Operations and Service Provision

1. Water service - risk decreased

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.

Risk exposure

Covering the entire water system from source to customers' taps, threats include: extreme weather which not only affects supply and demand through reduced rainfall, but can also affect raw water quality through fire or flooding; demographic changes affecting demand; asset health contributes to the frequency and magnitude of failure; and legal and regulatory change potentially increases the quality standards which will require time and investment in order to maintain compliance.

Potential impacts include: regulatory non-compliance; interruptions to water supply; or, in extreme cases, a danger to public health caused by poor water quality.

Control and mitigation

Strict quality controls supplement the physical and chemical treatment including a rigorous sampling regime, alarm systems and 'shut down and start up to waste' processes. Asset inspections, regular maintenance and cleaning are undertaken across our water assets, supported by a prioritised replacement regime. Water resources management, production planning, pressure/flow management and leak detection are undertaken to maintain supply and minimise interruptions. The integrated network, alternative supply vehicles and maintenance crews provide a response capability.

Performance indicators

- C-MeX
- Leakage
- Interruptions to supply
- Water quality compliance (CRI)

Most significant event-based risks

- Failure of significant water supply systems
- Failure of the distribution system (leakage)
- Dam failure
- Water sufficiency (dry weather)
- Water network failure

2. Wastewater service - risk stable

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

Risk exposure

Covering the entire wastewater and bioresource systems from customer properties to land, river or the sea, the key factors are: the capacity and capability of assets and operational processes;

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and the availability of sludge recycling outlets. Compounding issues include unauthorised third party discharges into the sewer network, changing demographics and extreme weather. Whilst generally designed to cope with the vast majority of storms, high intensity rainfall can overwhelm the system. Legal and regulatory change potentially increases standards or imposes restrictions which will require time and investment to maintain compliance.

Potential impacts include: regulatory non-compliance; interruptions to drainage services; pollution incidents (including odour nuisance and sewer flooding); and inability to dispose of sludge to land.

Control and mitigation

The sewer network is managed through a combination of the drainage and wastewater management plans and the wastewater network operating model which include asset condition surveys to identify defects, sewer rehabilitation projects, customer campaigns and sewer cleaning programmes. Integrated drainage area studies and the adoption of a pollution incident reduction plan aim to make further enhancements. Proactive maintenance, operative training, sampling, compliance audits and odour management systems supplement the treatment processes across our wastewater and biosolids systems.

Performance indicators

- C-MeX
- EA performance assessment
- Internal flooding incidents
- Pollution incidents

Most significant event-based risks

- Failure of wastewater network (sewer flooding)
- Failure to treat wastewater
- Failure of wastewater assets (serious pollution)
- Recycling of biosolids to agriculture

3. Retail and commercial - risk stable

Failing to provide good and fair service to domestic customers and third-party retailers or a failure of or issue in relation to non-United Utilities Water operations or businesses.

Risk exposure

Key factors include the social deprivation across the North West, the macroeconomic environment, and the experience and perception of customers towards our operations and service. Commercial contractual terms and conditions and the structure, positioning and efficiency of joint ventures, subsidiaries and undertakings are also factors.

Potential impacts include financial losses and an impact on profitability associated with poor cash-flow and an increase in bad debt. Poor service and associated decreased customer satisfaction could result in regulatory penalties and reputational harm.

Control and mitigation

Our customer-focused initiatives aim to drive excellent service and enhance the experience of all our customers. We have an award-winning Priority Services scheme for vulnerable customers and those needing help to pay, which has driven up our success in recovering charges. Bad debt risk is managed through best practice collection techniques, segmentation of customers

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and the use of data sharing to determine the most effective and collaborative collection and support activities.

The wholesale business maintains processes, systems and data to deal fairly with market participants and the central market operator in the business retail market in order to generate and collect revenue.

Performance indicators

- C-MeX
- Customer complaints
- D-MeX

Most significant event-based risks

- Billing accuracy
- Customer experience

Functional Service and Support

4. Supply chain and programme delivery - risk decreased

The potential ineffective delivery of capital, operational and change programmes/processes.

Risk exposure

As the supplier of essential water and wastewater services with a significant asset base, key factors include the consistent supply of critical goods and services and the ongoing development of operational facilities, distribution networks and systems. Disruption and delay can occur through macro economic conditions, political issues or natural disasters in the country of origin. Contractual issues, technical or engineering complications, natural hazards such as extreme weather or legal aspects such as planning permission or access rights are also factors.

Potential impacts include: implications to cash-flow; failure to take opportunities and competitive advantage; and ultimately failure to meet our obligations and customer outcomes.

Control and mitigation

Category management and supplier relationship management are key areas of control underpinned by contract management across our extensive supply chain. Capital, change and operational programmes are undertaken in order of priority following approval. Within the capital programme we have created better alignment and integration between our capital delivery partners, engineering service providers and our operating model. Our programmes and project management include risk and issue management.

Performance indicators

- Percentage invoices paid within 60 days
- Time, cost and quality index

Most significant event-based risks

- Unfunded developer-led projects
- Dispute with supplier

5. Resource - risk stable

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

Risk exposure

The nature and scale of our operations warrants a highly efficient, effective and competent set of resources that is adaptable to a constantly changing business environment. Key factors include: the recruitment and selection of talent, employee engagement, skill-set and knowledge; obsolescent systems due to innovative new ways of working and advances in technology; the quality of tools, equipment and vehicles; and ongoing deterioration of property, land and other assets.

Potential impacts include the inability to maintain efficiency, optimise opportunity and competitive advantage, or meet our obligations and customer outcomes.

Control and mitigation

Developing our people with the right skills and knowledge, combined with delivering effective technology to support the business in meeting its objectives. Employees are kept informed regarding business strategy and progress through various communication channels. Training and personal development programmes exist for all employees in addition to talent management programmes and apprentice and graduate schemes. We focus on change programmes and innovative ways of working to deliver better, more resilient and more cost-effective operations. Resources are closely monitored because of COVID-19, with homeworking and safe site working practices being adopted. People with multiple skill sets are able to add resilience across the business.

Performance indicators

- Employee engagement

Most significant event-based risks

- Land management
- Business critical data

6. Finance - risk decreased

The potential inability to finance the business appropriately.

Risk exposure

The extent of our capital programme and the scale of our operations means that it is important that we are able to raise finance when needed to preserve adequate liquidity. Key factors include unexpected and/or higher costs associated with an operational incident, fluctuations in commodity prices and our exposure to movements in interest rates and inflation. A reduction in credit ratings, the over payment of tax and a worsening of the pension scheme funding position are also factors. Contributing factors include the macroeconomy, the political and regulatory environments relative to the water sector, and our internal financial structure.

Potential impacts include cash flow implications, reduced profit and ultimately the solvency of the company in extreme cases.

Control and mitigation

Long-term refinancing with staggered maturity dates and significant liquidity to minimise the effect of short-term downturns. Counterparty credit exposure and settlement limits exist to reduce any potential future impacts. These are based on a number of factors, including the credit rating and the size of the asset base of the individual counterparty. The group employs hedging strategies to manage the impact of market fluctuations for inflation, interest rates and energy prices. Sensitivity analysis is carried out as part of the business planning process,

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influencing the various financial limits employed. Continuous monitoring of the markets takes place, including movements in credit default swap prices and movements in equity levels.

Performance indicators

- Return on Regulated Equity (RoRE)
- Underlying operating profit
- Gearing (net debt : RCV)

Most significant event-based risks

- Financial outperformance
- Credit ratings
- Pension deficit
- Fair payment of tax

Hazard-Based

7. Health, safety and environmental - risk stable

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

Risk exposure

The nature and scale of our operations presents multiple hazards to employees, contractors, the public and the environment. These include confined spaces, excavations, explosive atmospheres or high volume asset failures (e.g. dams or aqueducts), and polluting sewage and chemicals if accidentally or uncontrollably released.

Potential impacts include: serious injury or loss of life; catastrophic damage to property/infrastructure; and damage to, or destruction of, wildlife, fish or natural habitats. Environmental hazards, notably extreme weather, can affect our operational assets and service delivery.

Control and mitigation

We have a strong health, safety and environmental culture supported by strong governance and management systems certified to OHSAS 18001 and ISO 14001 respectively. We actively seek to improve health, safety and wellbeing across the group through targeted improvements and benchmarking against our peers and seek to protect and improve the environment through the responsible delivery of our services. This includes helping to support rare species and habitats through targeted engagement and activity, as well as our commitment to reducing our carbon emissions by designing out waste from our operations, generating our own energy and looking at ways to reduce our use of raw materials. Due to the impact the environment can have on our services, extreme weather and climate change is being integrated into our risk, planning and decision-making processes.

Performance indicators

- EA performance assessment
- Accident frequency rates

Most significant event-based risks

- Disease pandemic
- Process safety

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- Personal safety
- Carbon commitments
- Failure of above -ground assets (flooding)

8. Security - risk stable

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

Risk exposure

As the supplier of essential services and the owner and operator of critical national infrastructure, security is of paramount importance against an ever evolving and increasingly sophisticated threat through physical, technological, chemical or biological means. This could originate from rogue independent actors, nation states, organised crime, disgruntled employees, or as a result of commercial espionage.

Potential impacts include the loss or compromise of commercially sensitive data, the disruption of business activity and/or damage or destruction of systems, assets or infrastructure with a knock-on impact to service delivery and community infrastructure.

Control and mitigation

Security measures and awareness training combined with strong governance and inspection regimes aim to protect infrastructure, assets and operational capability. We work closely with our industry peers, the Centre for the Protection of National Infrastructure (CPNI), the National Cyber Security Centre (NCSC), the Drinking Water Inspectorate and Defra. We liaise with these organisations to shape the sector approach to security, understand how to better protect our business, and be compliant with the Network and Information Systems Directive (NIS). Ongoing system and network integration improves operational resilience and we maintain robust incident response, business continuity and disaster recovery procedures. We maintain insurance cover for loss and liability, and the instrument of appointment (licence) of the regulated business also contains a ‘shipwreck’ clause that, if applicable, may offer a degree of recourse in the event of a catastrophic incident.

Performance indicators

- Cyber incidents

Most significant event-based risks

- Cybercrime
- Terrorism

Regulatory and legal

9. Conduct and compliance - risk stable

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

Risk exposure

Our business extends to multiple stakeholders and is subject to a significant amount of legislation and regulation. Long-term sustainability, resilience and reputation rely on responsible conduct and compliance across our business and extended supply chain.

Failure to comply with legal obligations could lead to financial penalties, reputational harm and loss of customer and investor confidence. Fines of up to 10 per cent of group turnover could be imposed, particularly in the areas of environmental, health and safety, competition, and information and data security. Ultimately sanctions could include, in extreme circumstances,

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revocation of the instrument of appointment (licence) and the imposition of a special administration regime.

Control and mitigation

We place high importance and focus on corporate responsibility. Our well-established internal forums and engagement activities with communities, landowners, environmental groups and other stakeholders allow us to be aware of current issues and concerns. These include ethical supply chains, modern slavery risks, the needs of vulnerable customers and diversity and equality within our own employee population.

Performance indicators

- Community investment
- EA performance assessment
- C-MeX

Most significant event-based risks

- Non-compliance with the Bribery Act
- Digital Service licensing

10. Political and regulatory - risk stable

Developments connected with the political, regulatory and legislative environment.

Risk exposure

As a regulated business, the political and regulatory environment shapes how we operate as a business. Factors include the public perception of the water industry and its legitimacy to provide value, increased challenges on efficiency and the imposition of increased levels of competition across the sector.

There is therefore the potential for increased costs of administration and for sources of income and funding to be impacted. There is also the potential for reduced Regulatory Capital Value (RCV) and for greater uncertainty of returns.

Control and mitigation

We continue to take part in government and regulatory consultations in order to influence outcomes in respect of policy and legislation. We routinely communicate with customers so that their needs and expectations can be factored into our thinking and plans.

Performance indicators

- Return on Regulated Equity (RoRE)
- Underlying operating profit

Most significant event-based risks

- Reduced revenue at the next price review
- Upstream competition (bioresources)
- DPC – Haweswater Aqueduct Replacement Programme (HARP)

The company's most significant event-based risks

The most significant event-based risks represent: the ten highest-ranked risks by exposure relative to the likelihood of occurrence of the event and most likely financial impact (1 - 10 below); and those risks which have been assessed as having a significantly high impact, but low likelihood (A - F below). Depending on the circumstances, financial impacts will include loss of revenue, additional or extra cost, fines, regulatory penalties and compensation. Reputational

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impact relative to our multiple stakeholders is also assessed, reported and considered as part of the mitigation.

1. Failure of significant water supply systems

Risk exposure: The Haweswater Aqueduct (HA) is a key asset with current low resilience due to deterioration, potentially resulting in water quality issues and/or supply interruptions to a large proportion of our customer base.

Control/mitigation: Capital projects for asset replacement (including HARP), as well as extensive programmes of asset monitoring, surveys and maintenance.

2. Failure of wastewater network (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.

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

3. Cybercrime

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.

4. Reduced revenue at the next price review

Risk exposure: One of many potential issues relates to the Totex allowances through AMP8 revenues for labour costs, due to the Office of National Statistics ASHE Index taking account of lower wages associated with COVID-19.

Control/mitigation: Reviewing the rule book once published and liaising with Ofwat accordingly.

5. Failure to treat wastewater

Risk exposure: Inadequate capacity and capability of wastewater treatment works, leading to environmental permit breaches.

Control/mitigation: Improved Effective Operations & Maintenance (EO&M) programme and operating procedures including proactive maintenance, operative training and compliance audits.

6. 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.

7. Credit ratings

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.

8. Failure of wastewater assets (serious pollution)

Risk exposure: The unintended introduction of pollutants (including sewage) into the environment, due the capacity and capability of wastewater assets.

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Control/mitigation: Proactive identification of asset defects through condition surveys, staff training, incident analysis, drainage area studies and improvement plans.

9. Upstream competition (bioresources)

Risk exposure: Competition in the bioresources market leading to a loss of business and reduced operational efficiency.

Control/mitigation: Delivering operational efficiency, continued engagement with Ofwat and a strategic review of the bioresources business.

10. Failure of the distribution system (leakage)

Risk exposure: Network characteristics, asset condition, extreme weather or third party damage resulting in the loss of treated water and failure of the leakage target.

Control/mitigation: Management of pressure and flow combined with traditional and innovative leakage detection techniques.

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.

B) 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.

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.

D) 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.

E) 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 Protection of National Infrastructure (CPNI), regional counter terrorist units, local agencies and emergency services.

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F) Process safety

Risk exposure: The unintentional generation and/or release of dangerous substances and explosive atmospheres in sludge digestion or other processes, resulting in a catastrophic incident.

Control/mitigation: The design and engineering of facilities, training and maintenance of equipment. Effective control points exist with alarms monitored remotely and statutory inspections.

New and emerging risks

We continue to review and monitor external and internal business environments in order to establish and understand risks and issues that are new, developing, growing or becoming more prominent. We do this through a combination of business unit risk assessments, a specific new and emerging risk forum and other horizon scanning forums such as a compliance working group. This enables us to plan our strategy and operations to minimise threats of this nature. Notable new and emerging risks and some possible impacts are set out below.

- **Post-Brexit supply chain:** Despite the successful negotiation of the trade deal with the EU there remains some uncertainty in relation to the supply of goods and services. We manage the supply chain through category management with chemicals and critical spares being two categories which are fundamental to the delivery of our service provision. We will continue to monitor how the supply chain emerges and will adapt accordingly through category management and supplier relationship management.
- **Post-Brexit legislative change:** Post-Brexit uncertainty remains in relation to how European legislation will transition into UK law, for example, data protections laws governing the flow of data and information between the EU and UK. Changes in UK law, such as the Environment Bill, Sewage (Inland Waters) Bill and changes to Public Procurement will all have implications for the water sector.
- **Regulatory change:** The political landscape remains challenging for the water sector. There remains uncertainty regarding the introduction of further competition and therefore the associated implications for revenue and the asset base. Looking ahead to Price Review 2024 (PR24), the methodology remains uncertain, particularly in light of the outcome of other water companies' PR19 CMA appeals.
- **Plastics:** Implications associated with the current attention on single use plastics and microplastic pollution in water, wastewater effluent discharge and sludge disposal (see biosolids recycling to agriculture).
- **Biosolids recycling to agriculture:** The practice of disposing of biosolids to agriculture could be banned (partially or in full) in the UK based on similar actions within Europe.
- **Water scarcity and water trading:** Water scarcity is an emerging issue within the UK, which has knock-on implications to UU in relation to the proposed strategic transfer of water from the North West to the South East of England, and the associated service, commercial and reputational impacts.
- **COVID-19:** To a large degree, COVID-19 has become business as usual, however, the longer-term implications of the economic downturn with potential corporate failures and high unemployment could affect cash collection. Continued lower inflation will affect revenues, financing costs and RCV, however, rising inflation will have an upside over the longer term.

Material litigation

The group robustly defends litigation where appropriate and seeks to minimise its exposure by establishing provisions and seeking recovery wherever possible. Litigation of a material nature is regularly reported to the group board. Beyond that reported in previous years on the Argentina multiparty ‘class action’ and the Manchester Ship Canal Company matters (to which there have been no material developments), there is nothing specific to report on material litigation.

Corporate governance report

Biographical details of the board of directors

Sir David Higgins

Chairman

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: Chairman of Gatwick Airport Limited and a member of the Council at the London School of Economics. He is also Chairman 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 chairman 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: 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. Steve ceased to be a non-executive director of G4WS plc following its takeover in April 2021.

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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.

Specific contribution to the company's long-term success: As 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 company'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. 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.

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 Chairman 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.

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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 and Ladbrokes Coral PLC.

Current directorships/business interests: Mark was appointed as a non-executive director and chairman designate at Aggreko plc in October 2020. He was appointed as senior independent non-executive director at Wickes Group plc and as chairman of the remuneration committee in April 2021. He is non-executive chairman at Grainger plc and a non-executive director 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.

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. Former chairman Ashridge Business School. A Life Peer since 2008.

Current directorships/business interests: Group chief executive 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 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.

Corporate governance report

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 stepped down as a non-executive director at Brewin Dolphin Holdings plc in February 2021.

Current directorships/business interests: Kath is a non-executive director at RSA Insurance Group plc and chair of the remuneration committee. She is a non-executive director at Columbia Threadneedle Investments where she chairs the TPEN audit committee and a non-executive director of TP ICAP Group Plc. 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 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 at Meggitt PLC and a part-time executive chair 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 will provide the board with a better understanding of the views of employees and the culture of the company.

Brian May

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 committee.

Qualifications: BSc (Hons) Actuarial Science, Chartered Accountant FCA.

Appointment to the board: September 2012.

Skills and experience: Brian’s background in finance and accounting and the various roles that he has held are major assets to the board. He has been chair of the audit committee since September 2013 and has considerable knowledge of the company and the specifics of the utilities sector.

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Career experience: Brian was appointed group finance director of Bunzl plc in January 2006 and he retired from the board of Bunzl plc on 31 December 2019.

Current directorships/business interests: Brian was appointed as a non-executive director and member of the audit committee of Ferguson plc in January 2021. He is a non-executive director of ConvaTec Group Plc and a member of its audit and risk committee and chair of its remuneration committee. He is an independent non-executive director of United Utilities Group PLC.

Specific contribution to the company's long-term success: Brian contributes his considerable expertise in finance to the company primarily through the important roles as chair of both the audit committee and the treasury committee, which are important in overseeing the risk management of the group. The industry knowledge he has gained over the eight years he has been a board member enabled him to focus on, and contribute to, key risk areas during the regulatory price review process for the 2020–25 regulatory period.

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 (Hons) Mechanical Engineering and Management, 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.

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.

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.

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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:

Russ Houlden (CFO) and Sara Weller (independent non-executive director) both left the board at the end of the company's AGM in July 2020. Furthermore, they both ceased to be directors of United Utilities Group PLC at that time.

Brian May will not be seeking reappointment at the AGM in July 2021, having served on the board for almost nine years. At the same time he will cease to be a director of United Utilities Group PLC.

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Letter from the Chairman, Sir David Higgins:

Dear Shareholder

Over the past year the board's focus has been has been dominated by the group's response to the pandemic and ensuring the safety and support for our employees while maintaining the delivery of services to customers across our region. As a regulated monopoly supplier, with a population of 7.3 million in our region, we need to work hard to meet the high expectations customers have for us, both in terms of the services we provide but also in behaving as a responsible business in the way in which we provide them. To do so is crucial to the long-term success of United Utilities.

During the period May to November 2020, the board reviewed the impact of the pandemic on the financial performance of the group, including understanding the ability of some customers facing financial hardship to pay for our services. As a consequence, an extension of the company's social tariff arrangements were approved, to apply until the end of the 2021/22 financial year. At the same time, the board did not want to jeopardise the great progress made over the last five years in improved operational performance, led by Steve Mogford and his team. Throughout this report you will see examples of our improved operational performance as recognised against the benchmarks set by our regulators. These improvements have given the board greater confidence of achieving regulatory outperformance during AMP7, and support our longer term plans for the next asset management period.

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 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 2021.

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 holding company levels 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.

People

I would like to thank Brian May for his excellent work and support during my first full year as Chairman. It was announced in May 2021, that after nearly nine years' on the board, Brian would be stepping down at the conclusion of the AGM in July 2021. Doug Webb, whom we welcomed to the board in September 2020, was recruited as an independent non-executive director, to chair both the audit and treasury committees on Brian's departure. Doug brings to the role, as required by the code, 'recent and relevant financial experience'. Given the complexities of the work of both the audit committee, and the treasury committee particularly in terms of the regulatory operating model, it was felt that a handover period between Brian and Doug covering a full audit cycle would be particularly beneficial. Doug will also become a member of the remuneration committee when Brian steps down from the board.

In September 2020, along with Doug, we welcomed Kath Cates, as a new independent non-executive director. Kath brings a wealth of experience of regulated businesses from her executive career in financial services. Alison Goligher, who has served as a member of the remuneration committee since 2016, accepted the role as chair of the remuneration committee on Sara Weller's departure from the board at the conclusion of the 2020 AGM.

2021 is the first annual report presented by the board under the tenure of Phil Aspin as CFO. As demonstrated by his biography, Phil has many years' experience in different financial roles within the business, which has undoubtedly facilitated a smooth transition in a challenging year. Phil succeeded Russ Houlden, who retired from his executive responsibilities in July 2020.

ESG, and specifically our progress in terms of diversity and inclusion are increasingly areas of interest for many stakeholders. We have sought to respond by better articulation of our ESG activities throughout this annual report, including our efforts toward improving diversity and inclusion both at board level and across the business, and more information can be found on pages 132 and 138 of the UUG Annual report and financial statements respectively.

Corporate governance report

Sir David Higgins

Chairman

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 UUW 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 2020/21. 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 UUW Annual Performance Report, the United Utilities Water Limited statutory accounts 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, create value for shareholders and take account the needs of 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 2020/21 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.

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 can be found on pages 156 to 159 of the 2020/21 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

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information and views from stakeholders through utilising research and engagement – including that which contributed to our AMP7 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 2021, 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, particularly during this most extraordinary year, 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.

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.

