NORTHUMBRIAN WATER LIMITED

FINANCIAL STATEMENTS

FOR THE PERIOD ENDED 31 MARCH 2015

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FOR THE PERIOD ENDED 31 March 2015

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CHAIRMAN'S STATEMENT

I am pleased to introduce the financial statements of Northumbrian Water Limited (NWL or the Company) for the period ended 31 March 2015, including our regulatory accounts.

Our Chief Executive Officer, Heidi Mottram, highlights in her report some of the key operational achievements of NWL during 2014-15. Operational excellence is key to consistent delivery of outstanding customer service, which is at the heart of everything NWL does. This is reflected in the fact that much of the Board's time is spent constructively challenging the executive team to achieve continuous improvements in customer service and in the Company's health, safety and environmental performance.

'People' is one of our strategic themes and a detailed Health & Safety update is the first report on each Board agenda. This is a top priority for the Board, which is working with the Company's management to ensure that the Health & Safety strategy for 2016 to 2020 will deliver even better performance. The environment is another strategic theme and the Board reviews environmental performance at each Board meeting. The Strategic report, below, sets out our environmental performance in more detail, but I would like to highlight that we have delivered seven consecutive years' compliance with discharge consents at our sewage treatment works; an industry-leading position.

The PR14 process has been another important area of focus for the Board. Having agreed the main principles to be included in the Company's response to Ofwat's 'Future Price Limits' consultation, the Board was kept up to date with all Ofwat guidance and agreed the Company's responses to consultations. The Board was integral to the planning process, confirming strategic direction and monitoring progress. It spent a substantial amount of time at Board meetings in 2013 and 2014 discussing strategy, reviewing assurance arrangements and outcomes and endorsing the plan. The Board was given regular updates on the issues raised at meetings of the water forums and signed off the August data submission in July 2014.

The Board considered all further key submissions to Ofwat and was fully involved in analysing Ofwat's response to the plan and in all the work leading up to its re-submission on 2 May 2014, the further submissions to Ofwat in June and August 2014 and the representations on the Draft Determination submitted in July 2014. The Final Determination (FD) was published by Ofwat on 12 December 2014 and was carefully reviewed by the Board. After that review, the Board agreed unanimously not to contest the FD, and the Company worked with Ofwat to clarify certain details.

The Company's excellent operational performance is supported by the sound corporate governance standards maintained by the Board, which has regard to the principles underpinning the UK Corporate Governance Code (UK CGC) as required by the Company's Instrument of Appointment (the Licence). Whilst the Board does not consider that full compliance with all the detailed provisions of the UK CGC is practicable, given that NWL is privately owned, or is necessary for sound governance, the Board has embraced the key elements of the UK CGC's principles. The Corporate Governance report (on page 17 of these accounts) describes and explains areas of non-compliance with the relevant provisions of the UK CGC. The Board has also worked with Ofwat to develop a governance code, which balances the legitimate interests of all stakeholders and compliance with this code is confirmed on page 22 of these accounts.

The Board functions as an integrated whole and each director understands his or her individual responsibility to act in the best interests of the Company, as well as the importance of the service provided to our customers and our environmental responsibilities. All directors play a full part in Board meetings and shape the Company's strategy, as well as ensuring that customers' interests are central to investment and operational decisions. The involvement of our independent non-executive directors (INEDs) is critically important to NWL's governance and the Company has four, rather than the three required by its Licence. Paul Rew, our Senior INED, confirms in his report that the INEDs have full transparency on all the main aspects of NWL's governance and, importantly, participate in the Board meetings of our holding company, Northumbrian Water Group Limited.

CHAIRMAN'S STATEMENT (continued)

The Board, supported by the Risk & Compliance Committee, has overseen the development of a more resilient risk management framework, based on a 'bottom-up' risk assessment. The Risk & Compliance Committee receives regular updates on the top-rated risks and priorities for assurance and conducts 'deep-dives' into key areas of risk. Time has been set aside outside of the regular meeting schedule to consider strategic risk and the Committee is working with the Board to articulate the Company's risk appetite more clearly.

I can assure our stakeholders that NWL's special responsibilities as the only available provider of water and waste water services (for most of our customers) are recognised fully by the directors and influence all key decisions.

The Board will continue to drive the performance of the Company forward to ensure that our customers continue to receive exemplary service in 2015-16 and beyond.

Andrew J Hunter
Chairman

CHIEF EXECUTIVE OFFICER'S REPORT

I am pleased that our planning, hard work and investment in 2014-15 have resulted in service levels that continue to improve and are at the very forefront of industry performance. This brings us even closer to our aim 'to be the national leader in the provision of sustainable water and waste water services'.

- We have improved on our 2013-14 industry-leading performance for interruptions to supply.
- We have continued with our industry-leading sewage treatment look up table compliance.
- Our leading bathing water quality position has been regained.
- We have reduced the risk of internal sewer flooding for the largest number of properties ever in a single year and made further reductions in pollution incidents.
- Our work to address discoloured water contacts has reduced complaints significantly and met regulatory targets.
- Our Security of Supply Index (SoSI) is 100 for both our Northumbrian and Essex & Suffolk operating areas, now that the extended Abberton Reservoir is in service.
- We have achieved our leakage targets for the fourth consecutive year.
- We were second of the water and sewerage companies (WASCs) for the new qualitative Service Incentive Mechanism (SIM) measure (a result from the recent Water Service Regulation Authority (Ofwat) pilots).

Whilst this is an excellent set of outcomes, and we are justifiably proud of what we have achieved, we are not complacent and have plans to make further service improvements in 2015-16.

Now that we know performance in 2014-15, the last year of the AMP5 period, this allows us to reconcile performance against our FD regulatory contract for the price review period 2010 to 2015 (PR09). When changes agreed with regulators are taken into account, we have delivered on all of our commitments with only minor variations, defined by Ofwat as 'trivial'.

The last year has seen the completion of the periodic review of prices for 2015 to 2020 (PR14), which culminated in NWL agreeing the FD published by Ofwat. We listened to our customers so that we could produce a plan that reflected their priorities. Over the period 2015 to 2020, we will improve services across a range of measures, including a further reduction in flooding from sewers. With bills that will reduce slightly in real terms, we believe this package provides excellent value for our customers. Our aim will be to do even better than the minimum regulatory performance commitments wherever this is possible.

I am grateful to the members of our two independent Customer Challenge Groups (known in NWL as Water Forums), who challenged and advised us throughout the periodic review process on behalf of our customers and stakeholders. A number of members are leaving us, for various reasons, and I thank them all for their excellent contributions. We consider the Forums were a success and plan to continue with them in the future. We want to build on what we have learned and are undertaking a review, in liaison with Forum members and other stakeholders. This will help us design the structure, membership and remit of the Forums going forwards, with the aim of creating the best and most customer-focussed process we can achieve.

The opening of the water retail market in 2017 is coming ever closer, when all non-household customers, such as business customers, charities and public bodies, will be able to choose their retail supplier. We are working with Ofwat, Department for Environment, Food and Rural Affairs (DEFRA), Open Water and Market Operator Services Limited (MOSL) to help bring about the new arrangements whilst working on our own organisational changes to prepare us for market opening. In April 2014, we secured a retail licence to supply business customers and we are looking forward to competing successfully in the market and being the retailer of choice for business customers.

It is pleasing that Ofwat has already started its Water 2020 initiative, looking at the regulatory and market reforms necessary to meet future challenges. It is important this is completed in good time to inform the PR19 methodology. We are fully engaged in the debate and will continue to contribute to the 'market for ideas'.

CHIEF EXECUTIVE OFFICER’S REPORT (continued)

We fully support Ofwat’s transparency and confidence agenda and ensure the information we publish in both our financial statements and our annual performance report has been subject to stringent governance and assurance, overseen by the Board. We are also publishing a customer-facing annual performance review with its presentation using an innovative web-based approach.

I hope you find our financial statements helpful and informative.

H Mottram OBE
Chief Executive Officer (CEO)

STRATEGIC REPORT
for the fifteen months ended 31 March 2015

The Directors of NWL are pleased to present their strategic report on the affairs of the Company, along with their Directors' report, the audited statutory accounts and the auditor's report for the 15 month period ended 31 March 2015 and the regulatory accounts and the auditor's report for the year ended 31 March 2015.

On 20 November 2014 the Board approved the change of the Company's accounting reference date from 31 December to 31 March, therefore, the strategic report, Directors' report and statutory accounts relate to the period from 1 January 2014 to 31 March 2015. The regulatory accounts are prepared to comply with Condition F of the Company's Licence granted under the Water Industry Act 1991.

Cautionary statement

This report contains certain statements with respect to the future operations, performance and financial condition of NWL. By their nature, these statements involve uncertainty since future events and circumstances can cause results and developments to differ materially from those forecast. Such statements reflect knowledge and information available at the date of preparation of this report and the Company undertakes no obligation to update such statements. Nothing in this report should be construed as a profit forecast. Certain regulatory performance data contained in this report is subject to regulatory audit.

Business overview

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

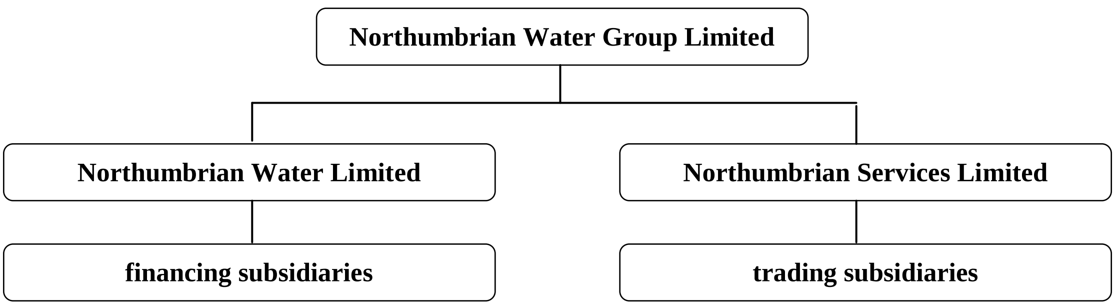
In the north east, the business comprises the supply of both potable and raw water and the collection, treatment and disposal of sewage and sewage sludge, serving 2.7 million people in the major population centres of Tyneside, Wearside and Teesside as well as the large rural areas of Northumberland and County Durham. We provide only waste water services in Hartlepool.

In the south, we supply water services to 1.5 million people in Essex and 0.3 million in Suffolk. Our Essex area is part rural and part urban and includes the main population centres of Chelmsford, Southend and the London Boroughs of Barking and Dagenham and Havering and Redbridge. Our Suffolk area is mainly rural with the largest towns being Great Yarmouth and Lowestoft.