Our three strategic themes are:

The best service to customers – This means that we put customers at the heart of everything we do. As well as delivering a reliable water service and removing wastewater, we proactively keep customers informed about work we are doing in their area and communicate with them in ways that meet their individual needs. We seek to engage with communities and customers about matters that are important to them, providing advice and support. We are always available through multiple channels when customers need us, interacting in a friendly and helpful manner and offering tailored support and assistance for customers households and businesses as well as the communities we serve. We ensure we have an active programme to act and listen to customers, using research, insight and data to make the service we deliver every day better. We consult regularly and co-design solutions with a customer panel of over 7,000 customers so that the services we deliver build on the input received from the very customers we are proud to serve every day.

At the lowest sustainable cost – In order to run a resilient business, it is important to ensure cost reductions are sustainable so that we can keep costs down in the long term without compromising on the resilience or quality of services we deliver. When we develop our plans and assess different options for consideration, we look to minimise the whole-life cost through a holistic approach. Our Systems Thinking approach helps us look at all options, and operating our entire network as a system rather than discrete assets opens up new avenues for service delivery that would otherwise not have been identified. Innovations in recent years have included installing sensors across our network that allow remote monitoring and control from our integrated control centre and building a fleet of alternative supply vehicles that inject treated water directly into supply while we undertake repairs and minimise supply disruptions.

In a responsible manner – Our purpose drives us to deliver our services in an environmentally sustainable, economically beneficial and socially responsible manner, looking after the interests of the stakeholders with whom we interact. 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 and working hard to drive a more inclusive and diverse workplace, ensuring that our services are representative of the customers we serve. It drives us to support local communities on issues that matter to them and 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 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.

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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.

The United Utilities Group PLC Annual Report and Financial Statements demonstrates how these strategic themes run through everything we do. For further information and explanation of our approach, we would refer in particular to the 2020/21 Strategic Report (pages 16 to 109), our key performance indicators (operational pages 52 to 72 and financial 74 to 75), our risk management framework (pages 100 to 109) and our description of governance (pages 112 to 191.)

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.

Our employees are at the heart of the culture of our business and further insight and evidence, as part of the board's assessment and monitoring of culture, has been gathered and fed back to the board by Alison Goligher, the current designated non-executive director for engagement with the workforce. Ordinarily Alison would have held face to face meetings with employees and visited a number of the company's sites but this has unfortunately not been possible due to the pandemic. Meetings of the Employee Voice panel have continued to be held virtually and chaired by Alison. The Employee Voice panel comprises representatives of a number of employee groups and employee networks already in existence (such as gender, ethnicity, ability and LGBT+) and with representatives drawn from across the geographical region.
Alison is keen to ensure, through these interactions, that there is a two-way flow of communication and information between the board and employees. The board has discussed updates from the Employee Voice panel including an oversight of the panel's activities, its links to employee network groups, its contribution to the work on diversity and inclusion and the "next ways of working project" which is considering how workplaces and work practices should evolve in the coming years. The board reflected on the insight provided by the Employee Voice panel and the results of the annual employee engagement survey.

In addition to the existing reporting, management has developed a dashboard of cultural metrics to provide a comprehensive overview to support the board in fulfilling its role in monitoring and assessing culture. The dashboard comprises relevant metrics derived from the annual employee engagement survey; human resources policies in relation to diversity and associated training; whistleblowing reporting; health, safety and wellbeing policies and practices; and measures that evidence how we are fulfilling our purpose.

In the last reporting year, the board has considered several matters relating to purpose and values. For example, it reviewed progress with our aspiration for a diverse and inclusive workforce and was kept appraised of our programme of work to increase diversity of the workforce and improve inclusivity. Our commitment to embed a health and safety culture to

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ensure employees go home safe and well was discussed, including examination of health, safety and wellbeing activities and consideration of health and safety incidents of employees and contractors. The implementation of employee wellbeing policies and activities was 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 2021/22 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. Details of how the board monitors culture and employee engagement are set out on pages 126 to 127 of the 2020/21 United Utilities Group PLC Annual Report and Financial Statements.

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 UUW 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 2021.

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 2021.
The boards of both UUG and UUW 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.

Provisions:

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 UUW 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 UUW contained within UUG board's schedule of matters reserved for its own decision, a copy of which can be found on our website at www.unitedutilities.com/globalassets/documents/pdf/03---schedule-of-matters-reserved-for-decision-by-the-board.pdf.

UUW 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 UUW represents approximately 98 per cent of UUG's revenues, decisions taken for UUW 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.
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 UUW board has delegated specific powers, subject to certain limits, relating to the capital investment programme to the UUW capital investment committee and in relation to financing, by way of power of attorney, to the Chief Financial Officer and/or the Treasurer. UUW does not

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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 UUW matters, given that UUW represents approximately 98 per cent of UUG's revenues. The alignment of the interests of UUW and UUG ensures that the interests of UUW and its customers are safeguarded, and avoids unnecessary duplication. The group has operated in this manner since 2011.

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 2020/21 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 in July 2019 and to have attained World Class ranking in the Dow Jones Sustainability Index for 14 consecutive years. 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 the audit committee.

Our human rights policy can be found on our website at 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. During the pandemic, we engaged with our supply chain partners and shortened our payment terms to assist them with their cashflow.

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

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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 external 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 completed by the company secretary's team. The external review took place this year in February 2021. This process identified action points and ongoing training needs. Further details of the evaluation can be found on page 135-136 of the 2020/21 United Utilities Group PLC 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. Further details of the company's approach to transparency and governance can be found in the corporate governance report contained within pages 112 to 191 of the 2020/21 United Utilities Group PLC Annual Report and Financial Statements .

Provisions:

A detailed explanation of the structure of the United Utilities group is set out on page 131 of the 2020/21 United Utilities Water Limited Annual Report and Financial Statements.
An explanation of dividend policies and dividends paid, and how these take account of delivery for customers and other obligations (including to employees).

In January 2020 the board set UUW's AMP7 dividend policy. This included a reduced assumption in relation to the base dividend compared to AMP6. In addition, the board committed to a significant number of additional considerations which will ensure that dividend payments continue to be taken subject to consideration of the interests of a broad range of stakeholders who have interests in the performance of the company. This approach includes commitments on financial assistance schemes for customers, safeguards about the level of company gearing, sharing of future outperformance, consideration of financial resilience, delivery of statutory obligations and delivery against performance targets. Further details of these policies is provided in section 2.4 of the APR. This section explains UUW's prudent decision to pay no dividends during 2020/21, demonstrating the application of the checks and balances outlined in the 2020-25 dividend policy.

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 100 to 109 of the 2020/21 United Utilities Group PLC Annual Report and Financial Statements.

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.

Board attendance table for the year ended 31 March 2021 - set out below are the number of scheduled meetings attended and the maximum number of scheduled meetings that could have been attended.

Sir David Higgins	8/8
Steve Mogford	8/8
Phil Aspin[1]	4/4
Mark Clare	8/8
Stephen Carter	8/8
Kath Cates[2]	4/4
Brian May	8/8
Alison Goligher	8/8
Paulette Rowe	8/8

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Doug Webb[3]	4/4
Russ Houlden[4]	4/4
Sara Weller[5]	4/4

1. Phil Aspin was appointed as a director and CFO with effect from 24 July 2020.
2. Kath Cates was appointed as a non-executive director on 1 September 2020.
3. Doug Webb was appointed as a non-executive director on 1 September 2020.
4. Russ Houlden stepped down from the board on 24 July 2020.
5. Sara Weller stepped down from the board on 24 July 2020.

Details of the attendance at meetings of the board committees can be found on page 124 of the 2020/21 United Utilities Group PLC Annual Report and Financial Statements

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 during 2020/21 is set out on pages 182-188 of the 2020/21 United Utilities Group PLC Annual Report and Financial Statements. Details of remuneration for the directors of UUW is set out within pages 132 to 134 of the UUW Limited Statutory Accounts. The criteria for awarding short and long-term performance related elements are 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 98 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 corporate governance report that can be found on pages 120 to 196 in the 2020/21 United Utilities Group PLC Annual Report and Financial Statements.

Provisions:

Boards and board committees have the appropriate balance of skills, experience, independence and knowledge of the company. Boards identify what 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 to 115 and the skills matrix of directors is set out on page 133 of the 2020/21 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 131 of the 2020/21 United Utilities Group PLC Annual Report and Financial Statements.) Appointments to the board are subject to a formal, rigorous and transparent procedure. The

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board diversity policy (see page 133 of the 2020/21 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 25 per cent and aspire to 33 per cent gender diversity by 2020 and to have at least one director of non-white ethnicity by 2021. These targets will be met as at the end of July 2021. An effective succession plan is maintained for board and senior management. Improving diversity and inclusion within the group has been a particular focus for the board during the year - further detail is set out on pages 138 to 140 of the 2020/21 United Utilities Group PLC Annual Report and Financial Statements. Input into the work on diversity and inclusion was provided, amongst others, by both the Employee Voice panel and from board members.

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 ten. Their biographies can be found on pages 112 to 115 of the 2020/21 United Utilities Group PLC Annual Report and Financial Statements. Independence is tested against the criteria set out in the code.

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 chairman 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 Chairman on 1 January 2020. The roles and responsibilities of the Chairman are set out as part of the group's governance framework.

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 undertaken by Independent Audit Limited. Full details, including recommendations, can be found on page 135 to 136 of the 2020/21 United Utilities Group PLC Annual Report and Financial Statements. 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 130 to 137 of the 2020/21 United Utilities Group PLC Annual Report and Financial Statements.

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.

Kath Cates and Doug Webb, who were appointed to the board on 1 September 2020 met (via video call) with representatives of Ofwat prior to their appointment on 2 July and 16 July 2020 respectively, as have all non- executive directors since April 2016.

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.

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E) Delivering for customers and stakeholders

In this first year of AMP7 we have delivered our best ever year for operational performance. We beat our leakage target for the 15th consecutive year, delivering our lowest level ever of leakage using a combination of techniques ranging from satellite technology to sniffer dogs. We have seen the benefits of delivering our Pollution Incident Reduction Plan with no serious pollution incidents for the second year running and reducing total pollution incidents by almost a third. For the first time ever we had no failing Wastewater Treatment Works as classified by the Environment Agency. We entered AMP7 knowing that our biggest challenge would be against our internal flooding performance commitment and this is the measure that has yielded the largest underperformance payment this year. As part of the £300 million extension to our AMP7 totex plans, we will be investing around £100 million in Dynamic Network Management (DNM) – a ground breaking application of Systems Thinking using state of the art sensors and predictive machine intelligence to move to a more proactive management of our wastewater network. This new digital capability is expected to improve service to customers and improve performance against our internal flooding commitments.

We have experienced significant variations in weather this year facing both long, dry periods and significant rainfall events, which has impacted on our performance for per capita consumption and numbers of flooding incidents. Despite all of the challenges we faced this year customer satisfaction with the services that we provide remains strong.

We are helping more customers struggling to pay their bills than ever before through our extensive support schemes and acted swiftly during the early stages of the pandemic to increase eligibility for our social tariff. We contributed an additional £2.7 million from the Trust Fund to help those struggling to pay their bills and a further £15 million was made available to help customers reduce their water bill to an affordable amount through extending our social tariff. We recognise that we are a unique position to make a real, positive contribution to society and have an ambitious and innovative approach to addressing affordability and vulnerability.

Our ongoing charitable support has helped provide support to local communities. One of our donations to the FareShare charity has supported them in delivering 600,000 meals to struggling families across the North West via local foodbanks, and will replace one of the charity's delivery vans, helping to ensure 6.4 million meals get to families in need over the next eight years.

Our activities support thousands of jobs in the supply chain, all of which play a part in helping to generate jobs and income for the North West economy. This is even more important this year as the country emerges from the worst effects of the Covid pandemic. Suppliers play an important role in maintaining supply for key parts of our business, and contractors, as well as direct employees, act as the face of our business for many customers and communities. We have been working closely with our supply chain partners following Government guidelines to protect employees, suppliers and customers while maintaining delivery of the critical services that we provide. We act in a fair and transparent manner with our all our suppliers and are a signatory of the Prompt Payment Code, paying over 99% of our invoices within 60 days during the first year of AMP7. In November 2020 we launched a new approach called United Supply Chain, which recognises suppliers as an extension of the United Utilities family and asked them to become a signatory to our responsible sourcing principles as a minimum. We encourage those suppliers who are integral to our operations, to become leaders and to work jointly with us to deliver improvements across environmental, social and governance areas and improve value to customers. At the end of March 38% of our targeted suppliers have signed up to the approach which will help us to deliver improvements across environmental, social and governance performance and deliver benefits to customers.

Our purpose drives us to deliver our services in an environmentally sustainable, economically beneficial and socially responsible manner and what we do creates a deep connection with the customers and stakeholders we serve. We achieved our climate changes objectives up to 2020, reducing greenhouse gas emissions by 73% from a 2005/06 baseline and we have made good progress in achieving our six carbon pledges. This year we have utilised 100% renewable electricity though our self-generation and purchasing of green energy. Our Catchment Systems

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Thinking (CaST) approach continues to mature, delivering partnership based solutions in key catchments in the region. We have been working with the Environment Agency (EA) and other stakeholders to develop a North West natural capital baseline and once this process is complete, we will engage with other partners across the region to drive a consistent approach to delivering greater natural capital value. This year, we pledged a £300,000 CaST Fund, for which charities and community groups are able to bid, in order to boost the idea of working collaboratively to address the challenges facing the environment.

Overall, the board considers that the company has responded well to the continued challenges faced in delivering our services to customers throughout the Covid pandemic. Our teams have addressed the unprecedented challenges of the last year, providing a largely seamless service to customers, whilst delivering high levels of customer satisfaction and resilient services in times of significantly increased demand.

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Providing great water and more for the North West

Thinking about the 'more'

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 most likely be 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 2020/21 S172 (1) Statement can be found on page 20.

Incorporating sustainability in our stewardship

Historically, a board's success criteria has primarily been judged on the company's financial performance and while this is still fundamental, boards of companies are now encouraged to adopt a more holistic approach to their stewardship. It is the responsibility of the directors to exercise their judgement, balancing the use of the company's resources to ensure its sustainable long-term success, and at times, the requirements and criteria for assessing our success by our different stakeholder groups will be in competition. Sustainability is a key component of the way in which we manage our business. We set out on page 23 how we create value for our stakeholders. Our board governance ethos, our culture and the way we operate as a business is to behave responsibly towards all our 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 conference call 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 63 to 82.

Working with our regulators – responding responsibly to the 'green recovery' in our region

As a business, we are aware of the importance of our financial contribution to the North West economy. The board was keen to respond to the Government's green recovery challenge and play our part, by putting forward a programme of work that we believe is achievable and which will not generate an unnecessary risk for the company. Consideration of our green recovery proposal is included in the statement by the directors in performance of their statutory duties in accordance with S172 (1) of the Act set out on page 20.

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Diversity and inclusion

We recognise that we need fantastic people to enable us to deliver a great service now and to ensure the long-term sustainable success of the business. We have to reach and recruit from every part of our community and to support our employees to achieve their full potential and feel valued and included, regardless of their gender, age, race, disability, sexual orientation or social background. We acknowledge that it will be a challenge to make significant step changes quickly in the workforce with low levels of attrition, regional variations in demographics and difficulties in recruiting females to STEM roles.

Working with a specialist inclusion partner we have updated our employee diversity and inclusion plan to drive our changes. We plan to set targets for the next 12 months based on the implementation of enabling activities before moving to comprehensive representation targets once we have understood our employee data and we will assess our progress with a further maturity audit.

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 mechanism (ODI), customer measure of experience (C-MeX) and financing expenditure (see pages 43 to 54) 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 83 to 87.

UUW board activity in 2020/21

Customer

- Considered and approved the publication and submission to Ofwat of 2021/22 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 the company's response to Covid-19 in relation to its stakeholders and approved an interim social tariff extension until 2021/22;
- Regular review and monitoring of the company's operational response and performance in relation to the 2020/21 extreme weather events, particularly the water resources challenges in the summer of 2020 and Storms Christoph and Darcy in January and February 2021 respectively;
- Met with representatives of YourVoice, the company's customer challenge group, discussing the ongoing work with the company, YourVoice's assurance on the 2020 annual performance report;
- Reviewed and discussed developments in cyber crime and the activities undertaken to enhance the effectiveness of the company' security controls;
- 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 and approval of funding for the company to deliver the programme via the Direct Procurement for Customers approach and noted the successful completion in

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November 2020 of the replacement of the Hallbank section of the Haweswater Aqueduct, as a preliminary stage of the programme;

- 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 an update on the progress of embedding the 'home safe and well' health and safety culture within the business. Further development and implementation of employee wellbeing policies and activities has been major focus throughout the year;
- 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;

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 UUW's DWI water quality performance;
- Received updates on the Environment Agency's performance assessment;
- Reviewed and accepted modifications to Licence Conditions;
- Noted changes as a result of the Ofwat Wholesale-Retail Market Code consultation;
- Reviewed and discussed communications received from Ofwat, the Environment Agency and the Drinking Water Inspectorate; and
- Considered an approach from Defra and proposed a plan of work to Ofwat to accelerate investment to deliver 'green' initiatives that would both benefit the environment and support the economic recovery for the COVID-19 pandemic

Governance

- Granted powers of attorney to senior managers in relation to treasury and property related matters;
- Review of Ofwat's report on how companies met the board leadership, transparency and governance principles which became effective from 1 April 2019;
- Approved the appointment of Phil Aspin as Chief Financial Officer with effect from 24 July 2020 and Kath Cates and Doug Well as independent non-executive directors with effect from 1 September 2020;
- Reviewed and discussed the external evaluation of the board;
- Reviewed and approved the slavery and human trafficking statement; and
- Adoption of new articles of association.

Financial

- Reviewed and approved UUW's proposed treasury activities for 2020/21;
- Considered and agreed that the 'base' dividend, as set out in the company's dividend policy for the 2020-25 regulatory period, would not be paid to the company's shareholder for the financial year 2020/21.;
- Approved the company's annual report and financial statements;
- Approved the company's business plan for 2021/22;

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- 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;
- Regular review of the progress of Water Plus Group Limited, the joint venture with Severn Trent serving commercial customers and approval of the restructuring and increase in working capital facilities of Water Plus aligning with those provided by the joint venture partner, reflecting the challenges to the business relating to the COVID-19 pandemic; and
- Approval of the redemption of 130,000,000 7 per cent redeemable preference shares and capitalising the capital redemption reserve in full, applying such sum in paying up in full a bonus issue of 130,000,000 ordinary shares of £1.00 each ranking pari passu with the existing ordinary shares in the capital of the company.

Purpose, values and strategy

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 2021, 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. Key to this is taking action to address any issues where there is misalignment with the company's culture. 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 action.

Culture and employee engagement

Our employees are at the heart of the culture of our business and further insight and evidence, as part of the board's assessment and monitoring of culture, has been gathered, and fed back to the board by Alison Goligher, the current designated non-executive director for engagement with the workforce.

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, it was recognised that the panel needed to meet more frequently during such a challenging period.

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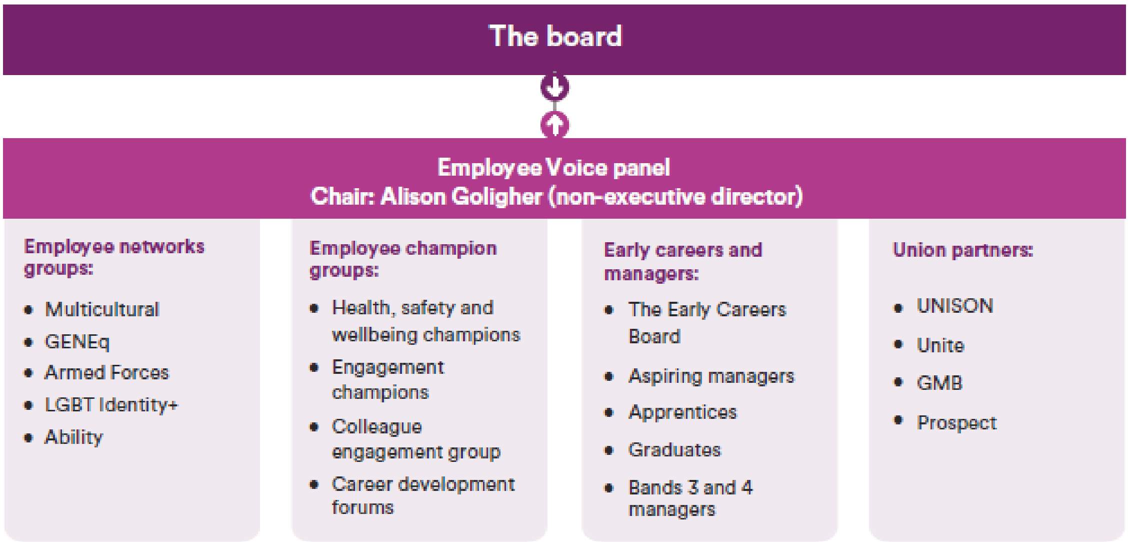

Members of the panel rotate approximately every two years. There is an open invitation to all board members to attend meetings of the panel. When the panel was established, the intention was to hold physical meetings, rotating around different operational and office locations, in order to encourage participation and enable colleagues to get a different perspective on working for the company; and enabling Alison to have first-hand experience of different company sites and gain a view of the company at 'grass-roots' level. However, due to the pandemic, all four meetings were held virtually. This did prove to be particularly beneficial to colleagues in operational roles, who found it much easier to attend panel meetings. Terms of reference were agreed when the panel was established along with the way in which the panel would operate. Such mechanisms will be reviewed in due course, particularly in relation to whether meetings will be held virtually.

Sub-groups, made up of panel members, have focused on specific aspects of the business, including cross-networks, culture and the employee engagement survey, providing updates at each meeting. The culture sub-group has focused its energies on obtaining a grass-roots view of 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. As part of the two-way communication, Alison provides updates to the panel from the perspective of the board and the corporate responsibility committee and she similarly provides feedback to the board and the committee on the work of the panel.

Listening to our employees

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 their work with the group for 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.

During the year, a virtual all employee engagement day was held which was very well received by those who attended. Set out on page 15 is the company's approach to our engagement with

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and creating value for employees, with health, safety and well-being 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 172 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 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, customer services and people director, head of internal audit and commercial 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 other stakeholder representatives including: Ofwat and YourVoice (the independent customer challenge group). Indeed, the chair of YourVoice regularly attends parts of UUW board meetings 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 14 to 19.

The stakeholder metrics table (see pages 44 to 54) provides data on a number of stakeholder and cultural indicators.

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 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 Euro Medium Term Note Programme, which gives us access to the sterling and euro public bond markets and privately arranged note issues. Committed credit facilities are arranged with our relationship banks on a bilateral basis. Additionally, the European Investment Bank (EIB), which is the financing arm of the European Union (EU), remains a significant lender to United Utilities Water, currently providing around £1.1 billion of loan funding supporting past capital investment programmes.

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Given that the UK left the EU on 31 January 2020, we are unlikely to obtain future funding from the EIB under its existing mandate, with our existing loan portfolio with the EIB entering into '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, and during the year the group raised a total of £725 million of term funding in the sterling public bond market, including our first sustainable bond of £300 million with a maturity date of October 2029, and paying a coupon of 0.875 per cent. The bond was issued under the group's sustainable finance framework established in November 2020.