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

Group structure

NWL owns a number of subsidiary companies which carry out financing activities on behalf of the Company (see Section A note 11) which, together with the Company, form the NWL group. NWL's immediate parent company, and controlling party at the balance sheet date, is Northumbrian Water Group Limited (NWGL). NWGL has one other direct subsidiary, Northumbrian Services Limited (NSL), which acts as a holding company for other non-regulated trading companies. NWGL and its subsidiaries together form the Group. The structure is shown in the chart below.



STRATEGIC REPORT (continued)

Group structure (continued)
At the balance sheet date, NWGL was indirectly wholly owned by Cheung Kong Infrastructure Holdings Limited (CKI), Cheung Kong (Holdings) Limited (CKH) and Li Ka Shing Foundation Limited.

On 3 June 2015, CK Hutchison Holdings Limited (CKHH), a company listed on the Hong Kong Stock Exchange, acquired CKH and (indirectly) Hutchison Whampoa Limited (HWL). As a consequence, CKHH gained control of both CKH and HWL's controlling interests in CKI, meaning that, in Directors' opinion, CKHH became the ultimate parent undertaking and controlling party of NWGL and, therefore, NWL.

Regulatory and legislative developments

PR14
In March 2014, NWL was commended by the regulator, Ofwat, for the high quality of its initial business plan, submitted in December 2013. After receiving further guidance from Ofwat, particularly in respect of their expectations on the balance of risk and reward, we resubmitted some elements of our plan in early May 2014. As a result, we received an early Draft Determination in late May 2014, to which we responded in July 2014. Throughout all this process, we retained the support of our Water Forums, stakeholder challenge groups, one in each operating area, established to provide constructive challenge to our plans. Our Board was fully involved and committed throughout the process.

We received our final determination of prices in December 2014, setting four separate price controls for 2015-20, for wholesale water and waste water and for household and non household retail. Average household bills will rise by less than inflation over the 2015-20 period. We have also agreed our business outcome statements, measures of performance and outcome delivery incentives for the period.

Retail competition for non households
The 2014 Water Bill was passed in May 2014. The most significant provision is the legislation to create a competitive market for retail water and waste water services for all non households with a target date for market opening of April 2017.

The development of a retail market has been led through the period by a high level steering group, on which NWL is represented. The delivery body, known as Open Water, has held many workshops throughout the period, in which we have actively participated, and has published a series of studies, consultations and an ongoing market blueprint on the design of the market. In May 2015, the third iteration of the Market Architecture Plan was published.

Ofwat has published an integrated plan for opening of the retail water market on its website. The plan sets out the various key activities that need to be undertaken by DEFRA, Ofwat, Open Water and water companies in order to implement the new market. This plan will be updated as the programme develops.

The work of Open Water is transitioning to Ofwat and MOSL, of which NWL was one of the three founding members. We will continue to support the programme as well as continuing our preparations for the organisational changes that the transition to market opening will require.

Changes in future financial and regulatory reporting
In November 2012, the Financial Reporting Council published Financial Reporting Standard (FRS) 100 'Application of Financial Reporting Requirements' which set out the future framework for financial reporting in the UK, replacing current UK Generally Accepted Accounting Practice (UK GAAP). For financial periods beginning on or after 1 January 2015, all companies in the UK will be required to adopt either full International Financial Reporting Standards, with a reduced disclosure framework available for qualifying subsidiaries under FRS 101; or a revised UK GAAP equivalent, FRS 102. The Board has approved that NWL will adopt FRS 101 with effect from 1 April 2015.

Changes in future financial and regulatory reporting (continued)

In February 2015, after a period of consultation, Ofwat published revised regulatory reporting requirements and accounting guidelines, to be effective for the regulatory year April 2015 to March 2016. All companies will be required to submit a single annual performance report which will replace the current requirements for regulatory accounts, per Section B of this report, and our annual performance review. The new report will include regulatory financial reporting, price control and additional segmental reporting, a summary of performance on outcomes and delivery service levels and additional financial and non-financial regulatory information.

Business strategy and objectives

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

We have underpinned our drive to be the best with five strategic themes, Competitiveness, Customer, People, Environment and Communities, described below, and achieving the right balance between them is essential to our success and reputation. As part of the PR14 process, we have developed a set of outcome statements, aligned to these themes, which encapsulate our long-term goals and what we aim to achieve.

Competitiveness:
- Our finances are sound, stable and achieve a fair balance between customers and investors.
- We are an efficient and innovative company.
- We are the retailer of choice for business customers.

Customer:
- We provide excellent service and impress our customers.
- Our customers consider the services they receive to be value for money.
- Our customers are well informed about the services they receive and the value of their water.
- We supply clean, clear drinking water that tastes good.
- We provide a reliable and sufficient supply of water.
- We provide a sewerage service that deals effectively with sewage and heavy rainfall.
- We deliver water and waste water services that meet the needs of current and future generations in a changing world.

People:
- Our people are talented, committed and inspired to deliver great services to customers.
- Our people act in line with our values.
- We are seen as a great place to work.
- Our workplaces are healthy and safe.

Environment:
- We protect and enhance the environment in delivering our services, leading by example.
- We help to improve the quality of rivers and coastal waters for the benefit of people, the environment and wildlife.

Communities:
- We are proud to contribute to the success of local communities.
- We work in partnership towards common goals.

STRATEGIC REPORT (continued)

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

One team – we work together consistently, promoting co-operation, to achieve our corporate objectives.

Customer focussed – we aim to exceed the expectations of our external and internal customers.

Results driven – we take personal responsibility for achieving excellent business results.

Creative – we continuously strive for innovative and better ways to deliver our business.

Ethical – we are open and honest in meeting our commitments, with a responsible approach to the environment and our communities.

Our progress in these areas during the period ended 31 March 2015 is described below and we continue to achieve the right balance between these key areas as this is essential to our success and reputation.

Performance
In order to measure delivery of the Company business plan and goals, a balanced scorecard of Key Performance Indicators (KPIs) is used spread across the strategic themes. Targets have been set by the Company, on a trajectory to deliver its vision, which are more stretching than the regulatory targets. In order to ensure alignment of the management team, this balanced scorecard represents 90% of the criteria contributing to their annual bonus, with a further 10% available for the achievement of bespoke personal targets. Further information about the executive Directors' remuneration is provided in note 10 to Section B, on page 72.

The table below details actual performance against the KPI targets and future targets. Targets which are measured on a calendar year basis, denoted by C in the table below, reflect the performance period January to December 2014. Targets which are measured on a regulatory year basis, denoted by R in the table below, reflect the performance period April 2014 to March 2015.

Scorecard measure	Performance period	2014-15			2015-16
		Target	Performance	Achieved	Target
Competitiveness					
Group EBIT	C	budget	achieved	Yes	budget
Group cash available for distribution	C	budget	achieved	Yes	budget
Customer					
Customer satisfaction					
- SIM qualitative score	R	>=4.7	4.59	No	>=4.65
- SIM quantitative score	R	<=90	91.66	No	<=63.75
Water supply interruptions >6 hours (average per property (minutes))	R	<=7.30	4.56	Yes	<=5.00
Coliform incidents (no.)	C	<=8	13	No	N/A
Mean zonal compliance	C	N/A	N/A	N/A	>=99.9
Repeat sewer flooding (properties)	R	N/A	N/A	N/A	<=269
People					
Employee engagement score	C	2*	1*	No	81%
Lost time reportable accidents (no.)	C	<=4	7	No	<=3
Environment					
Leakage (Mld)					
- NW	R	<=144	134.0	Yes	<=141
- ESW	R	<=66	58.4	Yes	<=66
STW failing LUT consent (%)	C	0	0	Yes	0
Pollution incidents (categories 1 & 2)	C	<=2	3	No	N/A
Communities					
BITC Platinum Plus accreditation	R	retain status	status retained	Yes	retain status
Just an Hour (employee participation)	C	>=50%	55%	Yes	>=50%

Performance (continued)
We are committed to our aspiration to deliver unrivalled customer service and to be the national leader in the provision of sustainable water and waste water services. We are making excellent progress towards this aim, making significant improvements to service in 2014-15. When all companies' performance is published we believe this will confirm that we have industry leading performance in a number of areas.

In April 2014 NWL was awarded the Queen's Award for Enterprise (sustainable development) for the second time, in recognition of our leading performance in sustainable development. The judges' comments highlighted our efforts in generating 20% of our energy from renewable sources, in particular through our advanced anaerobic digestion (AAD) processes, our use of reed-beds and investment to increase the capacity of Abberton reservoir. They also praised our work with the communities we serve.

Our 'Annual performance review 2014-15' provides further detail about the performance of our regulated business during the year. This is available on our websites (www.nwl.co.uk and www.eswater.co.uk).

Competitiveness
The competitiveness KPIs were successfully achieved in the year. The financial performance of the Company is detailed in the financial performance section later in this report.

The health of our assets remained satisfactory with serviceability, which measures how effectively we are operating and maintaining our substantial asset base to deliver an expected level of service now and into the future, assessed as stable in all asset classes.

In future periods we will monitor our asset health using baskets of measures that help us to ensure that the asset base is being properly maintained over time. As well as appropriate service related measures this also includes lead indicators of asset condition such as water mains bursts and sewer collapses.

Customer
Our customers and the quality of service we provide them remain central to our thinking and we are confident improvements will be seen over the coming year. Ofwat did not assess the SIM for 2014-15, however, we continued to measure it on a consistent basis. Whilst we failed to meet the stretching targets we set, with a slight dip in performance on the quantitative measure due to some temporary effects when we changed our way of operating to become more efficient and effective, our complaint numbers continue to drop steadily.

The SIM measure is changing for 2015-16 to focus more attention on the qualitative measure of customer experience, which we welcome, and during a recent Ofwat trial of the new SIM qualitative measure we were pleased to achieve joint second of all the WASCs. SIM will continue to include an assessment of unwanted customer contact and our work in getting service right first time has resulted in a 10% reduction in unwanted contact over the last three years. The quantitative target has been pro-rated to cover the nine month period April to December 2015.

To understand our customers' expectations we carry out extensive engagement through formal customer satisfaction tracking research and a daily survey, asking around 10,000 customers each week what they think of our service. Our net customer satisfaction score remained high at 88% whilst our net promoter score, used to benchmark ourselves outside the water industry, has increased from 24% in 2011 to 42% in 2014. We discuss our research with our Water Forums and CCWater for advice in interpreting the outcomes.

To help us to improve service on the ground we have invested in new workforce management tools and field equipment enabling our people to deliver improved customer service more efficiently. We are continuing with our investment in customer service systems and the provision of customer choice in how they wish to contact us. In the last year we have made it easier for customers to pay and access their accounts through our web services and have introduced a web chat option, as well as opening a new contact centre in Lowestoft.

Performance (continued)

Customer (continued)

Looking ahead, we have commenced a major programme to replace our legacy billing, collection and customer service systems, including reviewing how we deliver services to customers focussing on making the customer journey easier, faster and more efficient.