The group currently has gross borrowings of circa £8,452 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 and the EIB and the credit rating agencies. More information can be found on our website at **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 2020/21 financial year.

Chairman of the board

The role and behaviour of the Chairman 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 Chairman 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 Chairman, 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. It is also the role of the Chairman, again supported by the company secretary, to ensure that the directors receive accurate, timely and clear information. The Chairman 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.

Conflicts of interest and time commitment

The company's articles of association contain provisions which permit unconflicted directors to authorise conflict situations. Each director is required to notify the Chairman of any potential conflict or potential new appointment or directorship. 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 Chairman 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: Brian May appointed as a non-executive director at Ferguson plc; Mark Clare

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appointed as a non-executive director and chairman designate at Aggreko plc and as a non-executive director of Wickes Group plc; Alison Goligher as a non-executive director of Technip Energies NV and Kath Cates as a non-executive director of TP ICAP Group Plc.

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. In March 2021, although not a statutory directorship, Phil Aspin accepted a position on the UK Accounting Standards Endorsement Board (UKEB).

The directors are at all times fully mindful of the fact that they hold a directorship in both UUW and UUG. Steve Mogford and Phil Aspin have declared their directorships of Water Plus Limited as being a potential conflict of interest with the company. UUW and Water Plus Group Limited are, and operate as, distinct legal entities.

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.

Consideration of environmental and social issues are fundamental to the way in which we operate as a responsible business at United Utilities; such matters are central to board discussions (see the summary of board activity on UUG Annual Report pages 121 to 123 and the report of the corporate responsibility committee on pages 156 to 159). 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 interest 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 also received briefings from both Slaughter and May (legal and governance matters) and KPMG (governance changes relating to reporting requirements), along with a number of other advisers. Non-executive directors completed in-house online training courses on the Competition Act and the Bribery Act. A number of board members also attended a number of 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 understand the views of employees of the business. Paulette Rowe has contributed to the work on diversity and inclusion.

Induction of new non-executive directors

An induction programme is arranged for new non-executive directors, with programmes for Kath Cates and Doug Webb followed during the year. In addition, virtual one-to-one meetings with the Chairman and each of the existing non-executive directors were held. Furthermore, one to-one meetings were held with the CEO. Ordinarily, 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. New directors receive a briefing on the key duties of being a director of a regulated water company, including the role of the regulated company's holding company. They are required to meet with representatives of Ofwat prior to appointment.

Wider succession pipeline and talent management

For a number of years, we have had a written succession plan for our executive directors and other members of the executive team, which includes outline timescales. The plan identifies an interim internal successor to fill a role in the short term should the need arise, and the longer-

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term development needs of potential successors to be able to fulfil a role on a more permanent basis. As with all our board appointments, we would always aim to appoint the best person to fulfil a role. It would be common, when recruiting for a senior role, for an external search to be conducted alongside an internal candidate recruitment process.

Any changes that are required to the profile of the management team to reflect the changing needs of the business are considered by the board in the executive succession plan. Succession and development initiatives for senior executives include executive mentoring and coaching and/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. 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.

Fifty per cent of our executive team (excluding the CEO and CFO) is made up of women, and 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, BAME representation is 1.5 per cent. We are keen to develop our succession pipeline of female senior managers so that, over time, they can be considered for executive board appointments or as potential candidates for non-executive directorships in other companies. Our current talent programme at a senior level is well embedded and we believe a non-executive appointment for senior managers provides an excellent opportunity for both personal and career development. It is a way of gaining valuable experience that may be applied at United Utilities so long as no conflicts of interest occur.

Our graduate and apprentice programmes are thriving and we are focusing more effectively on middle/junior management succession.

Our gender pay data can be found on page 139 of the UUG Annual Report and Financial Statements. Historically, our industry has been male dominated, but we have measures in place to increase diversity in broad terms, including gender among our employees.

During the year, board directors have a number of opportunities to meet with members of the executive team, both formally when senior managers are required to present at board meetings on matters related to their responsibilities, and on more informal occasions. From time to time, board members have the opportunity to attend events and meet with members of the apprentice and graduate population and other employees identified as potential talent within the business.

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 in everything we do. It naturally flows through into our approach to the integrity of our financial reporting. Recognising that climate change is a key risk to our provision of water and wastewater services, 2020/21 is the second year that we have reported against TCFD. As part of the processes supporting the board's conclusion that the 2020/21 annual report and financial statements gives a fair, balanced and understandable assessment of the company's position and prospects, we took into account the existing processes of review and assurance of our TCFD and wider narrative reporting. We intend to further review the assurance processes of ESG matters, particularly those relating to TCFD reporting, ahead of this becoming a mandatory reporting requirement.

Board's approach to risk management and internal control

The board discharges its responsibility for determining the nature and extent of the risks that it is willing to take to achieve its strategic objectives through the risk appetite framework. As a key part of the risk management framework, risk appetite captures the board's desire to take and manage risk relative to the company's obligations, stakeholder interests and the capacity and capability of our key resources.

The board is also responsible for ensuring that the company's risk management and internal control systems are effectively managed across the business and that they receive an appropriate level of scrutiny and board time.

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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 risk that underpins our core operations and provision of water and wastewater services to customers.

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 158.

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 2028.

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 page 40 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 price and in a responsible manner over the longer term, underpinning our business model set out on pages 23 to 43.

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 the possible ongoing impact of the COVID-19 pandemic 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 83 to 97. 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 revenue variations, and expectations of future performance taking account of past performance in delivering for customers.

The viability assessment is performed on a standalone basis in relation to the United Utilities Water Limited group. The group is part of the United Utilities group[1]. The regulated activities of the United Utilities Water Limited group represent 98% of the total assets of the United Utilities group as a whole, which taken together with the financial resources and interests of the regulated business being robustly ring-fenced, means there is minimal risk from the non-regulated activities.

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

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[1] United Utilities Group PLC and its subsidiary undertakings

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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 £1.1 billion of available liquidity at March 2021 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 c[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 83 to 97. The baseline plan against which the viability assessment has been performed incorporates the estimated ongoing impact COVID-19 based on experience to date. This baseline plan is then subject to further stress scenarios and reverse stress testing that takes into account the potential impact of 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 63 to 82; political and regulatory risks; the risk of critical asset failure; significant cyber security breaches; longer term economic impacts resulting from COVID-19, including unemployment and corporate failures affecting debt collection and lower inflation affecting revenues, financing costs and RCV; and the potential for a restriction to the availability of financing resulting from a capital markets crisis. The UK's withdrawal from the EU and the ending of the transition period has not had a material adverse operational or financial impact on the group to date, and is not considered to represent a significant risk to the group's ongoing viability.

The scenarios considered are underpinned by the group's established risk management processes, taking into account those risks with a greater than 10% (1 in 10) cumulative likelihood of occurrence. The risks associated with COVID-19 are reflected within the baseline

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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	Example mitigations (none required)
Scenario 1: Totex £400m one-off impact in 2021/22	Broadly representing the largest 'severe but reasonable' risk which is a critical asset failure, all assumed to be operating costs	• Issuing new finance • Equity injection from parent • Closing out derivative asset positions
Scenario 2: Totex underperformance of 10% (c£120m) per annum for 2021/22-2027/28	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)	• Reduction in discretionary totex spend • Restriction of dividends • Capital programme deferral • Issuing new finance
Scenario 3: CPIH inflation of 1.0% below baseline plan for 2021/22-2027/28	Consistent with quantum of inflation impacts modelled within top 10 severe but reasonable risks 'Financial outperformance'	• Reduction in discretionary totex spend • Restriction of dividends • Equity injection from parent
Scenario 4: An increase in bad debt of £15m per annum across AMP7	Aligned to internal risk factor on debt collection. Slightly higher than the level of improvement in household statutory bad debt in AMP6	• Reduction in discretionary totex spend
Scenario 5: Additional ODI penalty of 1.0% RORE (c£50m) per annum	Assumes mid-point of UUW's baseline and FD P90 ODI position	• Reduction in discretionary totex spend • Restriction of dividends
Scenario 6: Combined scenario – 50% of scenarios 2-5	50% of scenarios 2-5	• Reduction in discretionary totex spend • Restriction of dividends • Capital programme deferral • Issuing new finance

The above scenarios reflect our company specific risks and risk mitigation strategies whilst having consideration to the 'common scenarios' prescribed by Ofwat for PR19.

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.

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The most extreme of the severe but reasonable scenarios modelled, without any mitigating action, resulted in: UUW comfortably retaining investment grade credit ratings; liquidity of > 1 year; and no projected breaches of financial debt covenants.

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.

These mitigations could cover a number of different extreme scenarios. For example, to mitigate against a large one-off impact (such as in scenario 2 – £400m 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 – recurring totex overspend, scenario 5 - ODI underperformance or scenario 3 - persisting low CPIH inflation) mitigations such as the restriction of dividend payments or a reduction in discretionary totex spend are viable alternative options. A mapping of some of the key mitigations which could apply to each scenario have been presented in the table on the previous page. However, it should be stressed that no specific mitigating action are required under any of the six scenarios modelled above.

Viability period of seven years

In determining the viability assessment period, the board had regard for the increasing level of uncertainty as the duration of the assessment period is extended and the desire to maintain a robust viability assessment. Notwithstanding the ongoing uncertainty arising from the ongoing COVID-19 pandemic, the board concluded that retaining an assessment period of seven years was appropriate.

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.

Significant issues considered in relation to the financial statements

With regard to the UUW financial statements the UUG audit committee and the UUW board reviewed a number of principal areas of judgement. These are disclosed on pages 152 to 153 of the UUG 2021 annual report and are all applicable to UUW with the exception of accounting for loans to the Water Plus joint venture, and accounting for the disposal of the UUG group's stake in its joint venture, AS Tallinna Vesi (Tallinn Water).

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 150 to 151 of the UUG 2021 annual

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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 page 150 of the UUG 2021 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.

Licence obligations

The board receives reports about the performance of the company, and during the year approved the 2020 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

The effectiveness of the internal audit function's work is continually monitored using a variety of inputs, including the ongoing audit reports received, the UUG 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 UUG audit 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. The UUG audit committee has received regular updates during the year from the head of audit and risk on the impact of the pandemic on the schedule of work of the internal audit team, due to remote working and social distancing measures. Some re-phasing of the original work was undertaken, with the team keeping on track with re-planned work. Only one audit, which required access to a third party's site, was deferred, with agreement by the committee, to the 2021/22 audit plan.

Taking all these elements into account, the UUG audit 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 UUG audit committee, on behalf of the UUG and UUW boards, receives updates and reports from the head of audit and risk on key activities relating to the company's risk management systems and processes at every meeting. These are then reported to the board, as appropriate. The group designs its risk management activities to manage rather than eliminate the risk of failure to achieve its strategic objectives.

The CFO has executive responsibility for risk management and is supported in this role by the head of audit and risk and the corporate risk manager and his team. The group audit and risk board (GARB) is a sub-committee of the executive team. The GARB meets quarterly and reviews the governance processes and the effectiveness and performance of these processes along with the identification of emerging trends and themes within and across the business. The work of the GARB then feeds into the information and assurance processes of the audit committee and into the board's assessment of risk exposures and the strategies to manage these risks.

Supplementing the more detailed ongoing risk management activities within each business area, the biannual business unit risk assessment process (BURA) seeks to identify how well risk management is embedded across the different teams in the business. The BURA involves a

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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 to underpin the company's risk management process. The maturity of the risk management framework and its application across the business is assessed on an annual basis against a defined maturity model. This assessment provides an objective appraisal of the degree of maturity in how the risk management system is being applied and the quality of each risk in terms of quantification and management. The results of the maturity assessment are reported to the GARB, and actions agreed with business units.

An external assessment of the risk management process last took place in 2017/18.

The UUG audit committee received a 'deep dive' session on the risk management process. This provided an explanation of the process of identification and assessment of risk along with the governance mechanisms in place prior to the reporting of the risk profile to the board.

Anti-fraud and anti-bribery

The UUG 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, customer services and people director, commercial director and head of internal audit and risk) to decide on the appropriate course of action and investigation and by whom.

During the year, the UUG audit committee was kept fully appraised in regular updates on the progress and findings of investigations of cases of alleged fraud and any remedial actions taken. A number of employees have been selected and received specialist training in order to conduct investigations of cases of alleged fraud.

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. As part of the anti-bribery programme, employees are also required to comply with the group's hospitality policy. The hospitality policy permits employees to accept proportionate and reasonable hospitality for legitimate business purposes only. As part of the group's United Supply Chain approach our responsible resourcing principles explain that we will not tolerate corruption, bribery and anti-competitive actions and we expect our suppliers to comply with applicable laws and regulations, and in particular never to offer or accept any undue payment or other consideration, directly or indirectly, for the purposes of inducing any person or entity to act contrary to their prescribed duties.

As part of the internal control self-assessment checklist (part of the group's internal control processes), senior managers in consultation with their teams are required to confirm, among other things, that they have complied with the group's anti-bribery and hospitality policies. The anti-bribery programme is monitored and reviewed biannually by the UUG audit committee.

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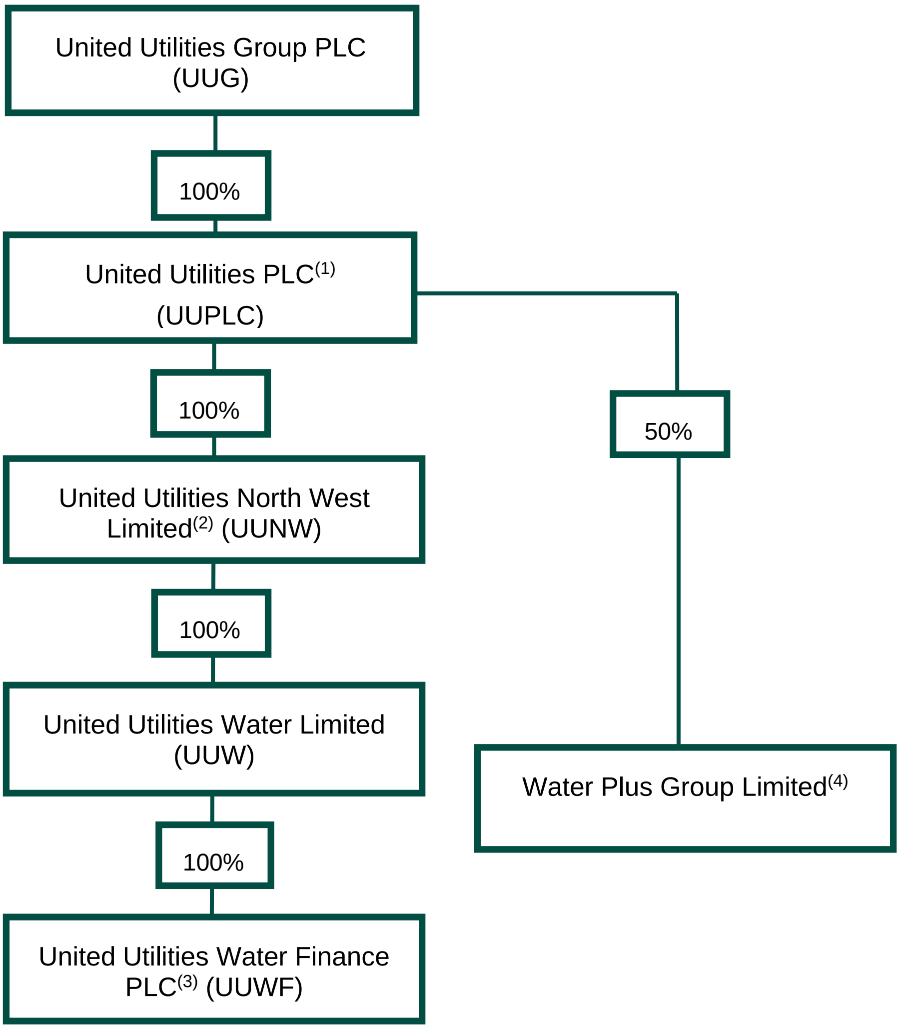
United Utilities group structure

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)(1) (which is also the holding company for a number of non-regulated and legacy/dormant companies) and United Utilities North West Limited (UUNW)(2). 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



(1)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.

(2)United Utilities North West Limited – previously held the electricity distribution business prior to its disposal in 2007 and is retained for legal purposes.

(3)United Utilities Water Finance PLC is used to raise debt finance in support of UUW.

(4)Water Plus Group Limited – 50 per cent joint venture with Severn Trent serving customers in the non-household (business) water and wastewater retail market.

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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 2020/21 (audited information)

	Base salary [1] £'000	Benefits £'000	Cash allowance in lieu of pension £'000	Bonus £'000	Long-term incentives [2] £'000	Total £'000
Steve Mogford	**736**	**30**	**171**	**824**	**1,179**	**2,940**
Russ Houlden	**139**	**8**	**36**	**174**	**579**	**936**
Phil Aspin	**275**	**13**	**33**	**293**	**89**	**703**

Note:

(1) Salary for Steve Mogford and Russ Houlden reflects a voluntary reduction of 20 per cent of salary for three months which was donated to charity.

(2) The long-term incentive amount is in respect of the Long Term Plan (LTP) award which was granted in June 2018 for which the outcome is based on performance over the three-year period from 1 April 2018 to 31 March 2021. 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 2021, and the awards for Steve Mogford and Russ Houlden will not vest until the end of an additional two-year holding period. Phil Aspin's award was granted prior to his appointment to the board and so no holding period applies. The shares under Russ Houlden's 2018 LTP award have been pro rated for time served in the performance period i.e. 28/36 months. For the purposes of this table the value of LTP awards has been calculated using an average UUG share price over the three-month period from 1 January 2021 to 31 March 2021 of 913.3 pence per share. This is higher 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.

(3) Salary, benefits, pension and annual bonus figures for Russ Houlden reflect part-year earnings and are for the period from 1 April 2020 to 31 July 2020 when his employment ended. He stepped down from the board on 24 July 2020.

(4) Salary, benefits, pension and annual bonus figures for Phil Aspin reflect part-year earnings and are for the period from 24 July 2020 when he was first appointed to the board. A bonus of around £53,000 was earned by Phil Aspin in respect of the period 1 April 2020 to 23 July 2020 prior to him joining the board. This is not included in the table.

A recharge of £221,000 during the year ended 31 March 2021 (2020: £274,000) was charged to other companies in the United Utilities group in relation to the provision of executive director services (£168,000 (2020: £219,000)) and non-executive director services (£53,000 (2020: £55,000)).

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Directors' remuneration report (continued)

2020/21 annual bonus (audited information)

Measure	Steve Mogford		Russ Houlden		Phil Aspin	
	Max. %	Actual %	Max. %	Actual %	Max. %	Actual %
Underlying operating profit	25.0	19.3	25.0	19.3	25.0	19.3
Customer service in year						
C-MeX ranking versus the other WASCs	10.0	7.5	10.0	7.5	10.0	7.5
Written compaints	10.0	0.0	10.0	0.0	10.0	0.0
Maintaining and enhancing services for customers						
Outcome delivery incentive (ODI) composite	35.0	35.0	35.0	35.0	35.0	35.0
Time, cost and quality of capital programme (TCQi)	20.0	20.0	20.0	20.0	20.0	20.0
Total as % bonus maximum	**100.0**	**81.8**	**100.0**	**81.8**	**100.0**	**81.8**
Total as % base salary	**130.0**	**106.3**	**130.0**	**106.3**	**130.0**	**106.3**
Total £'000		**824**		**174**[(1)]		**293**[(2)]

[(1)] This is the bonus earned by Russ Houlden until his date of leaving the company on 31 July 2020.

[(2)] This is the bonus earned by Phil Aspin since his appointment as CFO on 24 July 2020. A bonus of around £53,000 was earned by Phil in respect of the period 1 April 2020 to 23 July 2020 prior to him joining the board. This is not included in the table above.

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 2020/21 the performance measures, and achievement against those measures for UUG shares previously granted to UUW executive directors which vested in 2020/21, or whose performance period ended in 2020/21 are summarised below:

Performance measure	Weighting	Achievement
Relative total shareholder return (TSR) 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)
Sustainable dividends. Average underlying dividend cover over the part of the performance period up to the end of the regulatory period, with a dividend growth underpin of at least RPI in each of the years 2018/19 and 2019/20	33.3%	31.3% out of 33.3% (Actual)
Customer service excellence. Ranking for the year ended 31 March 2021 out of the 11 water and wastewater companies using a combined customer service measure comprising C-MeX performance and customer complaints	33.3%	25.0% out of 33.3% (Estimated)[1]
Total vesting		**89.6%**

[(1)] This is an estimate as the final outcome for the customer service excellence measure will not be known until the volume of written complaints received by other companies is published later in 2021.

Corporate governance report

Directors' remuneration report (continued)

Details of the number of UUG shares vesting and value of these shares which vested in 2020/21, or whose performance period ended in 2020/21, are as follows:

Director	Number of shares vesting	Value of shares vesting £'000
	2018 LTP[1]	**2018 LTP[2]**
Steve Mogford	129,065	1,179
Russ Houlden	63,437	579
Phil Aspin	9,753	89

(1) The 2018 Long Term Plan (LTP) awards were granted in June 2018 and performance was measured over the three-year period from 1 April 2018 to 31 March 2021. As they were executive directors when they were granted in 2018 the awards for Steve Mogford and Russ Houlden will normally vest in April 2023, following an additional two-year holding period. The unvested UUG shares will remain subject to withholding provisions during this two-year 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 UUG shares. The performance period started on 1 April 2017 and ended on 31 March 2021. The number and value of the vested 2017 LTP awards in the table above is estimated pending the final outcome of the customer service excellence measure, expected to be published in late summer 2020. Awards granted will normally vest in April 2022, following an additional two-year holding period. The awards accrue dividend equivalents.

(2) The value of the 2018 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 2021 to 31 March 2021 (913.3 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.

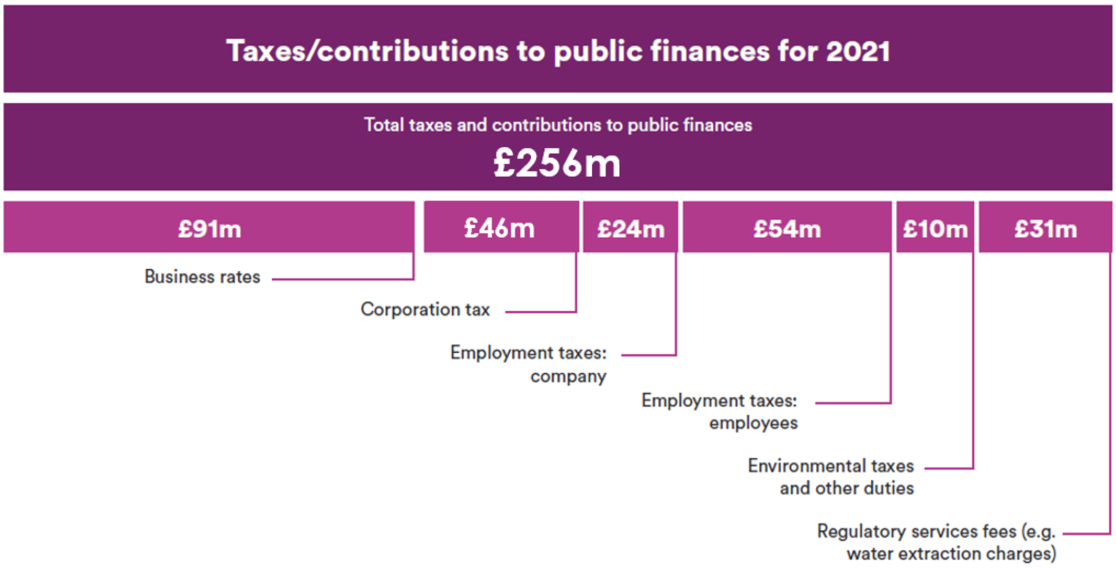
In any given year, the group’s effective cash tax rate on underlying profits may fluctuate from the standard UK rate mainly due to the available tax deductions on capital investment. These deductions are achieved as a result of utilising tax incentives, which have been explicitly put in place by successive 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 2020/21, 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 2021 of around £256 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 2021.