Through our customer engagement we have greatly improved our understanding of the pressures faced by our customers who are having difficulty paying their bills. Building on our successful partnership with the national debt charity ‘StepChange’, we have introduced two ‘SupportPLUS’ tariffs. The partnership reflects our commitment to understanding each customer’s financial situation in the round and working with them to find a sustainable solution. These schemes incentivise customers to get back into the payment habit and are funded by reducing bad debt costs.

Our strategy for drinking water quality remains focused on both public health and consumer confidence. We are committed to the supply of water which is healthy, clean and tastes good whilst continuing our delivery of schemes aimed at minimising discolouration contacts. Our drinking water quality standards remain very high, with sample pass rates of 99.94% in ESW and 99.95% for NW, and the microbiological performance at our treatment works and service reservoirs continued to improve with only 13 coliform failures recorded from 49,711 samples taken during the year, though not as low as our target, and we have developed robust action plans to help us meet our ambitious long term target of preventing these failures from occurring at all.

Since 2005 we have had an ongoing programme of work in place with DWI to reduce the number of discoloured water contacts received from consumers in NW region from 14,000 to below 4,000, and this was achieved in 2014, earlier than the undertaking commitment. This has been delivered through a major programme of large diameter trunk main cleansing, supported by other innovations such as unidirectional district metering area flushing, pipeline management to condition higher risk large mains and the development of two operational training centres.

We know that continuity of water supplies is important to our customers and we have achieved further improvements in reducing the average interruption time per property served, for which we are already industry-leading. Our SoSI remained at 100 for both operating regions and the period saw the enlarged Abberton reservoir completely filled with water for the first time ever, the climax of over 20 years work to promote and complete the project.

Internal sewer flooding is undoubtedly one of the worst service failures that our customers can experience and reducing sewer flooding is one of our highest business priorities. We are delivering a comprehensive investment programme to reduce the risk of sewer flooding for our customers and have also improved operational processes as well as increasing operational activity and providing property protection measures. This has helped to deliver a significant reduction in properties flooded over the past five years. In addition to increasing network capacity, we are working proactively with other agencies to introduce sustainable flood risk reduction solutions across our northern operating region.

People

We recognise that our success depends massively on the contribution of our employees and the extent to which they are willing to go the extra mile for customers and colleagues. The way that we do things is just as important as what we do and we have continued to train all of our people in Our Way, a tailored programme aimed at delivering excellent customer service internally and externally each and every time. We have also launched ‘Our Way at NWG’, a refreshed code of conduct clarifying how we expect our people to behave towards each other, our customers and suppliers.

We put great effort into creating an environment where people are encouraged to engage and perform to the best of their ability. A key part of this is being recognised as a great place to work. In 2014, we again entered the prestigious Sunday Times Best Companies survey and achieved One Star status. Whilst we were disappointed not to achieve our target of Two Star status, we are continuing to work with our employees to develop action plans to build on our current strong level of engagement. Our target for 2015-16 is to achieve an employee engagement score of 81%, measured by our internal employee survey, which we believe is in line with leading company performance.

Performance (continued)

People (continued)

In 2014, we refreshed the 'Our Vision, Our Values, Our Way' booklet to align with the business outcomes developed as part of the PR14 business planning process. This was communicated to everyone at one of our 55 employee roadshows. Supported by our Big Splash newspaper, our H2info weekly newssheet and our CEO's blog, our employee survey showed that 86% of our people felt that they were kept up to date with news and information. We maintain constructive employee relations through collaborative working with our trade union and employee representatives and actively engage with our people through an annual employee survey.

We have continued throughout the year to ensure that our people are fairly treated and we proactively promote diversity and inclusion to reap the benefits of a diverse workforce. Our equal opportunity policy seeks to ensure that all our current employees and potential employees are treated with respect. We welcome job applications from all parts of the community and it is our intention that all job applicants and employees are treated equally, regardless of their age, ability, marital or partnership status, race, religion or belief, gender or sexual orientation. At the end of the year, the company had 3,109 employees of which 2,108 were male and 1,001 female. Of the 12 Directors, 10 were male and 2 were female. The management team comprised 3 executive Directors (2 male and 1 female) plus a further 7 senior managers (4 male and 3 female).

We welcome employment applications from people with disabilities and, where existing employees develop disabilities, they are supported to remain in employment, wherever practicable, by providing appropriate adjustments to their roles and/or effective redeployments. Occupational health physicians assist this process with professional medical advice. We have been recognised with a gold award in the Business in the Community (BiTC) 'Opportunity Now' benchmarking index for gender equality and a silver award in the BiTC Race for Opportunity benchmarking index.

In 2014, we have continued to take a lead role to develop skills at a national level in response to the government's Employee Ownership of Skills pilot, and we are strongly represented at Council and Board level of the new Energy and Efficiency Partnership, an important sector wide initiative. NWL is also the water sector representative in the government's Trailblazer programme, where 60 leading companies are working to develop a brand new approach to apprenticeships in the UK.

Health and safety remains our top priority and in 2014, whilst lost time reportable accidents increased marginally to seven, above the stretching improvement target we had set, we saw a further reduction in total lost time injuries, from 18 to 13. Our biggest success in the year was the improvement in the identification of health and safety issues and near miss reporting through the success of our 'Spot-it' initiative. We have also seen an improvement in a number of leading health and safety indicators used to measure our performance which supports the change in culture required to achieve our lagging indicator targets. Our approach has gained external recognition and we recently won the Water Industry Sector 2015 Award from the Royal Society for the Prevention of Accidents for our health and safety management.

Environment

The environment is critical to us and our stakeholders and we acknowledge our responsibilities to protect and enhance the natural environment. Our carbon management plan is helping to reduce our carbon footprint and we aim to adopt good environmental practice in all aspects of our activity. Our integrated quality and environmental management systems are certified under ISO 9001, ISO 14001 and OHSAS 18001.

We continue to be the industry leader in sewage treatment operations with a seventh consecutive year of full compliance with consent standards. With our two AAD plants, we remain the first and only waste water company in the UK to use 100% of the sludge remaining after sewage treatment to produce renewable energy. We have further improved the process by cleaning and then injecting the generated gas direct to the gas grid, making our first injection of biomethane into the gas network in December 2014.

STRATEGIC REPORT (continued)

Performance (continued)

Environment (continued)

In 2014, all of the bathing waters in our area achieved the mandatory standard and 31 of 34 met the highest European water quality 'Guideline' standard, the highest pass rate in the country. In 2013, we introduced a new web page for customers to view real time alerts of spills from storm overflows which could temporarily affect bathing water quality and we are continuing to voluntarily provide real-time data on our sewer overflow discharges all year round.

The number of category 1 and 2 pollution incidents reduced from five to three and the total number of pollution incidents reduced from 133 to 90. To further improve our performance we continue to invest in sewer level monitoring technology and trend analysis to aid prediction of where pollution incidents are likely to occur and to detect and resolve problems at a warning level before they cause an overflow. We also added to the initiatives introduced in previous years with the concept of Water Rangers, encouraging members of the public to get involved by making regular observations on watercourses and alerting us to any unusual discharges.

For the fourth consecutive year, we achieved our targets on leakage in our northern and southern operating areas. We have continued with our vigorous promotion of water efficiency, exceeding the target for the 2010-2015 period and being recognised at the UK Water Efficiencies Awards.

Communities

We are dedicated to building strong relationships with the communities we serve and we ensure that corporate responsibility is embedded in the business. We support our communities in a number of ways focussing on five broad areas; investment in our communities, participation in our communities, educating our communities about their environment, supporting healthy communities and supporting developing communities through WaterAid.

More than 55% of our employees actively volunteered in their communities in 2014 through our Just an Hour scheme, supporting 713 different organisations and projects. This is a huge achievement and we are very proud of the contribution that our people are making to the communities in which we operate. In the year the Company was re-accredited as a Platinum Plus company by BiTC, their highest award.

Financial performance

In addition to the balanced scorecard, we use a range of financial indicators to monitor performance. All financial KPIs remained better than the target for the period, with the exception of Appointed business gearing, which increased to 67% as a result of the timing of a dividend payment being advanced by a month from April 2015 to March 2015, as explained below.

KPI	Target	Performance		Target
	2014-15	2014-15	2013	2015-16
Gearing: net debt to RCV[1] – NWL group[2] (%)	<70	68	63	<72
Gearing: net debt to RCV – Appointed business only (%)	<65	67	61	N/A
Cash interest cover (times) – NWL group	>3.0	3.3	3.8	>3.0
Cash flow to net debt (%) – NWL group	>13	20	18	>13

[1] Regulatory Capital Value (RCV)
[2] See Section A note 11.

The Company's profit and loss account and balance sheet are set out on pages 26 to 27. The statutory financial statements have been prepared on an historical cost basis in accordance with applicable Accounting Standards in the United Kingdom. The key accounting policies are summarised in note 1 to the statutory financial statements on pages 28 to 31 and these have been applied consistently throughout the current and preceding periods.

As a result of the change in accounting reference date, the current period values relate to a 15 month period and are, therefore, not directly comparable to the prior year values which reflect 12 months trading. However, once current period performance is adjusted for the impact of an exceptional asset impairment, described below, and the extended time period, the underlying operating profit performance for the current period is broadly in line with performance in the previous period.

Financial performance (continued)
Turnover was £984.9m for the fifteen months ended 31 March 2015 (year ended 31 December 2013: £774.6m). This reflected the application on water and sewerage charges of RPI of 2.6% less 1% in respect of the 2009 price review, with effect from April 2014. The average demand for measured supplies to household customers and total volumes supplied to non-household customers broadly stabilised in the period, after declines in prior years due to the difficult economic conditions.

Operating costs, including capital maintenance costs, for the fifteen months ended 31 March 2015 were £600.6m (year ended 31 December 2013: £443.4m). This included an exceptional one-off asset impairment charge of £30.7m in relation to sludge drying plant abandoned as a result of the successful implementation of AAD, which is explained further in Section A note 3(b) on page 32. Other cost movements reflected increases in manpower costs, power prices, depreciation and general inflationary increases, partially offset by the benefits of our efficiency programme. During the period, the Company invested £1.0m (year ended 31 December 2013: £1.1m) in research and development.

Our efficiency programme has continued to progress well and we have committed over £18m of sustainable operating efficiencies over the last two years, as well as significant capital efficiencies, through initiatives such as field workforce management, biomethane injection into the gas grid, operational process optimisation and transformation of support services. This positions us well to deliver our financial objective of being an efficient and innovative company.

Net interest payable was £138.5m in the fifteen months ended 31 March 2015 (year ended 31 December 2013: £119.1m). Whilst the charge is naturally higher due to the longer accounting period, the underlying charge is lower due to lower indexation on index linked debt, interest receivable on tax recoverable as a result of prior period capital allowances claims agreed with HM Revenue & Customs (HMRC) and a higher net receivable in relation to pension accounting.