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 second 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 16 to 109 and the audited financial statements of United Utilities Group PLC (the company) and its subsidiaries (together referred to as the group) for the year ended 31 March 2021.

Business model

A description of the company's business model can be found within the strategic report on pages 23 to 43.

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").

Profit and dividends

The results for the year, set out in the consolidated income statement on page 153 how that profit for the year after tax was £410.1 million (2020: £135.9 million).

The directors have not recommended a final ordinary dividend (2020: £nil). No interim ordinary dividends have been declared or paid during the year (2020: £513.2 million).

Corporate governance statement

The corporate governance report on pages 104 to 135 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 83 to 97.

Share capital

At 31 March 2020, the issued ordinary share capital of the company was £230.0 million (2020: £100.0 million) divided into 230,000,000 ordinary shares of £1.00 each (2020: 100,000,000 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 £5,801 (2020:£23,627; 2019: £9,388) as part of this process. At the 2020 UUG AGM, an authority was taken to cover such expenditure. A similar resolution will be put to UUG shareholders at the 2021 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 2020/21, we received 379 contacts from MPs' offices covering topics such as flooding and planning. 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. In 2020, this was a virtual event in which over 40 MP representatives accepted to join us. For those unable to participate in the live event, a link was sent so it could be viewed when convenient. There are two devolved administrations in the North West – the Greater Manchester Combined Authority and the Liverpool City Region (LCR) – we engage regularly with both, 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 Greater Manchester 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, which considers industry-wide priorities such as development of markets, customer trust, resilience, and legislation and regulation, and the Confederation of British Industry, which provides a policy-making voice for firms at a regional, national and international level. Others focus on specific professions such as the 100 Group representing the views of the finance directors of FTSE 100 and large UK private companies and the GC 100, the voice of general counsel and company secretaries in FTSE 100 companies. The company is 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 2020/21 was £420,403 (2019/20: £400,916).

In the past 12 months, the company has been involved in several engagements with political stakeholders through its membership of trade associations. Through Water UK, the company has supported efforts to interact with parliamentary bodies, such as select committees and chairs of other specific committees, to provide information on topics such as water efficiency labelling for white goods and the performance of combined sewer overflows in relation to river water quality. The company has supported Water UK in its effort to encourage the Government to ensure its forthcoming Environment Bill supports the sector's objectives to deliver resilient water services now and into the future.

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 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 consultations and discussions as part of the unlocking regional growth/levelling

Directors' report

up agenda, bringing together views of industry and regional government on opportunities and barriers.

Employees

Our policies on employee consultation and on equal opportunities for all employees can be found on pages 32 and 34 of the UUG 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 24 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 20. 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 164.

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/. Our approach to engagement with our environmental stakeholders and those in the communities we serve can be found on pages 13 to 20. 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 20.

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 20. 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 20. 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/; 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 2021, our average time taken to pay invoices was 14 days; in the previous six months it was 14 days.

Energy and Carbon

Our TCFD reporting includes our energy and carbon report on pages 63 to 82 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 on page 193

Events occurring after the reporting period

Details of events after the reporting period are included in note 22 on page 184.

Directors' report

Slavery and human trafficking statement

Our slavery and human trafficking statement can be found on our website at: 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 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 2021 can be found on pages 98 to 103.

Non-executive directors

Sir David Higgins	
Stephen Carter	
Kath Cates	(appointed 1 September 2020)
Mark Clare	
Alison Goligher	
Brian May	
Paulette Rowe	
Doug Webb	(appointed 1 September 2020)
Sara Weller	(resigned 24 July 2020)

Executive directors

Phil Aspin	(appointed 24July 2020)
Russ Houlden	(resigned 24 July 2020)
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 aware, there is no relevant audit information of which the group's auditor is unaware; and
2. they 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 29 June 2021 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 Strategic Report, the Directors' 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 have elected to prepare the group and parent company financial statements in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006 and applicable law.

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 international accounting standards in conformity with the requirements of the Companies Act 2006;
- 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 29 June 2021 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 2021 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 2021 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006;
- the parent Company financial statements have been properly prepared in accordance with international accounting standards in conformity with the requirements of, and as applied in accordance with the provisions of, the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation to the extent applicable.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the audit committee.

We were first appointed as auditor by the shareholders on 22 July 2011. The period of total uninterrupted engagement is for the ten financial years ended 31 March 2021. 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

<table>
<tr><td colspan="2">Revenue recognition and allowance for household customer debt
Revenue not recognised: £27.1 million (2020: £19.4 million)
Provision for customer debts: £74.9 million (2020: £49.4 million)
Refer to pages 160 to 161 and 216 (accounting policies), and notes 2 and 11 (financial disclosures)</td></tr>
<tr><td>The Risk

Subjective estimate:

At each balance sheet date:

- 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

- assumptions involving a high degree of estimation uncertainty are required to assess the recoverability of trade receivables.

The effect of these matters is that, as part of our risk assessment, we determined that the recoverability of trade receivables has a high degree of estimation uncertainty in particular because of the potential effects of the COVID-19 pandemic, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. The financial statements (see pages 158 to 163 accounting policies) disclose the sensitivity estimated by the group.

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.</td>
<td>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:

Accounting analysis: assessing the derecognition of revenue for compliance with relevant accounting standards where the collection of consideration is not probable on the date of initial recognition;

Methodology choice: assessing 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;

Assessing transparency: assessing 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.

Our results

We found the amount of the revenue recognised to be acceptable (2020: acceptable);

We considered the level of doubtful debt provisioning to be acceptable (2020: acceptable).</td></tr>
<tr><td colspan="2">Capitalisation of costs relating to the capital programme
£677.5 million (2020: £759.5 million)
Refer to pages 162 and 217 to 219 (accounting policies) and note 9 (financial disclosures)</td></tr>
<tr><td>The Risk

Subjective classification:

The group has a substantial capital programme which has been agreed with the Water Services Regulation Authority (Ofwat)</td>
<td>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</td></tr>
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Independent auditor's report

to the members of United Utilities Water Limited

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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. Costs capitalised include an allocation of overhead costs, relating to the proportion of time spent by support function staff, which is based on assumptions involving a high degree of judgement.

The effect of these matters is that, as part of our risk assessment, we determined that the costs capitalised has a high degree of judgement, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. The financial statements (Accounting policies section) disclose the sensitivities estimated by the Group.

</td><td>

support reliance on controls.

Our procedures included:

Accounting analysis: assessing the group's capitalisation policy for compliance with relevant accounting standards;

Tests of details: critically assessing the capital nature of a sample of projects against the capitalisation policy focusing on new projects approved, project overspend, forecast cost to complete;

Tests of details: identified and critically assessed the impact of changes in capitalisation rate for a sample of specific cost centres; and challenged the estimates made by management on the specific cost centres for year-on year movements and rate changes.

Historical comparisons: critically assessed the proportion of capitalised overhead costs using historical comparisons and expected changes based upon enquiry and our sector knowledge;

Sensitivity analysis: assessed the impact of different capitalization rates and the impact to capitalized overhead costs;

Assessing transparency: assessed the adequacy of the group's disclosures of its capitalisation policy including the judgement involved in assessing expenditure as capital and the judgement relating to the allocation of overhead costs.

Our results:

We found the group's classification of expenditure as capital or operating to be acceptable (2020: acceptable).

</td></tr>
<tr><td colspan="2">

Valuation of retirement benefit obligations
£2,435.3 million (2020: £2,256.5 million)
Refer to pages 162 and 222 (accounting policies) and notes 15 and A6 (financial disclosures)

</td></tr>
<tr><td>

The Risk

Subjective valuation:

The valuation of the retirement benefit obligations depends on a number of estimates, including the discount rates used to calculate

</td><td>

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

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Independent auditor's report

to the members of United Utilities Water Limited

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 (Accounting policies section) disclose the sensitivities estimated by the group.	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 (2020: acceptable).

Going concern

Going concern was included as a key audit matter in the prior period as a result of the uncertainty caused by the COVID-19 pandemic. However, there is now considered to be less uncertainty owing to the fact that the situation has moved on by a year and the group has continued to operate throughout. As a result, we have not assessed this as one of the most significant risks in our current year audit and, therefore, it is not separately identified as a key audit matter in our report this year.

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 £17.5 million (2020: £20 million), determined with reference to a benchmark of group profit before tax normalised to exclude net fair value gains or losses on debt and derivative instruments disclosed in note 6, of £434.3 million of which it represents 4.0% (2020: 4.1%). The group team performed procedures on the items excluded from normalised group profit before tax.

Materiality for the parent company financial statements as a whole was set at £17.0 million (2020: £19 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 3.9% (2020: 3.5%).

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% (2020: 75%) of materiality for the financial statements as a whole, which equates to £13.125m (2020: £15.0m) for the group and £12.75m (2020: £14.25m) 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 audit committee any corrected or uncorrected identified misstatements exceeding £0.5 million (2020: £0.5 million), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Of the group's two (2020: two) reporting components, we subjected two (2020: two) to full scope audits for Group purposes.

The work on all two components (2020: two) was conducted by the group team.

The Group team approved the component materialities, which ranged from £8 million to £17 million (2020: £8 million to £20 million) having regard to the mix of size and risk profile of the Group across the components.

During the course of the audit we held video and telephone conference meetings with each of two (2020: two) components.

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 the possible failure of the Haweswater water system resulting in a one-off totex impact.

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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 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. We assessed the completeness of the going concern disclosure.

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 gompany'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:

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- Enquiring of directors, the audit committee, internal audit and inspection of policy documentation as to the group's high level policies and procedures to prevent and detect fraud, including the internal audit function, and the group's channel for "whistleblowing", as well as whether they have knowledge of any actual, suspected or alleged fraud.
- Reading Board meeting minutes and audit committee/risk committee minutes relating to the ultimate parent, United Utilities Group PLC.
- Considering remuneration incentive schemes and performance targets for directors including Long Term Plan awards.

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, capitalisation of costs relating to the capital programme and valuation of retirement benefit obligations.

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 or treasury posted to unexpected or unrelated accounts.
- 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.

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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 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 strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the strategic report and the directors' report 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 those reports;
- in our opinion the information given in the strategic report and the directors' report 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

Independent auditor's report

to the members of United Utilities Water Limited

- 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.

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.

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
29 June 2021

Consolidated income statement

for the years ended 31 March

	Note	2021 £m	2020 £m
Revenue	2	1,797.6	1,849.9
Employee benefits expense	3	(158.4)	(157.6)
Other operating costs	4	(428.4)	(404.1)
Allowance for expected credit losses – trade and other receivables	4	(28.7)	(41.8)
Other income	4	3.7	3.6
Depreciation and amortisation expense	4	(419.3)	(480.2)
Infrastructure renewals expenditure		(164.8)	(143.0)
Total operating expenses		(1,195.9)	(1,223.1)
Operating profit		601.7	626.8
Investment income	5	18.6	18.7
Finance expense	6	(114.6)	(318.1)
Investment income and finance expense		(96.0)	(299.4)
Profit before tax		505.7	327.4
Current tax charge	7	(78.2)	(43.0)
Deferred tax charge	7	(17.4)	(148.5)
Tax	7	(95.6)	(191.5)
Profit after tax		410.1	135.9

All of the results shown above relate to continuing operations.

Consolidated statement of comprehensive income

for the years ended 31 March

	Note	2021 £m	2020 £m
Profit after tax		410.1	135.9
Other comprehensive income			
Items that may be reclassified to profit or loss in subsequent periods:			
Cash flow hedge effectiveness		9.3	(2.0)
Tax on items taken directly to equity	7	(1.8)	0.4
Other comprehensive income that may be reclassified to profit or loss		7.5	(1.6)
Items that will not be reclassified to profit or loss in subsequent periods:			
Remeasurement gains on defined benefit pension schemes	15	(62.3)	113.4
Change in credit assumptions for debt reported at fair value through profit or loss		(43.3)	34.2
Cost of hedging – cross-currency basis spread adjustment		(12.7)	1.3
Deferred tax adjustments in respect of prior years on net fair value gains		-	(2.4)
Tax on items taken directly to equity	7	30.3	(121.5)
Other comprehensive income that will not be reclassified to profit or loss		(88.0)	25.0
Total comprehensive income		329.6	159.3

Consolidated and company statement of financial position

at 31 March

Group and company

	Note	2021 £m	2020 £m
ASSETS			
Non-current assets			
Property, plant and equipment	9	11,732.3	11,445.0
Intangible assets	10	181.1	189.0
Investments	A1	0.1	0.1
Trade and other receivables	11	-	98.0
Retirement benefit surplus	15	531.0	579.1
Derivative financial instruments	A5	410.3	617.8
		12,854.8	12,929.0
Current assets			
Inventories		16.0	12.4
Trade and other receivables	11	224.8	281.5
Current tax asset		-	9.1
Cash and short-term deposits	12	648.6	501.8
Derivative financial instruments	A5	14.4	0.1
		903.8	804.9
Total assets		13,758.6	13,733.9
LIABILITIES			
Non-current liabilities			
Trade and other payables	18	(796.7)	(760.6)
Borrowings	13	(7,998.4)	(8,102.5)
Deferred tax liabilities	16	(1,384.6)	(1,393.0)
Derivative financial instruments	A5	(107.8)	(135.4)
		(10,287.5)	(10,391.5)
Current liabilities			
Trade and other payables	18	(318.3)	(323.8)
Borrowings	13	(717.1)	(926.4)
Current tax liabilities		(20.7)	-
Provisions	17	(11.1)	(16.4)
Derivative financial instruments	A5	(6.9)	(8.4)
		(1,074.1)	(1,275.0)
Total liabilities		(11,361.6)	(11,666.5)
Total net assets		2,397.0	2,067.4
EQUITY			
Capital and reserves attributable to equity holders of the company			
Share capital	20	230.0	100.0
Other reserves	19	6.6	9.4
Retained earnings		2,160.4	1,958.0
Shareholder's equity		2,397.0	2,067.4

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 29 June 2021, 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 2020	100.0	9.4	1,958.0	2,067.4
Profit after tax	-	-	410.1	410.1
Other comprehensive income				
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
Total comprehensive income	-	(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)	-	-	-	-
At 31 March 2021	230.0	6.6	2,160.4	2,397.0

Group and company

	Share capital £m	Other reserves* £m	Retained earnings £m	Total £m
At 1 April 2019	100.0	12.3	2,309.0	2,421.3
Profit after tax	-	-	135.9	135.9
Other comprehensive income				
Remeasurement gains on defined benefit pension schemes (see note 15)	-	-	113.4	113.4
Change in credit assumptions for debt reported at fair value through profit or loss	-	-	34.2	34.2
Cash flow hedge effectiveness	-	(2.0)	-	(2.0)
Cost of hedging – cross-currency basis spread adjustment	-	1.3	-	1.3
Deferred tax adjustments in respect of prior years on net fair value gains	-	(2.4)	-	(2.4)
Tax on items taken directly to equity (see note 7)	-	0.2	(121.3)	(121.1)
Total comprehensive income	-	(2.9)	162.2	159.3
Dividends (see note 8)	-	-	(513.2)	(513.2)
At 31 March 2020	100.0	9.4	1,958.0	2,067.4

* 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	2021 £m	2020 £m
Operating activities			
Cash generated from operations	A2	1,122.8	1,032.1
Interest paid		(142.5)	(159.0)
Interest received and similar income		6.3	10.1
Tax paid		(72.6)	(76.9)
Tax received		26.9	15.8
Net cash generated from operating activities		940.9	822.1
Investing activities			
Purchase of property, plant and equipment		(604.5)	(643.7)
Purchase of intangible assets		(33.6)	(27.2)
Grants and contributions received	18	5.0	34.7
Repayment of loans to joint ventures	A7	-	2.0
Net cash used in investing activities		(633.1)	(634.2)
Financing activities			
Proceeds from borrowings net of issuance costs		1,605.1	1,096.3
Repayment of borrowings		(1,762.1)	(595.7)
Dividends paid to equity holders of the company	8	-	(513.2)
Net (used in)/cash from financing activities		(157.0)	(12.6)
Net increase in cash equivalents		150.8	175.3
Cash and cash equivalents at beginning of the year		487.7	312.4
Cash and cash equivalents at end of the year	12	638.5	487.7

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 International Financial Reporting Standards (IFRSs) as adopted in the United Kingdom (UK). They have been prepared on the historical cost basis, except for the revaluation of financial instruments, accounting for the transfer of assets from customers and the revaluation of infrastructure assets to fair value on transition to IFRS.

The preparation of financial statements, in conformity with IFRS requires management to make estimates and assumptions that affect the amounts of assets and liabilities at the date of the financial statements and the amounts of revenues and expenses during the reporting periods presented. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from these estimates.

The financial statements have been prepared on the going concern basis as the directors have a reasonable expectation that the group has adequate resources for a period of at least 12 months from the date of the approval of the financial statements, and that there are no material uncertainties to disclose.

In assessing the appropriateness of the going concern basis of accounting the directors have reviewed the resources available to the group 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 the expected impacts of COVID-19. 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 group's ability to operate within the amount 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 group 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 considered indicate that the group will be able to operate within the amount 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

The following standards, interpretations and amendments, effective for the year ended 31 March 2021, have had no material impact on the group's financial statements:

- Amendments to IFRS 3 'Definition of a Business' (issued on 22 October 2018);
- Amendments were made to IAS 1 and IAS 8 'Definition of Material' (issued on 31 October 2018);

The IASB issued its revised Conceptual Framework in March 2018 which is mandatory for annual reporting periods beginning on or after 1 January 2020. It is not a standard and does not override any standard, but its principles apply to arrangements not covered by IFRS standards. No arrangements have been identified by the group which require a change in accounting treatment under the revised Conceptual Framework.

Accounting policies

Early adopted new and revised standards

'Phase Two' – 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 Two' IBOR Reform).

The amendments address the financial reporting impact from reform of the London Interbank Offered Rate (LIBOR) and similar benchmark interest rates (IBOR Reform). The Bank of England has asked UK market participants to complete the transition to alternative risk-free rates by the end of 2021, with the industry-led Working Group on Sterling Risk-Free Reference Rates having previously recommended the Sterling Overnight Index Average (SONIA) as the preferred risk-free rate in sterling markets.

The group chose to early-adopt the Phase Two reforms for the year ended 31 March 2021, though this has had no impact on the financial statements for the year then ended. When applicable, the group will take 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.

At 31 March 2021, the group had a net balance of £591.3 million relating to financial instruments, along with an additional £700.0 million of undrawn committed facilities, still referencing LIBOR. Detail on the derivation of this net balance can be found in note A4, along with further information on the group's transition to alternative benchmarks. This figure is inclusive of £2,117.8 million nominal value of swaps designated within fair value hedging relationships.

These Phase Two amendments will be applicable on modification of the instruments to be linked to the alternative risk-free rate, as well as when changes to the fair value hedges are required as a result of the reform. The reliefs provided for in this amendment mean that on transition to the new risk-free rate, no one-off charge or credit to the income statement will be recognised, provided the transition has occurred on an economically equivalent basis. The amendments also mean that the group expects no discontinuation of hedge accounting to be required on transition to the new interest rate benchmarks, with modifications to the documentation permitted, provided these are directly related to the IBOR reform.

The group has previously adopted 'Phase One' – Amendments to IFRS 9 and IFRS 7 - Interest rate benchmark reform, which allowed temporary relief from applying specific hedge accounting requirements to hedging arrangements directly impacted by IBOR reform. This temporary relief is expected to cease, on a hedge-by-hedge basis, when the designated hedge relationship is amended and application of Phase Two reliefs begins.

As a result of the relief, the group expects that no material gain or loss will arise from the replacement of LIBOR with an alternative risk-free rate.

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

Accounting policies

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 under IFRS, including specific considerations in light of the COVID-19 pandemic.

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:

The customer has not paid their bills for a period of at least two years; and

The customer has paid their bills in the preceding two years; however, has previously had statements de-recognised and has more than their current year debt outstanding.

This two-criteria approach resulted in £21.1 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 £7.9 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, amongst 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 2021, the allowance for doubtful receivables relating to household customer debt of £74.9 million was supported by a six-year cash collection projection. Based on a five-year or seven-year cash collection projection the allowance for doubtful receivables would have increased by £1.3 million or reduced by £0.6 million respectively.

At the prior year balance sheet date, the expected future impact of the Covid-19 pandemic on the ability of some customers to pay their bills was specifically been taken into consideration as part of the expected credit loss assessment for trade receivables. This gave rise to a further £16.7 million incremental increase in the allowance for expected credit losses based on judgements around the likely impact of the pandemic on the non-payment risk profile of the group’s customer base on a segmented basis.

A high level of uncertainty remains around how current economic conditions could impact the recoverability of household receivables, particularly in light of further lockdowns during the year. As government support schemes such as furlough unwind, this could result in increased unemployment and therefore further impact the ability of some customers to pay.

In recognition of this future uncertainty, the allowance for expected credit losses covering the group’s household customer base has been determined based on the assumption that cash collection experienced over the last two years continues into the future. This assumption

Accounting policies

supports the reported household bad debt charge of 2.2 per cent of household revenue and is considered to be a reasonable estimate of future collection. Had the group assumed that future collection was maintained at levels experienced during the last 12 months alone, the charge would have been increased by £2.6 million to 2.4 per cent of household revenue. If the group had assumed that future collection improved to an average of actual collection experienced over the last 3 years, then the bad debt charge would have reduced by £3.8 million to 1.8% of household revenue.

Accounting estimate – The company 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 date of the last meter reading and the billing date. Meters are read on a cyclical basis and the group recognises revenue for unbilled amounts based on estimated usage from the last billing through to each reporting date. The estimated usage is based on historical data, judgement and assumptions; actual results could differ from these estimates, which would result in operating revenues being adjusted in the period that the revision to the estimates is determined.

Revenue recognised for unbilled amounts for these customers at 31 March 2021 was £69.4 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 £4.8 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. Consumption patterns during the year have been significantly impacted by changes brought about by the COVID-19 pandemic, with household consumption having been above levels normally seen due to customers spending more time at home. As the year has progressed, the volume of household meter reads has gradually increased, resulting in the increased consumption during the pandemic period largely being captured in actual bills meaning that the level of estimation has reduced. By 31 March 2021, the system generated accrual had largely aligned to the independent automated meter read (AMR) data. AMR data is captured for around 25 per cent of all measured household customers, and this increase has been extrapolated across the remaining measured household customer base. The reasonableness of this approach has been validated through an assessment of bills raised in the period.

Accounting estimate – Due to temporary business closures required as a result of lockdown measures introduced by the UK Government, the level of non-household consumption has fallen significantly throughout the year ended 31 March 2021. Revenue in relation to wholesale charges billed to non-household retailers is recognised based on a series of settlement statements produced by the Central Market Operating System (CMOS), operated by Market Operator Services Ltd (MOSL). When generating bills in the absence of a current meter read, CMOS uses the 12 months prior to the last meter read to assess expected consumption. Depending on when a meter was last read, the calculated volumetric charge may not be wholly reflective of the consumption during the period estimated due to the impact that Covid-19 has had on different industries in the year. In recognition of this issue, MOSL advised non-household retailers in December 2020 that they should consider the trading status of their customers and amend their Yearly Volume Estimate to adjust the wholesale charges calculated by CMOS. The group has performed its own estimations of the adjustments required to these charges determined by CMOS, and has accrued for an additional £13.9 million of revenue in the year relating to non-household wholesale charges. This adjustment is based on an analysis of volume supplied for each particular end user at a supply point level, and comparing this with estimates in the CMOS system. Had this accrued income simply been based on the estimates calculated by CMOS, revenue would therefore have been £13.9 million lower, though based on the volumetric analysis performed management considers that this position would be overly prudent.

Accounting policies

Property, plant and equipment

Accounting judgement - the group recognises property, plant and equipment (PPE) on its water and wastewater infrastructure assets where such expenditure enhances or increases the capacity of the network, whereas any expenditure classed as maintenance is expensed in the period it is incurred. Determining enhancement from maintenance expenditure requires an accounting judgement, particularly when projects have both elements within them. Enhancement spend was 58 per cent of total spend in relation to infrastructure assets during the year. A change of +/- one per cent would have resulted in £4.0 million less/more expenditure being charged to the income statement during the period. In addition, management capitalises time and resources incurred by the group's support functions on capital programmes, which requires accounting judgements to be made in relation to the appropriate capitalisation rates. Support costs allocated to PPE represent 37 per cent of total support costs. A change in allocation of +/- 5 per cent would have resulted in £2.1 million less/more expenditure being charged to the income statement during the period.

Accounting estimate - the estimated useful economic lives of PPE and intangible assets is based on management's experience. When management identifies that actual useful economic lives differ materially from the estimates used to calculate depreciation, that charge is adjusted prospectively. Due to the significance of PPE and intangibles investment to the group, variations between actual and estimated useful economic lives could impact operating results both positively and negatively. As such this is a key source of estimation uncertainty. The depreciation and amortisation expense for the year was £419.3 million. A 10 per cent increase in average asset lives would have resulted in a £39.2 million reduction in this figure and a 10 per cent decrease in average asset lives would have resulted in a £46.0 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 £222.0 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 2021. 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.

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.

Accounting policies

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. In recent years depreciation was accelerated on a material value of bioresource facilities which were to be decommissioned in part as a result of the group's decarbonisation strategy. Following a robust series of asset life reviews in the period, no such material charges were deemed required for the year ended 31 March 2021.

The group is exposed to potential asset write-downs following flooding resulting from storms and other such 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.

The group has looked to further enhance the accuracy of its useful life assessment through the introduction of more forward-looking information in asset life reviews. This includes the use of data from the Pioneer Strategic Asset Planning System to assess the economic point of replacement for assets under future investment and performance scenarios. This information is to be used alongside other decommissioning data to inform useful economic 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.

	2021 £m	2020 £m
Wholesale water charges	751.0	784.8
Wholesale wastewater charges	941.5	939.5
Household retail charges	64.1	83.8
Other	41.0	41.8
	1,797.6	1,849.9

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

	2021 £m	2020 £m
Fees to non-executive directors	0.8	0.8
Salaries	1.2	1.4
Benefits	0.2	0.3
Bonus	0.7	0.7
Share-based payment charge	1.7	1.0
	4.6	4.2

Included within the above are aggregate emoluments of £2.5 million (2020: £1.9 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 2021 (2020: £0.3 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 (2020: two directors) received shares in United Utilities Group PLC in respect of qualifying services. Three directors (2020: two directors) had long-term incentive plans which vested during the year. Aggregate amounts receivable relating to long-term incentive plans of £1.8 million (2020: £1.6 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

	2021 £m	2020 £m
Salaries and short-term employee benefits	5.2	6.4
Share-based payment charge	3.1	1.3
	8.3	7.7

Key management personnel comprises all directors and certain senior managers who are members of the executive team.

Employee benefits expense (including directors)

	2021 £m	2020 £m
Wages and salaries	240.1	229.5
Employee-related taxes and levies	25.2	23.8
Severance	1.3	7.2
Post-employment benefits:		
Defined benefit pension expense (see note 15)	7.0	10.2
Defined contribution pension expense (see note 15)	23.4	22.4
Employee benefits expense before recharges	297.0	293.1
Amounts recharged to parent and fellow subsidiary companies	(1.7)	(1.6)
Charged to other areas including regulatory capital schemes	(136.9)	(133.9)
Employee benefits expense	158.4	157.6

Included within employee benefits expense there were £1.7 million (2020: £10.8 million) of restructuring costs.

A recharge of £1.7 million during the year ended 31 March 2021 (2020: £1.6 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 2021 UUG annual report and financial statements. Included within wages and salaries is an expense of £3.4 million (2020: £1.4 million) relating to a recharge of share-based payment costs from the ultimate parent undertaking (see note A7).

Notes to the financial statements

3. Directors and employees (continued)

Average number of employees during the year (full time equivalent including directors)

	2021 number	2020 number
Average number of employees during the year	5,158	5,091

The 2021 total employee benefits expense, before recharges, of £297.0 million (2020: £293.1 million) includes the employee costs relating to the persons employed during the year noted above in addition to costs of £17.8 million (2020: £17.0 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 196 (2020: 211).

4. Operating profit

	2021 £m	2020 £m
Other operating costs		
Hired and contracted services	96.0	95.9
Property rates	89.4	75.8
Power	88.2	82.7
Materials	81.8	74.7
Regulatory fees	28.0	28.3
Loss on disposal of property, plant and equipment and intangibles	8.4	13.9
Accrued innovation costs	6.2	-
Other expenses	30.4	32.8
	428.4	404.1
Allowance for expected credit losses – trade and other receivables		
Allowance for expected credit losses – trade and other receivables (see note 11)	28.7	41.8
	28.7	41.8
Other income		
Other income	(3.7)	(3.6)
	(3.7)	(3.6)
Depreciation and amortisation expense		
Depreciation of property, plant and equipment (see note 9)	376.8	439.0
Amortisation of intangible assets (see note 10)	42.5	41.2
	419.3	480.2

Included within depreciation of property, plant and equipment was £2.3 million of accelerated depreciation resulting from the group's strategic bioresources review. This compares with accelerated depreciation of certain bioresources assets amounting to £82.3 million in the prior year, primarily relating to incineration assets at the group's Mersey Valley Sludge Processing Centre, known as Shell Green. The accelerated depreciation in both years reflects the outcomes of the strategic review, whereby the likelihood of the group deriving future economic benefit from these assets was considered remote in light of improvements in alternative lower-cost and more environmentally friendly processes. In addition to this, in prior year, inventory spares held for use by these assets were written down to £nil.

Notes to the financial statements

4. Operating profit (continued)

Excluding the impact of this current and prior year accelerated depreciation, the group's depreciation and amortisation expense has increased by £19.1 million in the current year, principally reflecting the higher capital expenditure programme in AMP6 with a higher number of assets commissioned towards the end of the AMP. In the near term this depreciation and amortisation expense is expected to flatten out, reflecting the lower AMP7 capital programme.

During the prior year, the group incurred operating costs of £19.2 million in relation to the onset of the COVID-19 pandemic, comprising £16.7 million in relation to allowances for expected credit losses in respect of household trade receivables, £1.4 million allowances for expected credit losses in respect of non-household trade receivables, and £1.1 million of other operating expenses. The additional allowances for expected credit losses reflected the group's estimate of the potential impact of the pandemic on the recoverability of receivables over and above its existing expected credit loss assessment, and was treated as an adjusting item in arriving at the group's underlying operating profit included in its alternative performance measures. This was possible given the proximity of the group's year end reporting date to the introduction of lockdown measures in the UK.

Incremental costs for the year ended 31 March 2021 arising as a result of the pandemic are estimated to be around £8 million of operating costs, though these have been partially offset by savings realised elsewhere, and around £5 million of additional costs associated with expected credit losses due to the increased risk associated with cash collection as government support schemes are withdrawn. With the passage of time, and with the conditions brought about by the pandemic becoming embedded into normal processes during the current year, the group considers that, for the purpose of presenting an underlying operating profit position, splitting out these costs does not provide meaningful or useful additional information.

Property rates expenses in the current year include the impact of £1.1 million (2020: £8.1 million) of refunds in relation to rates paid in previous years, and £nil (2020: £8.2 million) reduction in accrued rates costs. These reductions ensure that the cumulative costs associated with property rates paid by the group are appropriately recorded.

Research and development expenditure for the year ended 31 March 2021 was £1.0 million (2020: £1.0 million). In addition, £6.2 million (2020: £nil) of costs accrued in relation to the Innovation in Water Challenge scheme operated by Ofwat for AMP7, which therefore did not apply in the prior year. These expenses directly offset £6.2 million recognised in revenue during the 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 £438,000 (2020: £403,000), which are broken down as follows:

	2021 £'000	2020 £'000
Audit services		
Statutory audit – group and company	304	289
Statutory audit – subsidiary	34	24
	338	313
Non-audit services		
Regulatory audit services provided by the statutory auditor	71	62
Other non-audit services	59	28
	468	403

Notes to the financial statements

5. Investment income

	2021 £m	2020 £m
Interest receivable on short-term bank deposits held at amortised cost	2.8	5.4
Interest receivable on loans to joint ventures of the UUG group held at amortised cost (see note A7)	2.4	2.4
Net pension interest income (see note 15)	13.4	10.9
	18.6	18.7

6. Finance expense

	2021 £m	2020 £m
Interest payable		
Interest payable on borrowings held at amortised cost[1]	180.0	229.6
Interest payable on borrowings from intermediate parent undertakings	1.4	2.9
Preference share dividends (see note 8)	4.6	9.1
	186.0	241.6
Fair value losses on debt and derivative instruments		
Fair value hedge relationships:		
Borrowings[2]	(155.1)	87.1
Designated swaps[2] [3]	132.8	(68.6)
	(22.3)	18.5
Financial instruments at fair value through profit or loss		
Borrowings designated at fair value through profit or loss[4]	(67.3)	57.8
Associated swaps[5]	67.8	(49.8)
	0.5	8.0
Fixed interest rate swaps[5]	(36.0)	52.3
Net payments on derivatives and debt under fair value option	(17.6)	(15.3)
Inflation swaps[5]	3.4	13.4
Other	0.6	(0.4)
	(49.6)	50.0
Net fair value (gains)/losses on debt and derivative instruments[6]	(71.4)	76.5
	114.6	318.1

Notes:

(1) Includes a £52.6 million (2020: £100.8 million) non-cash inflation uplift expense in relation to the group's index-linked debt and £1.7 million (2020: £1.6 million) interest expense on lease liabilities, representing the unwinding of discounting applied to future lease payments.

(2) Includes foreign exchange gains of £43.9 million (2020: £14.8 million losses), excluding those on instruments measured at fair value through profit or loss. These losses are largely offset by fair value gains on derivatives.

(3) Under the provisions of IFRS 9 'Financial instruments', changes in fair value resulting from changes to the foreign currency basis spread (£12.7 million loss) are recognised in other comprehensive income rather than profit or loss as they relate to items designated in an accounting hedge relationship (2020: £1.3 million gain).

(4) Under the provisions of IFRS 9 'Financial instruments', a £43.3 million fair value loss (2020: £34.2 million gain) due to changes in the group's own credit risk is recognised in other comprehensive income rather than within profit or loss.

(5) 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.

(6) Includes £21.4 million income (2020: £15.9 million) due to net interest on derivatives and debt under fair value option and £1.3 million expense (2020: £0.5 million income) due to non-cash inflation changes on index-linked derivatives.

Notes to the financial statements

6. Finance expense (continued)

Interest payable is stated net of £30.4 million (2020: £40.6 million) borrowing costs capitalised in the cost of qualifying assets, with £30.3 million (2020: £40.2 million) capitalised within property, plant and equipment and £0.1 million (2020: £0.4 million) capitalised within intangible assets during the year. This has been calculated by applying an average capitalisation rate of 2.3 per cent (2020: 3.2 per cent) to expenditure on such assets as prescribed by IAS 23 'Borrowing Costs'.

7. Tax

	2021 £m	2020 £m
Current tax		
UK corporation tax	78.1	53.8
Adjustments in respect of prior years	0.1	(10.8)
Total current tax charge for the year	78.2	43.0
Deferred tax		
Current year	19.6	11.2
Adjustments in respect of prior years	(2.2)	4.9
	17.4	16.1
Change in tax rate	-	132.4
Total deferred tax charge for the year	17.4	148.5
Total tax charge for the year	95.6	191.5

An increase in the headline rate of corporation tax to 25 per cent effective from 1 April 2023 was announced in the Chancellor's Budget on 3 March 2021. This change was substantively enacted on 24 May 2021 and will result in a future deferred tax charge, currently estimated at around £380 million. The deferred tax charge of £132.4 million in the prior year reflects the Government's reversal of the planned reduction in the rate of corporation tax from 19 per cent to 17 per cent from 1 April 2020.The adjustments in respect of prior years relate to agreement of routine prior years' UK tax matters.

The table below reconciles the notional tax charge at the UK corporation tax rate to the total tax charge and total effective tax rate for the year:

	2021 £m	2021 %	2020 £m	2020 %
Profit before tax	505.7		327.4	
Tax at the UK corporation tax rate	96.1	19.0	62.2	19.0
Adjustments in respect of prior years	(2.1)	(0.4)	(5.9)	(1.8)
Change in tax rate	-	-	132.4	40.4
Net expense not deductible for tax	1.6	0.3	2.8	0.9
Total tax charge and effective tax rate for the year	95.6	18.9	191.5	58.5

Notes to the financial statements

7. Tax (continued)

The table below reconciles the notional tax charge at the UK corporation tax rate to the total current tax charge for the year:

	2021 £m	2020 £m
Profit before tax	505.7	327.4
Profit before tax multiplied by the standard rate of UK corporation tax of 19%	96.1	62.2
Relief for capital allowances in place of depreciation	(78.6)	(82.1)
Disallowance of depreciation charged in the accounts	70.0	81.6
Financial transactions timing differences	(7.8)	11.7
Pension timing differences	-	(17.4)
Relief for capitalised interest	(5.8)	(7.7)
Other timing differences	2.6	2.7
Adjustments to tax charge in respect of prior years	0.1	(10.8)
Expenses not (Income not taxable)/deductible for tax purposes	(0.7)	0.6
Depreciation charged on non-qualifying assets	2.3	2.2
Current tax charge for the year	78.2	43.0

The Group's current tax charge is lower than the UK headline rate of 19% 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 atypical bioresources asset write down in the prior year.

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 company making accelerated deficit repair contributions of £81.4 million in the prior year.

The current year adjustments to tax charge in respect of prior years of £0.1 million was lower in the current year mainly due to the agreement of various routine capital allowance matters covering multiple years in the prior year.

Notes to the financial statements

7. Tax (continued)

Tax on items taken directly to equity

	2021 £m	2020 £m
Current tax		
Relating to other pension movements	(2.7)	-
Deferred tax (see note 16)		
On remeasurement (losses)/gains on defined benefit pension schemes	(19.7)	114.3
Relating to other pension movements	2.7	-
Adjustments in respect of prior years on net fair value gains	-	2.4
On net fair value (losses)/gains recognised in other comprehensive income	(8.8)	6.8
	(25.8)	123.5
Total tax charge on items taken directly to equity	(28.5)	123.5

The 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.

The tax adjustments taken to equity primarily relate to remeasurement movements on the group's defined benefit pension schemes. In the prior year this included the adjustment arising from a change in the rate at which the deferred tax liabilities are measured, from 17 per cent to 35 per cent. This change in rate reflected a revised judgement as to the most likely method by which the defined benefit pension surplus would be realised. Whereas prior to the year ended 31 March 2020 it was assumed that the surplus could be realised through a reduction in future contributions, from the year ended 31 March 2020 onwards 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:

	2021 £m	2020 £m
Ordinary shares		
Interim dividend for the year ended 31 March 2021 at 0.0 pence per share (2020: 134.5 pence)	-	134.5
Interim dividend for the year ended 31 March 2021 at 0.0 pence per share (2020: 77.5 pence)	-	77.5
Interim dividend for the year ended 31 March 2021 at 0.0 pence per share (2020: 301.2 pence)	-	301.2
	-	513.2

The directors have not recommended a final ordinary dividend (2020: £nil).

Until their redemption and cancellation during the year, the company's redeemable preference shares were included in the statement of financial position as a liability and, accordingly, dividends payable on them were included in net interest payable (see notes 6 and 13).

Notes to the financial statements

9. Property, plant and equipment

Property, plant and equipment comprises owned and leased assets.

	2021 £m	2020 £m
Property, plant and equipment – owned	11,676.1	11,390.7
Right of use assets – leased	56.2	54.1
Net book value	11,732.3	11,444.8

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
Cost						
At 1 April 2019	361.4	5,490.4	7,363.3	542.2	1,619.0	15,376.3
Opening balance adjustment	(0.1)	-	-	-	-	(0.1)
Additions	1.8	140.5	150.1	9.7	443.4	745.5
Transfers	5.9	131.1	352.7	24.1	(513.8)	-
Disposals	(13.5)	(31.5)	(251.0)	(13.2)	-	(309.2)
At 31 March 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	365.4	5,897.9	8,002.4	519.7	1,483.8	16,269.2
Accumulated depreciation						
At 1 April 2019	127.3	421.2	3,327.8	402.8	-	4,279.1
Charge for the year	8.7	44.5	350.6	33.4	-	437.2
Disposals	(13.5)	(31.2)	(236.9)	(12.9)	-	(294.5)
At 31 March 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	129.1	477.1	3,582.5	404.4	-	4,593.1
Net book value						
At 31 March 2020	233.0	5,296.0	4,173.6	139.5	1,548.6	11,390.7
At 31 March 2021	236.3	5,420.8	4,419.9	115.3	1,483.8	11,676.1

During the year, there was a transfer of £2.0 million cost and associated £1.0 million accumulated depreciation from property, plant and equipment to intangible assets following a data cleanse exercise in respect of the fixed assets register.

Notes to the financial statements

9. Property, plant and equipment (continued)

Property, plant and equipment – leased

Group and company	Land and buildings £m	Operational assets £m	Fixtures, fittings, tools and equipment £m	Total £m
Cost				
At 1 April 2019	-	-	-	-
Opening balance adjustment on adoption of IFRS 16[1]	45.4	5.8	-	51.2
Additions	4.0	0.8	-	4.8
Disposals	-	(0.1)	-	(0.1)
At 31 March 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
Accumulated depreciation				
At 1 April 2019	-	-	-	-
Charge for the year	0.8	1.0	-	1.8
At 31 March 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
Net book value				
At 31 March 2020	48.6	5.5	-	54.1
At 31 March 2021	49.9	6.1	0.2	56.2

Note:

[1] Following a review of underlying assets during the year, the opening balance adjustment on adoption of IFRS 16 at 1 April 2019 has been re-presented such that £1.4 million of right of use assets relating to vehicles have been included in operational assets whereas they were previously included in fixtures, fittings, tools and equipment. After taking account of additions, disposals and depreciation, the effect of this is that cost and net book value of operational assets is £1.7 million and £0.8 million higher at 31 March 2020 compared with the presentation in the prior year financial statements, and the cost and net book value of fixtures, fittings, tools and equipment at 31 March 2020 are lower by the same amount.

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 2021, the group and company had entered into contractual commitments for the acquisition of property, plant and equipment amounting to £335.5 million (2020: £431.3 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

Group and company	Total £m
Cost	
At 1 April 2019	435.9
Additions	27.6
Disposals	(22.7)
At 31 March 2020	440.8
Additions	32.7
Disposals	(51.0)
Transfers	2.0
At 31 March 2021	424.5
Accumulated amortisation	
At 1 April 2019	233.2
Charge for the year	41.2
Disposals	(22.6)
At 31 March 2020	251.8
Charge for the year	41.5
Disposals	(50.9)
Transfers	1.0
At 31 March 2021	243.4
Net book value at 31 March 2020	189.0
Net book value at 31 March 2021	181.1

The group and company's intangible assets relate mainly to computer software.

During the year, there was a transfer of £2.0 million cost and associated £1.0 million accumulated depreciation from property, plant and equipment to intangible assets following a data cleanse exercise in respect of the fixed assets register.

At 31 March 2021, the group and company had entered into contractual commitments for the acquisition of intangible assets amounting to £0.9 million (2020: £2.6 million).

11. Trade and other receivables

Group and company	2021 £m	2020 £m
Trade receivables	61.4	76.5
Amounts owed by intermediate parent and fellow subsidiary undertakings (see note A7):		
Trading balances	1.0	1.3
In relation to guarantees	-	4.4
Floating rate loan	-	40.0
Amounts owed by other related parties (see note A7)	27.1	146.3
Other debtors and prepayments	34.1	38.9
Accrued income	101.2	72.1
	224.8	379.5

Notes to the financial statements

11. Trade and other receivables (continued)

At 31 March 2021, the group and company had £nil (2020: £98.0 million) of trade and other receivables classified as non-current, which related to amounts owed by related parties of £nil (2020: £93.6 million) and amounts owed by intermediate parent undertaking in relation to guarantees of £nil million (2020: £4.4 million). During the year the revolving credit facility extended to Water Plus, to which this balance related, was transferred to the group's intermediate parent and as a result the guarantees are no longer required. Further details of this transfer can be found in note A7.

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:

Group and company	2021 £m	2020 £m
At the start of the year	71.3	56.4
Amounts charged to operating expenses (see note 4)	28.7	41.8
Trade receivables written off	(20.2)	(28.0)
Amounts charged to deferred income	0.5	1.1
At the end of the year	80.3	71.3

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. In the year ended 31 March 2020, an allowance for expected credit losses of £18.1 million was recognised in relation to trade and other receivables, reflecting the direct impact of COVID-19 estimated at the onset of the pandemic In the year ended 31 March 2021, a further charge of around £5 million was recognised due to increased risk associated with cash collection as government support schemes are withdrawn.

At 31 March 2021 and 31 March 2020, the group and company had no trade receivables that were past due and not individually impaired.

Notes to the financial statements

11. Trade and other receivables (continued)

The following table provides information regarding the ageing of net trade receivables that were past due and individually impaired:

Group and company	Aged less than one year £m	Aged between one year and two years £m	Aged greater than two years £m	Carrying value £m
At 31 March 2021				
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	42.0	18.8	0.6	61.4

Group and company	Aged less than one year £m	Aged between one year and two years £m	Aged greater than two years £m	Carrying value £m
At 31 March 2020				
Gross trade receivables	72.8	31.6	43.4	147.8
Allowance for expected credit losses	(19.3)	(15.7)	(36.3)	(71.3)
Net trade receivables	53.5	15.9	7.1	76.5

At 31 March 2021, the group and company had no trade receivables that were not past due (2020: £nil).