Profit on ordinary activities before taxation for the fifteen months ended 31 March 2015 was £245.8m (year ended 31 December 2013: £212.1m). Current tax for the fifteen months ended 31 March 2015 was a credit of £17.1m (year ended 31 December 2013: £43.1m charge), including exceptional credit adjustments of £64.5m in respect of prior period capital allowances claims agreed with HMRC. Deferred tax for the fifteen months ended 31 March 2015 was a charge of £67.7m (year ended 31 December 2013: £53.7m credit), including adjustments in respect of prior periods of £46.2m, reflecting the exceptional capital allowances items in current tax. The current tax credit and deferred tax charge are explained in more detail in Section A note 8. Profit for the financial period was £195.2m (year ended 31 December 2013: £222.7m).

The Directors do not recommend payment of a final ordinary dividend (31 December 2013: £nil). Total dividends paid in the fifteen months ended 31 March 2015 were £311.5m (year ended 31 December 2013: £190.2m). Following a change in the Company's statutory accounting reference date, the timing of dividend payments has been amended, with the payment budgeted for April 2015 advanced by one month and paid in March 2015. As a consequence, a third interim dividend has been paid in the current period. This does not change the underlying dividend policy, and does not change the total dividend planned to be paid to shareholders in the calendar year to 31 December 2015. The dividend policy is explained in Section A note 9.

Capital investment
Total fixed asset additions in the fifteen months ended 31 March 2015 were £311.9m, representing capital investment to maintain and enhance our asset base.

Capital investment in the regulated business, net of grants and contributions, for the year ended 31 March 2015 was £229.5m under regulatory accounting guidelines (year ended 2014: £212.5m). This included £134.3m investment in maintaining the health of our assets, ensuring that stable serviceability was again achieved across all asset bases. We are working very hard to reduce the number of sewer flooding incidents and have delivered an extensive programme of investment in the regulatory year to address 552 properties.

STRATEGIC REPORT (continued)

Capital structure and liquidity
The Company's long term debt structure remained largely unchanged with 64% fixed at an average rate of 5.66%, 25% index linked at an average real rate of 1.59% and 11% on a variable rate basis (including short term funding from committed facilities). The blended average rate for the Company for the year ended 31 March 2015 was 4.82%.

In January 2014, the Company drew the first £50m tranche of a £100m facility from the European Investment Bank (EIB) on an index linked basis with a coupon of 0.34%. The remaining £50m was drawn in April 2014 on an index linked basis with a coupon of 0.38%. The Company is in preliminary discussions with the EIB regarding the provision of further investment funding over the next five year period.

In December 2014, the Company renewed its committed five year bank facilities, to maintain general liquidity, with a total value of £350m maturing in 2019. The undrawn bank committed facilities amounted to £258m at 31 March 2015.

Cash interest cover and gearing measures have remained consistent with the strong investment grade credit rating for the Company remaining at BBB+ stable (Standard & Poors and Fitch) and Baa1 stable (Moody's).

Treasury policies
The Board is responsible for the financing strategy of the Company which is determined within treasury policies set by NWGL. The treasury function's main purposes are to assess the ongoing capital requirement, to maintain short term liquidity, ensuring access to medium term committed back up facilities, and to raise funding, taking advantage of any favourable market opportunities. It also invests any surplus funds the Company has in accordance with the treasury policy. On occasion, derivatives are used as part of this process, but the treasury policy prohibits their use for speculation.

Principal risks and uncertainties
The Board sets the tone for risk management within the Company and determines the appropriate risk appetite. The Board's approach to monitoring, managing and mitigating risk is set out in the Directors' report.

The key business risks facing the Company are:

- funding and liquidity risk (explained below);
- unfavourable changes to the regulatory structure as a result of the Water Act 2014, such as upstream competition, a move away from RCV based regulation or a move away from RPI for indexation of RCV and allowed wholesale revenues;
- delivery of the change programme for readiness for the opening of the non-household retail market in 2017;
- loss of key business systems due to a malicious attack or failure of cyber security;
- breach of Data Protection Act or Environmental Information Regulations;
- loss of supply to a large volume of customers due to failure of the water systems, such as failure of a strategic water main or treatment works or contamination of a service reservoir; and
- environmental pollution incidents due to failures in the waste water network giving rise to potential fines and reputational damage.

Risk management is a dynamic process reflecting changes in the external environment and consequently some of the principal risks have changed from those reported in the previous year. In some cases, this is an increase in an existing risk, such as the loss of key business systems due to a malicious attack or failure of cyber security, whilst others relate to legal changes, such as the water industry being brought into scope of the Environmental Information Regulations. The risk related to non-household retail competition has been refined to reflect the development of the change programme.

Treasury activities

As noted above, the Company's financing strategy reflects its treasury policies and the Board reviews and agrees policies for managing each of these risks. These are summarised below. The treasury activities of the Company are conducted in accordance with these policies.

Funding risk

The level of capital expenditure which NWL is obliged to incur is such that we cannot be wholly financed by internally generated sources. As a result, we must rely upon raising additional finance on a regular basis, to be principally used to fund the long term assets required by the regulated business. In order to raise this finance efficiently, the Board's aim is to retain strong investment grade credit rating at BBB+ stable (Standard & Poors and Fitch) and Baa1 stable (Moody's). A reduction in the credit rating would likely restrict future sources of funding and increase the associated cost of new borrowing.