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 2021 and 31 March 2020, 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

Group and company	2021 £m	2020 £m
Cash at bank and in hand	2.4	31.7
Short-term bank deposits	646.2	470.1
Cash and short-term deposits	648.6	501.8
Book overdrafts (included in borrowings, see note 13)	(10.1)	(14.1)
Cash and cash equivalents in the statement of cash flows	638.5	487.7

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.

Notes to the financial statements

13. Borrowings

Group and company	2021 £m	2020 £m
Non-current liabilities		
Bonds[1]	5,656.3	5,251.0
Bank and other term borrowings	1,710.4	1,814.9
Lease liabilities (see note 14)	54.1	51.8
Amounts owed to intermediate parent undertaking (see note A7)	577.6	984.8
	7,998.4	8,102.5
Current liabilities		
Bonds	388.5	-
Bank and other term borrowings	152.4	707.2
Book overdrafts (see note 12)	10.1	14.1
Lease liabilities (see note 14)	3.0	2.6
130,000,000 7.0 per cent £1.00 redeemable preference shares (see note 20)	-	130.0
Amounts owed to intermediate parent undertaking (see note A7)[2]	163.0	72.5
	717.0	926.4
	8,715.4	9,028.9

Note:

[1] For the company, bonds includes £3,064.8 million (2020: £2,245.6 million) of amounts owed to subsidiary undertakings.

[2] For the company, £0.4 million (2020: £0.3 million) of amounts is owed to subsidiary undertakings.

The £130.0 million 7.0 per cent redeemable preference shares were redeemed by the company on 30 September 2020, resulting in a reduction in retained earnings and the creation of a capital redemption reserve. A bonus issue of ordinary shares was subsequently made, with £130.0 million of ordinary share capital allotted to the company's immediate parent as fully paid, resulting in the elimination of this capital redemption reserve.

These redeemable preference shares had been presented as amounts falling due within one year as they could be redeemed by not less than 30 days' written notice served by the group or the shareholder. 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 group.

For further details of the principal economic terms and conditions of outstanding borrowings see note A4.

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.

Notes to the financial statements

14. Leases (continued)

The maturity profile of lease liabilities recognised at the balance sheet date is:

Group and company	2021 £m	2020 £m
Less than 1 year	3.0	2.7
1 to 5 years	9.4	7.8
5 to 10 years	6.7	8.3
10 to 25 years	24.8	24.5
35 to 50 years	41.0	40.5
50 to 100 years	81.0	80.1
100 to 500 years	107.6	106.9
Longer than 500 years	3.2	3.2
Total undiscounted cash payments	276.7	274.0
Effect of discounting	(219.6)	(219.6)
Present value of cash payments	57.1	54.4

During the year ending 31 March 2021, £1.7 million (2020: £1.6 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 2021 was £3.2 million (2020: £3.1 million), of this £1.7 million (2020: £1.6 million) was payment of interest and £1.5 million (2020: £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

Defined benefit schemes

The net pension expense before tax recognised in the income statement in respect of the defined benefit schemes is summarised as follows:

Group and company	2021 £m	2020 £m
Current service cost	4.6	5.6
Curtailments/settlements	0.4	3.6
Administrative expenses	2.0	1.0
Pension expense charged to operating profit	7.0	10.2
Net pension interest income credited to investment income (see note 5)	(13.4)	(10.9)
Net pension income credited before tax	(6.4)	(0.7)

Defined benefit pension costs excluding curtailments/settlements included within employee benefit expense were £6.6 million (2020: £6.6 million) comprising current service costs and administrative expenses.

Total post-employment benefits expense excluding curtailments/settlements charged to operating profit of £30.0 million (2020: £29.1 million) comprise the defined benefit costs

Notes to the financial statements

15. Retirement benefit surplus (continued)

described above of £6.6 million (2020: £6.6 million) and defined contribution pension costs of £23.4 million (2020: £22.5 million) (see note 3).

Included within curtailments/settlements is £0.3 million (2020: £nil) 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:

Group and company	2021 £m	2020 £m
At the start of the year	579.1	373.8
Income recognised in the income statement	6.4	0.7
Contributions	7.8	91.2
Remeasurement (losses)/gains gross of tax	(62.3)	113.4
At the end of the year	531.0	579.1

Included in the contributions paid of £7.8 million (2020: £91.2 million) were deficit repair contributions of £nil (2020: £81.4 million), enhancements to benefits provided on redundancy of £0.6 million (2020: £1.6 million), payments in relation to historic unfunded, unregistered retirement benefit schemes of £0.9 million (2020: £1.4 million), and administration expenses of £0.2 million (2020: £0.2 million). Contributions paid in relation to current service cost during the year were £6.1 million (2020: £6.6 million).

Remeasurement gains and losses are recognised directly in the statement of comprehensive income.

Group and company	2021 £m	2020 £m
The return on plan assets, excluding amounts included in interest	185.4	(96.3)
Actuarial (losses)/gains arising from changes in financial assumptions	(323.5)	188.0
Actuarial gains/(losses) arising from changes in demographic assumptions	60.5	(5.3)
Actuarial gains arising from experience	15.3	27.0
Remeasurement (losses)/gains on defined benefit pension schemes	(62.3)	113.4

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 and company made £23.4 million (2020: £22.5 million) of contributions to defined contribution schemes which are included in employee benefit expense (see note 3).

Notes to the financial statements

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:

Group and company	Accelerated tax depreciation £m	Retirement benefit obligations £m	Other £m	Total £m
At 1 April 2019	1,073.6	63.5	(16.1)	1,121.0
Charged/(credited) to the income statement	12.6	17.4	(13.9)	16.1
Change in tax rate (see note 7)	127.0	7.5	(2.1)	132.4
Charged to equity (see note 7)	-	114.3	9.2	123.5
At 31 March 2020	1,213.2	202.7	(22.9)	1,393.0
Charged to the income statement	8.6	-	8.8	17.4
Credited to equity (see note 7)	-	(17.0)	(8.8)	(25.8)
At 31 March 2021	1,221.8	185.7	(22.9)	1,384.6

Certain deferred tax assets and liabilities have been offset in accordance with IAS 12 'Income Taxes'.

The deferred tax charge in the prior year of £132.4 million reflects the Government's reversal of the planned reduction in the rate of corporation tax from 19 per cent to 17 per cent from 1 April 2020.

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 are mainly 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 movements have no impact on future corporation tax payments as they only impact the year-on-year deferred tax movement.

Notes to the financial statements

17. Provisions

Group and company	Restructuring £m	Other £m	Total £m
At 1 April 2019	2.8	14.0	16.8
Charged/(credited) to the income statement	7.2	(0.6)	6.6
Utilised in the year	(5.1)	(1.9)	(7.0)
At 31 March 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

The group and company had no provisions classed as non-current at 31 March 2021 or 31 March 2020.

The restructuring provision as at 31 March 2021 and 31 March 2020 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 legal claims.

18. Trade and other payables

Group and company	2021 £m	2020 £m
Non-current		
Deferred grants and contributions	780.4	736.8
Other creditors	16.3	23.8
	796.7	760.6
Current		
Trade payables	32.7	35.4
Amounts owed to parent and fellow subsidiary undertakings (see note A7)	4.7	1.5
Amounts owed to other related parties (see note A7)	1.3	0.3
Other tax and social security	5.9	5.8
Deferred grants and contributions	15.4	14.5
Accruals and other creditors	207.4	221.8
Deferred income	50.9	44.5
	318.3	323.8
	1,115.0	1,084.4

Included within accruals and other creditors as at 31 March 2021 was £17.9 million (2020: £12.0 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 (2020: 15 days).

The carrying amounts of trade and other payables approximates to their fair value at 31 March 2021 and 31 March 2020.

Notes to the financial statements

18. Trade and other payables (continued)

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

Group and company	2021 £m	2020 £m
At the start of the year	751.3	684.5
Amounts capitalised during the year	5.0	35.1
Transfer of assets from customers	55.0	47.0
Credited to the income statement – revenue	(14.6)	(13.8)
Credited to the income statement – other operating costs	(0.4)	(0.4)
Credited to allowance for bad and doubtful receivables	(0.5)	(1.1)
At the end of the year	795.8	751.3

19. Other Reserves

	Capital redemption reserve £m	Cost of hedging reserve £m	Cash flow hedging reserve £m	Total £m
At 1 April 2020	-	10.7	(1.3)	9.4
Other comprehensive income				
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
Total comprehensive income	-	**(10.3)**	**7.5**	**(2.8)**
Redemption of preference shares	(130.0)	-	-	-
Elimination of capital redemption reserve on allotment of ordinary shares	130.0	-	-	-
At 31 March 2021	-	0.4	6.2	6.6

	Cost of hedging reserve £m	Cash flow hedging reserve £m	Total £m
At 1 April 2019	12.0	0.3	12.3
Other comprehensive income			
Change in fair value recognised in other comprehensive income	1.3	(7.6)	(6.3)
Amounts reclassified from other comprehensive income to profit or loss	-	5.6	5.6
Deferred tax adjustments in respect of prior years on net fair value gains	(2.4)	-	(2.4)
Tax on items taken directly to equity	(0.2)	0.4	0.2
At 31 March 2020	10.7	(1.3)	9.4

Notes to the financial statements

19. Other Reserves (continued)

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	2021 £m	2020 £m
Issued, called up and fully paid		
230,000,000 (2020: 100,000,000) ordinary shares of £1.00 each	230.0	100.0
Nil (2020: 130,000,000) 7 per cent cumulative redeemable preference shares of £1.00 each	-	130.0
	230.0	230.0
Less: 130,000,000 7 per cent cumulative redeemable preference shares of £1.00 each designated as borrowings (see note 13)	-	(130.0)
	230.0	100.0

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 simply 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. For further information, see note 13.

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 with the litigation currently in its early stages. While the litigation's likely direction and the quantum of any compensation being claimed is uncertain at this stage, 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 2021 by either the group or the company (2020: none).

Notes to the financial statements

22. Events after the reporting period

On 3 March 2021, an increase in the headline rate of corporation tax to 25 per cent from 1 April 2023 was announced in the Chancellor's Budget. This increase was substantively enacted on 24 May 2021 and will result in a future deferred tax charge currently estimated at around £380 million. As this substantive enactment occurred after the reporting date, no adjustments have been made to current or deferred tax amounts recognised in the financial statements at and for the year ended 31 March 2021.

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
Subsidiary undertakings			
England and Wales			
United Utilities Water Finance PLC	Ordinary	100.00	Financing company
Lingley Mere Management Company Limited	Ordinary	68.10	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 68.10 per cent and 18.90 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

	2021 £m	2020 £m
Profit before tax	505.7	327.4
Adjustment for investment income (see note 5) and finance expense (see note 6)	96.0	299.4
Operating profit	601.7	626.8
Adjustments for:		
Depreciation of property, plant and equipment (see note 9)	376.8	439.0
Amortisation of intangible assets (see note 10)	42.5	41.2
Loss on disposal of property, plant and equipment (see note 4)	8.4	13.9
Amortisation of deferred grants and contributions (see note 18)	(15.0)	(13.8)
Changes in working capital:		
Increase in inventories	(3.6)	(2.0)
Decrease in trade and other receivables	112.5	18.5
Increase/(decrease) in trade and other payables	5.6	(10.1)
Decrease in provisions (see note 17)	(5.3)	(0.4)
Pension contributions paid less pension expense charged to operating profit	(0.8)	(81.0)
Cash generated from operations	1,122.8	1,032.1

The group and company have received property, plant and equipment of £55.0 million (2020: £47.0 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[(1)]

Group and company	2021 £m	2020 £m
Purchase of property, plant and equipment in statement of cash flows	**604.5**	**643.7**
Non-cash additions:		
Transfers of assets from customers (see note 18)	55.0	47.0
IAS 23 capitalised borrowing costs (see note 6)	30.3	40.2
Net book value transfers to intangible assets	1.0	-
Timing differences on cash paid[(2)]	(18.9)	14.6
Property, plant and equipment additions	**671.9**	**745.5**

[(1)] 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.

[(2)] 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

	2021 £m	2020 £m
Purchase of intangibles assets in statement of cash flows	**33.6**	**27.2**
IAS 23 capitalised borrowing costs (see note 6)	0.1	0.4
Net book value transfers to intangible assets	(1.0)	-
Intangible asset additions	**32.7**	**27.6**

For the year ended 31 March 2021, the group has enhanced its disclosures relating to the statement of cash flows in respect of relevant accounting policies, judgements taken, and how items can be reconciled to other areas of the financial statements. Please see note A8 for further details.

A3 Net debt

During the period, the group has revised its definition of net debt in order to exclude the impact of derivatives that are not hedging specific debt instruments and therefore give a fairer reflection of the net debt amount the group is contractually obliged to repay. This updated approach is now consistent with that taken by credit rating agencies, and better reflects the underlying regulatory economics. Under this revised definition net debt comprises borrowings, net of cash and short-term deposits and loans receivable from the group's intermediate parent undertaking, and net of derivatives but excluding the fair value of the group's fixed interest swaps, electricity derivatives, and inflation swaps (apart from the principal accretion element). Previously net debt had been defined as borrowings, net of cash and short-term deposits and derivatives.

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 on borrowings and their associated swaps that are included in net debt are not materially opposite in value for the year ended 31 March 2021. The effects of COVID-19 on financial market volatility in the period has impacted the credit spread recognised on the group's fair value option debt, and material basis spread adjustments have been recorded on the group's cross-currency swaps. Both of these items have been recorded in other comprehensive income. In addition, material credit spread adjustments have been recorded with respect to the group's derivatives in fair value hedge relationships, which has been recorded in the consolidated income statement in the period.

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: Bonds	Borrowings: Bank and other term borrowings	Borrowings: Lease liabilities	Borrowings: Amounts owed to intermediate parent undertaking	Borrowings: Redeemable Preference shares	Derivatives: in a fair value hedge	Derivatives: at fair value through profit or loss	**Total liabilities from financing activities**	Loan receivable	Cash and cash equivalents	Adjustments in calculating net debt	**Net debt**
	£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)**
Non-cash movements												
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)**
Cash flows used in financing activities:												
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(1)	-	669.0	1.5	950.9	130.0	10.8	-	**1,762.1**	-	(1,762.1)	-	-
Payment in respect of loan receivable	-	-	-	-	-	-	-	**-**	(40.0)	40.0	-	-
Dividends paid	-	-	-	-	-	-	-	**-**	-	-	-	**-**
Changes arising from financing activities	**(793.7)**	**659.4**	**(4.4)**	**316.7**	**130.0**	**(132.7)**	**(40.1)**	**135.1**	**(40.0)**	**(157.0)**	**(33.3)**	**(95.2)**
Cash flows used in investing activities	-	-	-	-	-	-	-	**-**	-	(633.1)	-	**(633.1)**
Cash flows generated from operating activities	-	-	1.7	-	-	-	-	**1.7**	-	940.9	-	**942.6**
At 31 March 2021	**(6,044.8)**	**(1,862.8)**	**(57.1)**	**(740.6)**	**-**	**263.0**	**40.5**	**(8,401.7)**	**-**	**638.5**	**98.4**	**(7,664.8)**

Notes to the financial statements

A3 Net debt (continued)

	Borrowings					Derivatives						
	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	**Total liabilities from financing activities**	Loan receivable	Cash and cash equivalents	Adjustments in calculating net debt	**Net debt**
	£m	£m	£m	£m	£m	£m	£m	**£m**	£m	£m	£m	**£m**
At 31 March 2019	(4,882.6)	(2,444.6)	-	(769.9)	(130.0)	327.1	82.0	**(7,818.0)**	40.0	312.4	76.4	**(7,389.2)**
Adjustment on initial adoption of IFS 16	-	-	(51.1)	-	-	-	-	**(51.1)**	-	-	-	**(51.1)**
At 1 April 2019	(4,882.6)	(2,444.6)	(51.1)	(769.9)	(130.0)	327.1	82.0	**(7,869.1)**	40.0	312.4	76.4	**(7,440.3)**
Non-cash movements												
Inflation uplift on index-linked debt	(58.2)	(42.6)	-	-	-	-	-	**(100.8)**	-	-	-	**(100.8)**
Fair value movements	(69.9)	(2.0)	-	(23.6)	-	57.8	(3.6)	**(41.3)**	-	-	55.3	**14.0**
Foreign exchange	(9.5)	(5.3)	-	-	-	-	-	**(14.8)**	-	-	-	**(14.8)**
Other	(1.4)	-	(6.4)	(2.9)	-	-	-	**(10.7)**	-	-	-	**(10.7)**
Cash flows used in financing activities:												
Receipts in respect of borrowings and derivatives	(651.1)	(137.1)	-	(310.9)	-	-	-	**(1,099.1)**	-	1,096.3	-	**(2.8)**
Payments in respect of borrowings and derivatives[1]	421.7	109.5	1.5	50.0	-	10.8	2.2	**595.7**	-	(595.7)	-	-
Dividends paid	-	-	-	-	-	-	-	**-**	-	(513.2)	-	**(513.2)**
Changes arising from financing activities	**(368.4)**	**(77.5)**	**(4.9)**	**(287.4)**	**-**	**68.6**	**(1.4)**	**(671.0)**	**-**	**(12.6)**	**55.3**	**(628.2)**
Cash flows used in investing activities	-	-	-	-	-	-	-	**-**	-	(634.2)	-	**(634.2)**
Cash flows generated from operating activities	-	-	1.6	-	-	-	-	**1.6**	-	822.1	-	**823.7**
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)**

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 2021 £m	Carrying value 2021 £m	Fair value 2020 £m	Carrying value 2020 £m
Borrowings in fair value hedge relationships			**2,913.5**	**2,895.4**	**2,440.0**	**2,590.5**
5.75% 375m bond	GBP	2022	394.5	388.5	405.1	399.4
2.0% 450m bond(1)	GBP	2025	470.6	465.3	451.8	468.5
2.867% 320m bond(1)	HKD	2026	31.7	32.0	33.4	35.9
2.92% 739m bond(1)	HKD	2026	73.2	74.1	77.2	83.4
1.129% 52m bond(1)	EUR	2027	46.9	46.6	44.2	48.6
2.37% 830m bond(1)	HKD	2027	79.6	81.9	82.7	93.3
5.625% 300m bond	GBP	2027	388.0	380.4	380.6	398.7
5.02% JPY 10bn dual currency loan	JPY/USD	2029	87.2	90.2	94.5	106.8
0.875% 300m bond(1)	GBP	2029	284.8	295.8	-	-
2.058% 30m bond(1)	EUR	2030	28.9	28.6	26.8	30.2
2.625% 350m bond(1)	GBP	2031	460.8	440.5	366.4	380.5
1.641% 30m bond(1)	EUR	2031	28.0	27.4	25.7	28.9
2.9% 600m bond(1)	HKD	2031	60.4	56.4	62.2	67.2
1.474% 35m bond(1)	USD	2031	23.5	22.7	-	-
1.707% 28m bond(1)	EUR	2032	26.1	27.0	23.8	28.7
1.653% 26m bond(1)	EUR	2032	24.0	24.7	21.9	26.2
1.70% 30m bond(1)	EUR	2033	27.8	29.0	25.3	30.8
2.0% 50m bond(1)	GBP	2033	103.8	98.4	51.4	53.3
5.0% 200m bond	GBP	2035	273.7	285.9	267.0	310.1
Borrowings designated at fair value through profit or loss			**373.6**	**373.6**	**397.5**	**397.5**
6.875% 400m bond (owed to intermediate parent)	USD	2028	373.6	373.6	397.5	397.5
Borrowings measured at amortised cost			**6832.4**	**5,446.5**	**6,661.8**	**6,040.9**
1.61% + RPI 50m EIB IL loan	GBP	2020	-	-	68.1	67.0
1.73% + RPI 50m EIB IL loan	GBP	2020	-	-	68.1	66.9
1.84% + RPI 50m EIB IL loan	GBP	2020	-	-	68.1	66.9
1.90% + RPI 50m EIB IL loan	GBP	2020	-	-	68.1	66.8
1.93% + RPI 50m EIB IL loan	GBP	2020	-	-	68.0	66.7
1.88% + RPI 50m EIB IL loan	GBP	2020	-	-	67.9	66.6
2.10% + RPI 50m EIB IL loan	GBP	2020	-	-	67.9	66.5
2.46% + RPI 50m EIB IL loan	GBP	2020	-	-	68.2	66.6
Short-term bank borrowings - fixed	GBP	2022	50.7	50.7	72.2	72.2
0.80% + LIBOR 100m loan	GBP	2022	101.1	100.0	99.7	100.0
0.47% + RPI 100m IL loan	GBP	2023	125.2	119.7	121.2	118.1
0.49% + RPI 100m IL loan	GBP	2025	126.6	115.2	118.9	113.6
0.013% + RPI 25m IL bond(1)	GBP	2025	30.7	28.7	29.1	28.3
0.1275% + RPI 100m IL loan	GBP	2026	125.0	113.6	116.2	112.1
0.01% + RPI 20m IL bond(1)	GBP	2028	25.0	23.7	23.1	23.6
1.23% + RPI 50m EIB (amortising) IL loan	GBP	2029	40.5	36.8	43.6	40.8
0.288% + CPI 100m IL loan	GBP	2029	113.9	102.1	110.3	101.3
1.29% + RPI 50m EIB (amortising) IL loan	GBP	2029	42.9	38.8	45.9	42.8
1.12% + RPI 50m EIB (amortising) IL loan	GBP	2029	42.4	38.5	45.3	42.5
1.10% + RPI 50m EIB (amortising) IL loan	GBP	2029	42.3	38.5	45.2	42.4
0.75% + RPI 50m EIB (amortising) IL loan	GBP	2029	43.6	39.8	46.1	43.7
0.76% + RPI 50m EIB (amortising) IL loan	GBP	2030	43.6	39.7	46.0	43.5
1.15% + RPI 50m EIB (amortising) IL loan	GBP	2030	44.1	39.6	46.6	43.4
1.11% + RPI 50m EIB (amortising) IL loan	GBP	2030	44.2	39.7	46.7	43.5
0.178% + RPI 35m IL bond(1)	GBP	2030	46.1	40.2	42.2	39.6

Notes to the financial statements

A4 Borrowings (continued)

Borrowings measured at amortised cost (continued)	Currency	Year of final repayment	Fair value 2021	Carrying value 2021	Fair value 2020	Carrying value 2020
0.245% + CPI 20m IL bond(1)	GBP	2031	24.0	21.5	20.7	21.4
0.01% + RPI 38m IL bond(1)	GBP	2031	48.6	44.5	43.8	44.2
3.375% + RPI 50m IL bond	GBP	2032	140.2	83.1	105.1	81.7
0.709% + LIBOR 100m EIB (amortising) loan	GBP	2032	68.7	68.8	71.3	75.0
0.691% + LIBOR 150m EIB (amortising) loan	GBP	2032	107.6	107.8	110.4	117.2
0.573% + LIBOR 100m EIB (amortising) loan	GBP	2033	74.2	75.0	75.5	81.3
0.511% + LIBOR 150m EIB (amortising) loan	GBP	2033	115.7	117.2	117.7	126.6
2.0% 250m bond(1)	GBP	2033	259.4	245.7	257.0	245.7
0.01% + RPI 100m EIB (amortising) IL loan	GBP	2033	100.3	92.2	100.1	98.0
0.01% + RPI 75m EIB (amortising) IL loan	GBP	2034	75.3	69.1	75.0	73.4
0.01% + RPI 75m EIB (amortising) IL loan	GBP	2034	77.9	71.4	75.0	75.6
0.01% + RPI 75m EIB (amortising) IL loan	GBP	2034	77.9	71.4	75.0	75.6
1.9799% + RPI 100m IL bond	GBP	2035	243.9	155.2	204.0	152.7
0.873%+LIBOR 100m EIB (amortising) loan	GBP	2035	91.6	90.6	91.3	96.9
0.840%+LIBOR 75m EIB (amortising) loan	GBP	2035	71.2	70.3	69.3	75.0
0.01% + RPI 26.5m IL bond(1)	GBP	2036	35.7	33.0	30.3	32.8
0.379% + CPI 20m IL bond(1)	GBP	2036	25.6	21.5	20.1	21.3
0.01% + RPI 29m IL bond(1)	GBP	2036	38.9	34.2	32.4	33.9
0.093% + CPI 60m IL bond(1)	GBP	2037	73.7	64.1	57.3	63.6
1.66% + RPI 35m IL bond	GBP	2037	68.2	49.6	60.5	49.0
1.75% 250m bond(1)	GBP	2038	236.7	248.1	232.1	248.0
2.40% + RPI 70m IL bond	GBP	2039	148.8	96.8	129.6	95.5
1.7829% + RPI 100m IL bond	GBP	2040	237.4	153.5	193.5	151.1
0.01% + CPI 125m IL bond(1)	GBP	2040	144.5	145.6	-	-
1.3258% + RPI 50m IL bond	GBP	2041	117.8	76.6	100.7	75.4
1.5802% + RPI 100m IL bond	GBP	2042	205.1	153.1	147.3	150.6
1.875% 300m bond(1)	GBP	2042	287.7	295.3	-	-
1.5366% + RPI 50m IL bond	GBP	2043	49.6	30.6	37.9	30.1
1.397% + RPI 50m IL bond	GBP	2046	113.6	76.5	94.2	75.3
0.359% + CPI 32m IL bond(1)	GBP	2048	41.0	33.8	28.2	33.5
1.7937% + RPI 50m IL bond	GBP	2049	122.4	76.2	97.1	75.0
Commission for New Towns (amortising) loan – fixed	GBP	2053	52.6	26.2	50.7	26.8
1.847% + RPI 100m IL bond	GBP	2056	255.0	149.8	194.6	147.7
1.815% + RPI 100m IL bond	GBP	2056	251.9	149.1	188.8	147.1
1.662% + RPI 100m IL bond	GBP	2056	241.6	148.8	186.1	146.8
1.5865% + RPI 50m IL bond	GBP	2056	122.0	74.4	92.8	73.4
1.591% + RPI 25m IL bond	GBP	2056	60.5	37.1	46.3	36.6
1.556% + RPI 50m IL bond	GBP	2056	121.6	74.0	92.4	73.0
1.435% + RPI 50m IL bond	GBP	2056	119.4	73.7	90.0	72.7
1.3805% + RPI 35m IL bond	GBP	2056	82.4	51.6	62.3	50.9
1.585% + RPI 100m IL bond	GBP	2057	311.2	143.2	284.1	141.3
0.387% + CPI 33m IL bond(1)	GBP	2057	44.4	34.5	26.7	34.2
1.702% + RPI 50m IL bond	GBP	2057	124.5	72.2	93.6	71.3
Preference shares (owed to immediate parent undertaking)	GBP	2099	-	-	130.0	130.0
Amounts owed to intermediate parent undertaking	GBP	Various	367.9	367.0	659.8	659.8
Book overdrafts (see note 12)	GBP	2021	10.1	10.1	14.1	14.1
Lease liabilities	GBP	Various	57.1	57.1	54.4	54.4
			10,119.5	**8,715.4**	**9,499.3**	**9,028.9**

(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.

Notes to the financial statements

A4 Borrowings (continued)

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.

During the year, the group issued £75 million fixed rate notes as a fungible increase to £350 million fixed rate notes issued in prior years, due February 2031 with a coupon of 2.625 per cent. The group issued £50 million fixed rate notes as a fungible increase to £300 million fixed rate notes issued in the prior year, due July 2033 with a coupon of 2 per cent.

Notes to the financial statements

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 2021, the group and company had £1,203.6 million (2020: £1,067.5 million) of available liquidity, which comprised £648.6 million cash and short-term deposits (2020: £501.8 million) and £565.7 million (2019: £565.4 million) of undrawn committed borrowing facilities. Short-term deposits mature within three months and bank overdrafts are repayable on demand.

The group and company had available committed borrowing facilities as follows:

Group and company	2021 £m	2020 £m
Expiring within one year	80.0	40.0
Expiring after one year but in less than two years [(1)]	80.0	678.0
Expiring after more than two years	395.0	435.0
Total borrowing facilities	555.0	1,153.0
Facilities drawn[(2)]	-	(587.3)
Undrawn borrowing facilities	555.0	565.7

Note:

(1) Figure includes £nil (2020: £598 million) facility provided by intermediate parent undertaking.

(2) Facilities drawn are provided by the intermediate parent undertaking, expiring after one year but in less than two years.

These facilities are arranged on a bilateral rather than a syndicated basis, which spreads the maturities more evenly over a longer time period, thereby reducing the refinancing risk by providing several renewal points rather than a large single refinancing point.

Notes to the financial statements

A5 Financial Risk Management (continued)

Maturity analysis

Concentrations of risk may arise if large cash flows are concentrated within particular time periods. The maturity profile in the following table represents the forecast future contractual principal and interest cash flows in relation to the group 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[(1)]**	**Adjustment[(2)]**	**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[(2)]	(5,242.4)	(5,242.4)						
Borrowings	8,658.3	(5, 242.4)	861.8	625.4	316.2	838.9	513.0	10,745.4
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[(2)]	188.6	188.6						
Derivatives – net assets	(310.0)	188.6	(52.7)	(82.5)	(54.0)	(63.7)	(73.1)	(172.6)

Group and company	**Total[(1)]**	**Adjustment[(2)]**	**1 year or less**	**1-2 years**	**2-3 years**	**3-4 years**	**4-5 years**	**More than 5 years**
At 31 March 2020	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Bonds	7,491.1		155.5	459.3	63.8	65.0	66.1	6,681.4
Bonds – UUWF	2,760.2		38.9	38.9	38.9	39.0	489.0	2,115.5
Bank and other term borrowings	2,687.4		677.4	122.0	352.1	122.7	255.8	1,157.4
Preference shares	130.0		130.0	-	-	-	-	-
Parent borrowings	1,172.0		98.9	611.4	22.1	22.1	22.1	395.4
Adjustment to carrying value[(2)]	(5,266.2)	(5,266.2)						
Borrowings	8,974.5	(5,266.2)	1,100.7	1,231.6	476.9	248.8	833.0	10,349.7
Derivatives:								
Payable	1.7		0.8	0.1	0.5	0.4	0.2	(0.3)
Receivable	(434.4)		(54.6)	(54.8)	(81.5)	(47.2)	(129.8)	(66.5)
Adjustment to carrying value[(2)]	(41.4)	(41.4)						
Derivatives – net assets	(474.1)	(41.4)	(53.8)	(54.7)	(81.0)	(46.8)	(129.6)	(66.8)

Notes:

[(1)] Forecast future cash flows are calculated, where applicable, using forward interest rates based on the interest environment at year-end and are, therefore, susceptible to changes in market conditions. For index-linked debt it has been assumed that RPI will be three per cent and CPI will be two per cent over the life of each instrument.

[(2)] The carrying value of debt is calculated following various methods in accordance with IFRS 9 'Financial Instruments' and therefore this adjustment reconciles the undiscounted forecast future cash flows to the carrying value of debt in the statement of financial position, excluding £57.1 million (2020: £54.4 million) of lease liabilities.

For the company, those bonds with United Utilities Water Finance PLC represent amounts owed to subsidiary undertakings.

Notes to the financial statements

A5 Financial Risk Management (continued)

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.

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 2021, Water Plus was the group's single largest debtor, with amounts outstanding in relation to wholesale services of £27.7 million (2020: £52.7 million). During the year, sales to Water Plus in relation to wholesale services were £362.9 million (2020: £438.3 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 2021 and 31 March 2020, the maximum exposure to credit risk for the group and company is represented by the carrying amount of each financial asset in the statement of financial position:

Group and company	2021 £m	2019 £m
Cash and short-term deposits (see note 12)	648.6	501.8
Trade and other receivables (see note 11)	223.8	379.5
Derivative financial instruments	424.7	617.9
	1,297.1	1,499.2

Notes to the financial statements

A5 Financial risk management (continued)

Credit risk (continued)

The credit exposure on derivatives is disclosed gross of any collateral held. At 31 March 2021, the group and company held £50.7 million (2020: £72.2 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.

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 (from circa 87 per cent RPI-linked and circa 13 per cent CPI-linked as at 31 March 2020).

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 £4,094.3 million at 31 March 2021 (2020: £4,082.2 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

Group and company	2020 £m	2019 £m
1 per cent increase in RPI/CPI	(35.4)	(39.6)
1 per cent decrease in RPI/CPI	35.4	39.6

Notes to the financial statements

A5 Financial risk management (continued)

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).

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

Group and company	2021 £m	2020 £m
1 per cent increase in interest rate	124.2	117.1
1 per cent decrease in interest rate	(128.3)	(125.8)

Notes to the financial statements

A5 Financial risk management (continued)

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.

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	375.0	-	450.0	1,325
Average contracted fixed interest rate %	1.98	0.00	1.36	2.00

This table represents the derivatives that are held in fair value hedging relationships, with only the weighted average for the fixed interest elements of the swaps disclosed.

Further detail on the fair value hedging relationships is provided below:

Risk exposure	Interest rate risk on borrowings	
Nominal amount of hedging instruments	£m	2,150
Carrying amount of hedging instruments	£m	215.9
Accumulated fair value (gains)/losses on hedged items	£m	198.6
Fair value (gains)/losses used for calculating hedge ineffectiveness for the year ended 31 March 2021[(1)]:		
Hedged items	£m	(88.9)
Hedging instruments	£m	90.9
Hedge ineffectiveness recognised in the income statement	£m	2.0
Nominal amount of hedging instruments directly impacted by the IBOR reform	£m	1,675.0

Note:

[(1)] 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.

Notes to the financial statements

A5 Financial risk management (continued)

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.

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	369.7
Average contracted fixed interest rate %	-	-	2.71	2.29

This table represents the derivatives that are held in fair value hedging relationships, with only the weighted average for the fixed interest elements of the swaps disclosed.

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	469.6
Carrying amount of hedging instruments	£m	59.9
Accumulated fair value (gains)/losses on hedged items	£m	66.6
Fair value (gains)/losses used for calculating hedge ineffectiveness for the year ended 31 March 2021[1]:		
Hedged items	£m	(66.2)
Hedging instruments	£m	66.5
Hedge ineffectiveness recognised in the income statement	£m	0.3
Nominal amount of hedging instruments directly impacted by the IBOR reform	£m	442.8

Note:

[1] 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.

Notes to the financial statements

A5 Financial risk management (continued)

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 rate such as the Sterling Overnight Index Average (SONIA).

Whilst uncertainty around the mechanism to replace IBOR, the timing of the replacement, and the method and timing for the calculation of a spread adjustment remained, amendments were included within IFRS 9 'Financial Instruments' providing temporary exceptions from applying specific hedge accounting requirements in cases where hedging relationships are directly impacted by the IBOR reform. These reliefs are applied until the uncertainty surrounding the IBOR reform has ended or the hedging relationship has been discontinued.

At the point of IBOR transition, further amendments are included within IFRS 9 to allow for specific changes to hedge documentation to be made without the requirement to discontinue the hedging relationship, as well as including a practical expedient when financial liabilities and assets are modified to calculate cash flows based on the alternative interest rate, provided the modification has been done on an economically equivalent basis. Given the reliefs provided as part of the phase 2 amendments, the anticipation is that on transition the risk of significant movements in the income statement or on the balance sheet as a result of the transition is low.

The amount of financial instruments left to transition to alternative benchmarks can be found below. Non-derivative financial instruments are presented at their carrying value, with the derivatives at their nominal value to give the fairest representation of the magnitude of instruments left to transition to RFRs. All of the instruments left to transition reference LIBOR. In addition to the below, the group holds £555 million of undrawn committed facilities that reference LIBOR.

Type of financial instrument	Amount left to transition to RFR (£m)
Non-derivative financial liabilities (pay GBP LIBOR)	£729.7
Derivative instruments (pay GBP LIBOR)	£2,343.9*
Derivative instruments (receive GBP LIBOR)	£(2,482.3)*
Net position	£591.3

*Future dated transition to RFR contractually agreed

During the financial year, the group adhered to the ISDA 2020 IBOR fall-backs protocol, embedding fall-back provisions into the interest rate derivatives of compounded SONIA plus a spread, which will automatically replace the London Inter-bank Offered Rate (LIBOR) at a future index cessation effective date. On 5 March 2021, following an announcement from the FCA on the future cessation and loss of representativeness of the LIBOR benchmarks, ISDA advised that a LIBOR cessation trigger event had occurred under the protocol. The index cessation effective date for GBP LIBOR will therefore by 1 January 2022. All of the group's derivative counterparties have adhered to the protocol and so from 1 January 2022 all of the group's derivatives will automatically transition from LIBOR to RFRs. The group does not expect to renegotiate interest rate swaps to reference a RFR prior to this date.

Further detail on the risk management strategy can be found within the interest rate risk section of this note.

Notes to the financial statements

A5 Financial risk management (continued)

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 £130.0 million redeemable preference shares have been classified as more than five years according to their latest redemption date of 1 October 2099.

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.

Group and company At 31 March 2021	Total £m	1 year or less £m	1-2 years £m	2-3 years £m	3-4 years £m	4-5 years £m	More than 5 years £m
Borrowings in fair value hedge relationships							
Fixed rate instruments	2,895.5	388.6	-	-	465.3	106.1	1,935.5
Effect of swaps	-	2,590.5	-	-	(465.3)	(106.1)	(1,935.5)
	2,590.5	2,895.5	-	-	-	-	-
Borrowings designated at fair value through profit or loss							
Fixed rate instruments	373.6	-	-	-	-	-	373.6
Effect of swaps	-	373.6	-	-	-	-	(373.6)
	373.6	373.6	-	-	-	-	-
Borrowings measured at amortised cost							
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	-	-	-	-	-
	5,446.3	4,574.4	1.0	1.1	0.9	3.7	865.1
Effect of fixed interest rate swaps	-	(2,332.3)	164.5	575.0	350.0	200.0	1,042.8
Total borrowings	8,715.4	5,511.2	165.5	576.1	350.9	203.7	1,907.9
Cash and short-term deposits	(648.6)	(648.6)	-	-	-	-	-
Net borrowings	8,066.8	4,862.6	165.5	576.1	350.9	203.7	1,907.9

Notes to the financial statements

A5 Financial risk management (continued)

Repricing analysis (continued)

Group and company At 31 March 2020	Total £m	1 year or less £m	1-2 years £m	2-3 years £m	3-4 years £m	4-5 years £m	than 5 years £m
Borrowings in fair value hedge relationships							
Fixed rate instruments	2,590.5	-	399.4	-	-	468.5	1,722.6
Effect of swaps	-	2,590.5	(399.4)	-	-	(468.5)	(1,722.6)
	2,590.5	2,590.5	-	-	-	-	-
Borrowings designated at fair value through profit or loss							
Fixed rate instruments	397.5	-	-	-	-	-	397.5
Effect of swaps	-	397.5	-	-	-	-	(397.5)
	397.5	397.5	-	-	-	-	-
Borrowings measured at amortised cost							
Fixed rate instruments	777.1	73.2	1.0	1.1	0.7	0.8	700.3
Floating rate instruments	1,345.9	1,345.9	-	-	-	-	-
Index-linked instruments	3,917.9	3,917.9	-	-	-	-	-
	6,040.9	5,337.0	1.0	1.1	0.7	0.8	700.3
Effect of fixed interest rate swaps	-	(2,382.3)	50.0	164.5	575.0	350.0	1,242.8
Total borrowings	9,028.9	5,942.7	51.0	165.6	575.7	350.8	1,943.1
Cash and short-term deposits	(501.8)	(501.8)	-	-	-	-	-
Net borrowings	8,527.1	5,440.9	51.0	165.6	575.7	350.8	1,943.1

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.

Hedge accounting

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.

Notes to the financial statements

A5 Financial risk management (continued)

Details of electricity swaps that have been designated in cash flow hedging relationships are summarised below:

Risk exposure	Electricity price risk	
Nominal amount of hedging instruments	£m	46.5
Carrying amount of hedging instruments	£m	6.5
Fair value (gains)/losses used for calculating hedge ineffectiveness for the year ended 31 March 2021[1]:	£m	(9.3)
Hedge ineffectiveness recognised in the income statement	£m	-
Cash flow hedge reserve	£m	7.8
Amount reclassified from the cash flow hedge reserve to the income statement	£m	-

Note:

[1] 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.

Due to the relative low value of the electricity swaps in comparison to that of the derivative portfolio, no maturity profile and fixed price breakdown has been disclosed.

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 UUW 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 UUW of at least A- with Fitch Ratings (Fitch). Debt issued by UUW's financing subsidiary, United Utilities Water Finance PLC, is guaranteed by UUW and is therefore rated in line with UUW.

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) and Funds from Operations (FFO) to debt) 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.

Notes to the financial statements

A5 Financial risk management (continued)

Fair values

The table below sets out the valuation basis of financial instruments held at fair value and financial instruments where fair value has been separately disclosed in the notes as the carrying value is not a reasonable approximation of fair value.

Group and company

At 31 March 2021	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets at fair value through profit or loss				
Derivative financial assets – fair value hedge	-	272.8	-	272.8
Derivative financial assets – held for trading[1]	-	142.6	-	142.6
Derivative financial assets – cash flow hedge	-	6.9	-	6.9
Investments	-	0.1	-	0.1
Financial liabilities at fair value through profit or loss				
Derivative financial liabilities – fair value hedge	-	(12.6)	-	(12.6)
Derivative financial liabilities – held for trading[1]	-	(100.3)	-	(100.3)
Derivative financial liabilities – cash flow hedge	-	-	-	-
Financial liabilities designated as fair value through profit or loss	-	(373.6)	-	(373.6)
Financial liabilities for which fair value has been disclosed				
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)
	(4,629.4)	(5,180.6)	-	(9,810.0)

At 31 March 2020	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets at fair value through profit or loss				
Derivative financial assets – fair value hedge	-	395.7	-	395.7
Derivative financial assets – held for trading[1]	-	222.0	-	222.0
Derivative financial assets – cash flow hedge	-	0.2	-	0.2
Investments	-	0.1	-	0.1
Financial liabilities at fair value through profit or loss				
Derivative financial liabilities – fair value hedge	-	-	-	-
Derivative financial liabilities – held for trading[1]	-	(141.4)	-	(141.4)
Derivative financial liabilities – cash flow hedge	-	(2.4)	-	(2.4)
Financial liabilities designated as fair value through profit or loss	-	(397.5)	-	(397.5)
Financial liabilities for which fair value has been disclosed				
Financial liabilities in fair value hedge relationships	(1,981.5)	(458.5)	-	(2,440.0)
Other financial liabilities at amortised cost	(199.9)	(6,461.9)	-	(6,661.8)
	(2,181.4)	(6,843.7)	-	(9,025.1)

Notes:
[1] These derivatives form economic hedges and, as such, management intends to hold these through to maturity. Derivatives forming an economic hedge of the currency exposure on borrowings included in these balances were £146.3 million (2020: £221.9 million).

Notes to the financial statements

A5 Financial risk management (continued)

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable).

The group has calculated fair values using quoted prices where an active market exists, which has resulted in £2,181.4 million (2019: £2,997.8 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 £816.4 million decrease (2019: £1,620.2 million decrease) in 'level 1' fair value measurements is largely due to a decrease in the number of observable quoted bond prices in active markets at 31 March 2021.

During the year, changes in the fair value of financial liabilities designated at fair value through profit or loss resulted in a £23.6 million gain (2019: £26.2 million loss). Included within this was a £34.2 million gain (2019: £6.6 million gain) attributable to changes in own credit risk, recognised in other comprehensive income. The cumulative amount due to changes in credit spread was £79.0 million profit (2019: £44.8 million profit). The carrying amount is £171.4 million (2019: £147.8 million) higher than the amount contracted to settle on maturity.

A6 Retirement benefits

Defined benefit schemes

The group participates in two major funded defined benefit pension schemes in the United Kingdom – the United Utilities Pension Scheme (UUPS) and the United Utilities PLC group of the Electricity Supply Pension Scheme (ESPS), both of which are closed to new employees. The assets of these schemes are held in trust funds independent of the group's finances.

The trustees are composed of representatives of both the employer and employees. The trustees are required by law to act in the interests of all relevant beneficiaries and are responsible for the investment policy with regard to the assets plus the day-to-day administration of the benefits.

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.

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	2021 £m	2020 £m
Total value of current employees benefits	717.1	610.4
Deferred members benefits	320.0	293.7
Pensioner members benefits	1,398.2	1,352.4
Total defined benefit obligation	2,435.3	2,256.5

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 requirements

The latest finalised funding valuations of the schemes were carried out by independent qualified actuaries as at 31 March 2018, earlier than originally planned due to the aforementioned changes to the pension scheme, and determined that the schemes were both in a deficit position on a funding basis. The basis on which scheme liabilities are valued for funding purposes differs from the basis required under IAS 19, with liabilities on a funding basis being subject to assumptions at the valuation date that are not updated between revaluations. Funding deficits vary significantly from company to company, but neither the deficits, the assumptions on which they are based, the associated sensitivities, nor the risk exposures are disclosed by many companies and, therefore, meaningful cross-company comparisons are not possible. Conversely, scheme liabilities are valued on a consistent basis between companies under IAS 19 and are subject to assumptions and sensitivities that are required to be disclosed. Consequently, the relative economic positions of companies are comparable only on an IAS 19 basis, subject to normalisation of assumptions used between companies.

A retirement benefit surplus was recognised as an asset at both 31 March 2021 and 31 March 2020 as, under both the UUPS and ESPS scheme rules, the group has an unconditional right to a refund of the surplus assuming the full settlement of the plans' liabilities in a single event, such as a scheme wind-up.

Under UK legislation there is a requirement that pension schemes are funded prudently, and that funding plans are agreed by pension scheme trustees. The group had plans in place with the schemes' trustees to address the funding deficits by 31 December 2021 for the UUPS and 30 September 2024 for the ESPS, through a series of deficit recovery contributions. This timescale has been accelerated, with accelerated deficit repair contributions of £80.5 million and £0.9 million made to the UUPS and ESPS respectively in April 2019. These payments represent the final acceleration of deficit repair contributions set out in the schedules of contributions agreed with the schemes' trustees as part of the 31 March 2018 valuation process, and reduce the deficit repair contributions payable, due from the company, to £nil. Accordingly, no deficit repair contributions were required during the year ended 31 March 2021.

As the 2018 valuation basis was consistent with a long-term target for self-sufficiency, the expectation is that the pension schemes will be fully funded on a low dependency basis without additional contributions from the company.

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.

Following further evolution in the group's investment and risk management strategies during the year ended 31 March 2020, both UUPS and ESPS 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 'Further reporting analysis' section of this appendix.

The group expects to make further contributions of £7.5 million in the year ending 31 March 2022, £6.2 million and £0.4 million in respect of current service contributions to UUPS and ESPS respectively, and £0.2 million in respect of expenses to the ESPS.

The schemes' funding plans are reviewed regularly, and the next funding valuation for UUPS and ESPS is due as at 31 March 2021. The valuation is expected to be finalised by 31 March 2022.

Impact of scheme risk management on IAS 19 disclosures

Under the prescribed IAS 19 basis, pension scheme liabilities are calculated based on current accrued benefits. Expected cash flows are projected forward allowing for RPI and CPI and the current member mortality assumptions. These projected cash flows are then discounted by a high-quality corporate bond rate, which comprises an underlying interest rate and a credit spread.

The group has de-risked its pension schemes through hedging strategies applied to the underlying interest rate and 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 spread have not been hedged primarily due to difficulties in doing so over long durations, while 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.

In contrast, the schemes' specific funding bases, which formed the basis for regular deficit repair contributions, are unlikely to suffer from significant volatility due to credit spread, because a prudent, fixed credit spread assumption is applied.

Pension benefits under the defined benefit element of the UUPS hybrid section, that became effective for pensionable service from 1 April 2018, are linked to CPI rather than RPI.

In the year ended 31 March 2021, the discount rate decreased by 0.25 per cent (2020: 0.1 per cent decrease), which includes a 0.85 per cent decrease in credit spreads and a 0.6 per cent increase in gilt yields over the year. The IAS 19 remeasurement loss of £62.3 million (2020: £113.4 million gain) reported in note 15 has largely resulted from a decrease in credit spreads during the year and an RPI inflation assumption increase of 0.55 per cent (2020: 0.65 per cent decrease). 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.

Notes to the financial statements

A6 Retirement benefits (continued)

Guaranteed Minimum Pensions (GMP) equalisation

A second UK High Court Ruling in the Lloyds Guaranteed Minimum Pensions (GMP) equalisation case was published on 20 November 2020. The implication of the first court ruling on 26 October 2018 was that GMP will be equalised for males and females and resulted in GMP equalisation past service cost (and corresponding increase in liabilities) of £5.5 million for the UUPS being recognised for the year ended 31 March 2019. The second ruling requires schemes to equalise GMP in respect of past transfers out (dating back to 17 May 1990) where those benefits were not equalised under the 2018 judgement. This is not expected to have a material impact on the group's financial statements.

For the year ended 31 March 2021, there has been a further £0.3 million (UUPS) increase to the pension liability and past service costs in relation to GMP equalisation as a result of the six-year look-back period previously assumed for back payments no longer being applicable, as it has been concluded that there is no limit for back payments.

Reporting and assumptions

The results of the latest funding valuations at 31 March 2018 have been adjusted for IAS 19 to assess the position at 31 March 2021, by taking account of experience over the period, changes in market conditions, and differences in the financial and demographic assumptions. The present value of the defined benefit obligation, and the related current service costs, were measured using the projected unit credit method.

Member data used in arriving at the liability figure included within the overall IAS 19 surplus has been based on the finalised actuarial valuations as at 31 March 2018 for both UUPS and ESPS.

Financial assumptions

The main financial and demographic assumptions used by the actuary to calculate the defined benefit surplus of UUPS and ESPS are outlined below:

	2021 % p.a.	2020 % p.a.
Discount rate	2.05	2.30
Pension increases	3.35	2.80
Pensionable salary growth:		
ESPS	3.35	2.80
UUPS	2.45	1.60
Price inflation - RPI	3.35	2.80
Price inflation - CPI(1)	2.75	1.60

Note:

(1) The CPI price inflation assumption represents a single weighted average rate derived from an assumption of 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 2.05 per cent being equivalent to gilts plus 75 basis points (31 March 2020: 2.30 per cent being equivalent to gilts plus 160 basis points). To align to emerging market practice and provide a more robust estimate, an exercise was carried out during the year to revisit the population of high quality corporate bonds used in deriving the discount rate. The primary change resulting from this exercise was to expand the corporate bond population used to include those rated at least AA by one or more credit rating agencies, whereas previously the rate was derived based on bonds rated AA by two or more agencies. Overall, the changes resulting from this exercise have not given rise to any material change in the discount rate or fair value of defined benefit obligations as at 31 March 2021 compared with using the same approach as that used in the prior year.

Notes to the financial statements

A6 Retirement benefits (continued)

In September 2019, the Chancellor of the Exchequer highlighted the UK Statistics 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. 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. In arriving at the company's best estimate for RPI, an inflation risk premium of 0.2 per cent (2020: nil) has been deducted from the breakeven inflation rate for the year ended 31 March 2021. The impact of this is a decrease in the defined benefit obligation of around £90 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.

The assumption for CPI inflation includes a 0.2 per cent inflation risk premium (2020: 0.3 per cent) and 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, reducing to 0.1 per cent 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 the confirmation of RPI reform is a circa £10 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 after 2030. A reduction in RPI will result in a reduction to pension scheme liabilities; however, as our pension schemes are hedged for RPI inflation, this will result in a comparable reduction to pension scheme assets.

Demographic assumptions

At both 31 March 2021 and 31 March 2020, mortality in retirement is assumed to be in line with the Continuous Mortality Investigation's (CMI) S2PA year of birth tables, with a scaling factor of 106 per cent and 109 per cent for male pensioners and non-pensioners respectively and 104 per cent and 105 per cent for female pensioners and non-pensioners respectively, reflecting actual mortality experience. At 31 March 2021, mortality in retirement is based on CMI 2020 (2020: CMI 2019) long-term improvement factors, with a long-term annual rate of improvement of 1.25 per cent (2020: 1.50 per cent). It is too early at this stage to analytically determine the long-term impact of the COVID-19 pandemic on future mortality trends for the schemes' membership, therefore no explicit adjustment to the mortality assumptions have been made in this regard.

The current life expectancies at age 60 underlying the value of the accrued liabilities for the schemes are:

	2021 years	2020 years
Retired member – male	26.0	26.6
Non-retired member – male	26.9	27.7
Retired member – female	28.4	28.9
Non-retired member – female	29.5	30.2

Notes to the financial statements

A6 Retirement benefits (continued)

Sensitivity of the key scheme assumptions

The measurement of the group's defined benefit surplus is sensitive to changes in key assumptions, which are described above. The sensitivity calculations presented below allow for the specified movement in the relevant key assumption, while all other assumptions are held constant.

This approach does not take into account the interrelationship between some of these assumptions or any hedging strategies adopted.

Asset volatility
If the schemes' assets underperform relative to the discount rate used to calculate the schemes' liabilities, this will create a deficit. The schemes hold some growth assets (equities, diversified growth funds and emerging market debt) which, though expected to outperform the discount rate in the long term, create volatility in the short term. The allocation to growth assets is monitored to ensure it remains appropriate given the schemes' long-term objectives.

Discount rate
An increase/decrease in the discount rate of 0.25 per cent would have resulted in a £106.7/£114.2 million (2020: £99.5 million) increase/decrease in the schemes' liabilities at 31 March 2021, although as long as credit spreads remain stable this will be largely offset by an increase/decrease in the value of the schemes' bond holdings and other instruments designed to hedge this exposure. The discount rate is based on high-quality corporate bond yields of a similar duration to the schemes' liabilities.

Price inflation
An increase/decrease in the inflation assumption of 0.25 per cent would have resulted in a £108.6/£102.3 million (2019: £93.4 million) increase/decrease in the schemes' liabilities at 31 March 2021, 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 2021, 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.

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 £25.0 million decrease in the schemes' liabilities at 31 March 2021 (2020: £33.2 million decrease based on an increase in the mortality long-term improvement rate from 1.50 per cent to 1.75 per cent).

Life expectancy
An increase/decrease in life expectancy of one year would have resulted in a £113.1 million (2020: £86.0 million) increase/decrease in the schemes' liabilities at 31 March 2021. 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

At 31 March, the fair value of the schemes' assets recognised in the statement of financial position were as follows:

Group	Schemes' assets %	2021 £m	Schemes' assets %	2020 £m
Non-equity growth assets	10.4	307.5	9.5	268.1
Gilts[1]	34.6	1,025.6	36.4	1,032.4
Bonds	46.2	1,371.6	47.8	1,355.4
Other	8.8	261.7	6.3	179.7
Total fair value of schemes' assets	100.0	2,966.4	100.0	2,835.6
Present value of defined benefit obligations		(2,435.4)		(2,256.5)
Net retirement benefit surplus		531.0		579.1

[1] Following a review of the fair value of the schemes' assets and derivatives during the year, the fair value of the schemes' assets at 31 March 2020 have been re-presented such that £336.3 million fair value of derivatives have been included in gilts where they were previously included in other. The effect of this is that the fair value of the schemes' assets classified as gilts is £336.3 million lower at 31 March 2020 compared with that presented in the prior year financial statements, and the fair value of the schemes' assets classified as other is £336.3 million higher.

Included within the group's defined benefit pension scheme assets are assets with a fair value estimated to be £222 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 2021. 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 assets, in respect of UUPS, included in the table above, have been allocated to each asset class based on the return the assets are expected to achieve as UUPS has entered into a variety of derivative transactions to change the return characteristics of the physical assets held to reduce undesirable market and liability risks. As such, the breakdown shown separates the assets of the schemes to illustrate the underlying risk characteristics of the assets held.

The portfolio contains a proportion of assets set aside for collateral purposes linked to the derivative contracts entered into, as described above. The collateral portfolio, comprising cash and eligible securities readily convertible

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 assets	Fair value of derivatives	Combined
At 31 March 2021	£m	£m	£m
Non-equity growth assets	307.5	-	307.5
Gilts	2,188.8	(1,163.2)	1,025.6
Bonds	1,378.5	(6.9)	1,371.6
Other	280.2	(18.5)	261.7
Total fair value of schemes' assets	4,155.0	(1,188.6)	2,966.4
At 31 March 2020			
Other non-equity growth assets	268.1	-	268.1
Gilts	1,368.7	(336.3)	1,032.4
Bonds	1,379.8	(24.4)	1,355.4
Other	247.4	(67.7)	179.7
Total fair value of schemes' assets	3,264.0	(428.4)	2,835.6

The derivative values in the tables above represent the net market value of derivatives held within each of these asset categories as follows:

Group and company	UUPS £m	ESPS £m	2021 Total £m	UUPS £m	ESPS £m	2020 Total £m
Gilts						
Repurchase agreements	(1,162.2)	(1.0)	(1,163.2)	(336.1)	(0.2)	(336.3)
	(1,162.2)	(1.0)	(1,163.2)	(336.1)	(0.2)	(336.3)
Bond – hedging non-sterling exposure back to sterling						
Currency forwards	(7.4)	-	(7.4)	(22.9)	-	(22.9)
Interest rate swaps	-	0.5	0.5	-	(1.5)	(1.5)
	(7.4)	0.5	(6.9)	(22.9)	(1.5)	(24.4)
Other – managing liability risks targeting a high level of interest rate and inflation hedging						
Asset swaps	(22.0)	-	(22.0)	(25.0)	-	(25.0)
Interest rate swaps	19.2	-	19.2	21.3	(0.1)	21.2
RPI inflation swaps	(14.9)	(0.6)	(15.5)	(62.1)	(1.7)	(63.8)
Total return swaps	-	(0.2)	(0.2)	-	(0.1)	(0.1)
	(17.7)	(0.8)	(18.5)	(65.8)	(1.9)	(67.7)
Total fair value of derivatives	(1,187.3)	(1.3)	(1,188.6)	(424.8)	(3.6)	(428.4)

Notes to the financial statements

A6 Retirement benefits (continued)

The derivatives shown in the tables only cover those expressly held for the purpose of reducing certain undesirable asset and liability risks. The schemes invest in a number of other pooled funds that make use of derivatives. No allowance is made in the figures above for any derivatives held within these, as these are not held expressly for the purpose of managing risk. The total fair value of pooled funds held within the schemes' assets was £522.5 million (2020: £531.9 million).

Movements in the fair value of the schemes' assets were as follows:

	2021 £m	2020 £m
At the start of the year	2,835.6	2,905.6
Interest income on schemes' assets	63.9	70.2
The return on plan assets, excluding amounts included in interest	185.4	(96.3)
Member contributions	2.3	2.5
Benefits paid	(126.6)	(136.6)
Administrative expenses	(2.0)	(1.8)
Group contributions	7.8	(1.0)
At the end of the year	2,966.4	2,835.6

The group's actual return on the schemes' assets was a gain of £249.3 million (2019: £26.1 million loss), principally due to losses on derivatives hedging the schemes' liabilities.

Movements in the present value of the defined benefit obligations are as follows:

	2021 £m	2020 £m
At the start of the year	(2,256.5)	(2,531.8)
Interest cost on schemes' obligations	(50.5)	(59.3)
Actuarial (losses)/gains arising from changes in financial assumptions	(323.5)	188.0
Actuarial gains/(losses) arising from changes in demographic assumptions	60.5	(5.3)
Actuarial gains arising from experience	15.3	27.0
Curtailments/settlements	(0.4)	(3.6)
Member contributions	(2.3)	(2.5)
Benefits paid	126.6	136.6
Current service cost	(4.6)	(5.6)
At the end of the year	(2,435.4)	(2,256.5)

Notes to the financial statements

A7 Related party transactions

The aggregate disclosable transactions between the UUW group and company and the related parties in the wider UUG group of companies were as follows:

	Sales of goods and services		Purchase of goods and services		Recharge of costs to/(by) related parties at nil margin	
	2021	2020	2021	2020	2021	2020
Group	£m	£m	£m	£m	£m	£m
Ultimate parent undertaking	-	-	-	-	(3.5)	(1.4)
Intermediate parent undertaking	-	-	-	-	0.2	0.5
Fellow subsidiaries	-	-	4.8	4.1	2.0	2.1
Joint ventures of the UUG group	362.0	437.4	-	-	-	-
	362.0	437.4	4.1	4.1	1.3	1.2

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.

In addition to the above, a termination payment of £2.7 million (2020: £nil) was made to a fellow subsidiary in accordance with the terms of an agreement between the two parties. This related to the early removal of a solar array to facilitate the completion of capital projects. There were also £nil (2020: £0.4 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.

In addition to the above, £1.6 million (2020: £2.4 million) of interest income was recognised on loans to joint ventures of the UUG group.

Company

In addition to the above amounts, the company incurred interest charges of £48.7 million (2020: £40.3 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 (2020: £0.1 million) in relation to the services provided by UUWF.

The following amounts were outstanding at the reporting date:

	Amounts owed by related parties		Amounts owed to related parties	
	2021	2020	2021	2020
Group	£m	£m	£m	£m
Ultimate parent undertaking	-	-	2.0	1.2
Intermediate parent undertaking	0.5	45.4	740.6	1,057.6
Immediate parent undertaking	-	-	-	130.0
Fellow subsidiaries	0.5	0.3	2.7	-
Joint ventures of the UUG group	27.1	146.3	1.3	0.3
	28.1	192.0	746.5	1,189.1

Notes to the financial statements

A7 Related party transactions (continued)

At 31 March 2021, amounts owed by related parties were £28.1 million (2020: £192.0 million), comprising £28.1 million (2020: £54.0 million) of trade balances and £nil (2020: £138.0 million) relating to loans. Trade balances are unsecured and will be settled in accordance with normal credit terms. Included within these balances was £27.1 million (2020: £52.7 million) owed by Water Plus and £1.0 million (2020: £1.3 million) owed by the group's intermediate parent company and fellow subsidiaries of the UUG group.

Included within these loans receivable in the year ended 31 March 2020 was £98.0 million outstanding on a £100.0 million revolving credit facility extended to Water Plus, which was guaranteed by United Utilities PLC and had a maturity date of 30 September 2021. This balance comprised £93.6 million being the amount expected to be received from Water Plus after accounting for expected credit losses, with the shortfall of £4.4 million being receivable from United Utilities PLC as guarantor for the facility. United Utilities PLC, as guarantor for the facility, recognised a charge to the income statement in relation to expected credit losses on the facility; no charge was recognised by UUW. During the year ended 31 March 2021, this facility transferred from UUW to United Utilities PLC, and so no revolving credit facility is now recognised by UUW.

£nil (2020: £40.0 million) was owed by United Utilities PLC, which is repayable within one month.

No expense or allowance has been recognised for bad and doubtful receivables in respect of the amounts owed by related parties (2020: £nil).

At 31 March 2021, amounts owed to related parties were £746.5 million (2020: £1,189.1 million), comprising £6.0 million (2020: £1.5 million) of trade balances, £740.5 million (2020: £1,057.3 million) of borrowings (see note 13) and its associated accrued interest of £0.1 million (2020: £0.3 million) owed to United Utilities PLC, and £nil (2020: £130.0 million) relating to preference shares in the company held by United Utilities North West Limited (see notes 13 and 20). Included within these trade balances were £1.3 million (2020: £0.3 million) owed to Water Plus and £2.0 million (2020: £1.2 million) owed to United Utilities Group PLC.

During the year, guarantees with an aggregate limit of £32.1 million (2020: £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 £3,024 million (2020: £2,245.6 million) in respect of borrowings (see note 13), and £17.9 million (2020: £12.0 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 158 to 163.

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.

Notes to the financial statements

A8 Accounting policies (continued)

Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used under the relevant local GAAP into line with those used by the group. Amounts attributable to non-controlling interests are presented separately in equity and total comprehensive income where material.

Subsidiaries

Subsidiaries are entities controlled by the group. Control is achieved where the group is exposed to, or has the rights to, variable returns from its involvement in an entity and has the ability to affect those returns through its power over the entity. In the parent company accounts, investments are held at cost less provision for impairment.

On acquisition, the assets and liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill. Any deficiency of the cost of acquisition below the fair values of the identifiable net assets acquired is credited to the income statement in the period of acquisition. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

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 district 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

Notes to the financial statements

A8 Accounting policies (continued)

or issue of a financial asset or financial liability are included in the initial fair value of that instrument. Where borrowing costs are attributable to the acquisition, construction or production of a qualifying asset, such costs are capitalised as part of the specific asset.

Tax

Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity. Assessing the outcome of uncertain tax positions requires judgements to be made regarding the application of tax law and the result of negotiations with, and enquiries from, 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.

The useful economic lives of these assets are primarily as follows:

- Water and wastewater infrastructure assets:
  - impounding reservoirs 200 years;

Notes to the financial statements

A8 Accounting Policies (continued)

- mains and raw water aqueducts 30 to 300 years;
- sewers and sludge pipelines 60 to 300 years;
- sea outfalls 77 years;

- Buildings 10 to 60 years;
- Operational assets 5 to 80 years; and
- Fixtures, fittings, tools and equipment 3 to 40 years.

Employee and other related costs incurred in implementing the capital schemes of the group are capitalised.

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.

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

Notes to the financial statements

A8 Accounting Policies (continued)

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.

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.

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.

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.

Notes to the financial statements

A8 Accounting Policies (continued)

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.

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.

Notes to the financial statements

A8 Accounting Policies (continued)

Where feasible, the group designates its financial instruments within fair value hedge relationships. In order to apply fair value hedge accounting, it must be demonstrated that there is an economic relationship between the borrowing instrument and the hedging derivative and that the designated hedge ratio is consistent with the group's risk management strategy.

Borrowings designated within a fair value hedge relationship

Where designated, bonds and loans are initially measured at fair value, being the cash proceeds received net of any direct issue costs. They are subsequently adjusted for any change in fair value attributable to the risk being hedged at each reporting date, with the change being charged or credited to finance expense in the income statement.

Hedge accounting is discontinued prospectively when the hedging instrument is sold, terminated or exercised, or where the hedge relationship no longer qualifies for hedge accounting.

Under the provisions of IFRS 9 'Financial Instruments', changes in the group's own credit risk are recognised in other comprehensive income.

Borrowings designated at fair value through profit or loss

Designation is made where the requirements to designate within a fair value hedge cannot be met at inception despite there being significant fair value offset between the borrowing and the hedging derivative. Where designated, bonds and loans are initially measured at fair value being the cash proceeds received and are subsequently measured at fair value at each reporting date, with changes in fair value being charged or credited to finance expense in the income statement.

Derivative financial instruments

The group's default treatment is that derivative financial instruments are measured at fair value at each reporting date, with changes in fair value being charged or credited to finance expense in the income statement. The group enters into financial derivatives contracts to manage its financial exposure to changes in market rates (see note 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

Notes to the financial statements

A8 Accounting Policies (continued)

hedge its exposure to changes in the applicable underlying interest rate and it is this portion of the cash flows that is included in the valuation model (excluding any applicable company credit risk spread).

The valuation of debt designated at fair value through the profit or loss incorporates an assumed credit risk spread in the applicable discount factor. Credit spreads are determined based on indicative pricing data.

Inventories

Inventories are stated at the lower of cost and net realisable value. For properties held for resale, cost includes the cost of acquiring and developing the sites, including borrowing costs where applicable.

Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

Employee benefits

Retirement benefit obligations

The group operates two defined benefit pension schemes, which are independent of the group's finances, for its employees. Actuarial valuations to determine the funding of the schemes, along with future contribution rates, are carried out by the pension scheme actuary as directed by the trustees at intervals of not more than three years. In any intervening years, the trustees review the continuing appropriateness of the funding and contribution rates.

From a financial reporting perspective and in accordance with IAS 19 'Employee Benefits', defined benefit assets are measured at fair value while liabilities are measured at present value, using the projected unit credit method. The difference between the two amounts is recognised as a surplus or obligation in the statement of financial position. Where this difference results in a defined benefit surplus this is recognised in accordance with IFRIC 14 'IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction' on the basis that the group has an unconditional right to a refund of any surplus that may exist following the full settlement of plan liabilities in a single event.

The pension cost under IAS 19 is assessed in accordance with the advice of a firm of actuaries based on the latest actuarial valuation and assumptions determined by the actuary, which are used to estimate the present value of defined benefit obligations. The assumptions are based on information supplied to the actuary by the company, supplemented by discussions between the actuary and management. The assumptions are disclosed in note A5.

The cost of providing pension benefits to employees relating to the current year's service (including curtailment gains and losses) is included within employee benefits expense, while the interest on the schemes' assets and liabilities is included within investment income and finance expense respectively. Remeasurement gains/losses on scheme assets and liabilities are presented in other comprehensive income.

In addition, the group also operates a defined contribution pension section within the United Utilities Pension Scheme. Payments are charged as employee costs as they fall due. The group has no further payment obligations once the contributions have been paid.

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.

Notes to the financial statements

A8 Accounting Policies (continued)

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).

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 are 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 leases 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.

Notes to the financial statements

A8 Accounting Policies (continued)

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.

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.