Liquidity risk

The Company's policy is to have available standby committed bank borrowing facilities with a value of no less than £50m and with a bank agreement availability period of no less than three months. At 31 March 2015, NWL had £258m (31 December 2013: £420m) of undrawn facilities, which mature in 2019.

Interest rate risk

The Company finances its operations through a mixture of retained profits and borrowings. It borrows at both fixed and variable rates of interest and, on occasion, uses derivatives to generate the desired interest profile and to manage its exposure to interest rate fluctuations. The Company's policy is to keep a minimum 50% of its borrowings at fixed rates of interest. At 31 March 2015, 64% (31 December 2013: 75%) of the borrowings of the Company were at fixed rates of interest. Index linked borrowings are treated as variable rate debt.

Credit risk

The Company invests surplus cash with banks on a short term basis. The treasury policy specifies which counterparties the Company can invest with and sets a limit for the maximum exposure to each counterparty. These limits take account of published credit ratings. The Company serves around 2 million properties and no individual customer accounts for a significant proportion of income or debt, therefore, there is no material customer credit risk. Note 1(o) of Section A sets out the Company's bad debt policy.

Foreign currency risk

The Company's policy is that any foreign currency exposure in excess of £100,000 sterling equivalent of a transactional nature, or £3m sterling equivalent of a translation nature, should be covered as soon as they are identified. At 31 March 2015, the Company had forward foreign exchange contracts of £2.7m (31 December 2013: £2.1m) for the purpose of hedging the foreign currency risk of committed future purchases.

Market price risk

The Company's exposure to market price risk principally comprises interest rate exposure. The Company's policy is to accept a degree of interest rate risk. On the basis of the Company's analysis, it is estimated that a 1% rise in interest rates would not have a significant effect.

By order of the Board

M Parker, Company Secretary,
13 July 2015

DIRECTORS' REPORT
for the fifteen months ended 31 March 2015

DIRECTORS

The Directors who served during the period were as follows:

A J Hunter	Non-Executive Chairman
P Rew *	Senior Independent Non-Executive Director
H Mottram OBE	Chief Executive Officer
C I Johns	Finance Director
G Neave	Operations Director (resigned 31 December 2014)
A C Jones	Assets and Assurance Director
M Fay CBE *	Non-Executive Director
Dr S Lyster *	Non-Executive Director
M A B Nègre *	Non-Executive Director
F R Frame	Non-Executive Director
T C E Ip	Non-Executive Director
H L Kam	Non-Executive Director
D N Macrae	Non-Executive Director
L S Chan	Alternate Non-Executive Director
W C W Tong-Barnes	Alternate Non-Executive Director

* Independent Non-executive Directors.

Information about Directors' remuneration is contained in note 5 in Section A and note 10 in Section B to the accounts.

SENIOR INDEPENDENT NON-EXECUTIVE DIRECTOR'S REPORT

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

As mentioned by the Chairman, the INEDs play a key role in NWL's governance and decision making. I chair the Audit and Risk & Compliance Committees and other INEDs are members of both those Committees and the Remuneration Committee. We therefore have full transparency on all the main aspects of NWL's governance and the internal performance review conducted this year indicated that the members believe the Committees provide good support to the Board in ensuring that sound governance is maintained. Whilst these Committees are not entirely comprised of INEDs, as suggested by the UK CGC, the Board is satisfied that the composition of the Committees is appropriate to the Company's circumstances. The INEDs also meet from time to time without management or the other directors being present.

Most decisions relating to NWL are made by the NWL Board alone and the only decisions referred to the NWGL Board are certain large contract awards, capital project approvals, substantial funding arrangements and the re-appointment of certain Directors. During the last year, the NWGL Board has endorsed all the recommendations of the NWL Board. Although the INEDs are not members of the NWGL Board, we are present at its Board meetings and participate fully, encouraging a cohesive approach at both Boards. Dr S Lyster, M Fay and I also sit on the Company's Corporate Responsibility Management Group.

The INEDs have participated fully in all aspects of the PR14 process. Dr S Lyster and I sat on the Board's PR14 sub-group from the start and we were joined by a third INED, M Fay, as the key decision-making time approached. Two other NEDs and the Executive Directors also took part.

SENIOR INDEPENDENT NON-EXECUTIVE DIRECTOR'S REPORT (continued)

The sub-group met monthly, and latterly more frequently, to advise management, challenge proposals and facilitate more detailed Board involvement.

I would like to emphasise that, in addition to our work on PR14 and our participation in formal meetings, the INEDs have had very broad involvement in NWL's overall business. We have taken part in extensive sessions with management on water resources and customer service and have had regular direct exposure to customers, through stakeholder events and other channels.

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

P Rew
Senior Independent Non-Executive Director

CORPORATE GOVERNANCE

Corporate Governance obligations

The Company's Licence contains provisions, beyond those which would otherwise apply to a private company, to ensure that the Company's governance is sound and that its Directors, acting as such, act independently of parent companies. The Licence requires the Company to have particular regard to the UK CGC.

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

The Board considers that it complies substantially with the relevant provisions of the UK CGC, to the extent that it is compatible with NWL's ownership structure, except as explained on pages 21 to 22.

INEDs and the Company's Licence

The Licence requires the Company to obtain undertakings from its ultimate controllers to underpin the Licence and to require the Company's Board to include 'not less than three independent non-executive Directors, who shall be persons of standing with relevant experience' and who have collective knowledge of, and connections with, the Company's areas of supply and customers. Throughout the year, the Company had four INEDs, as detailed below. P Rew, Dr S Lyster and M Fay were the three INEDs for the purpose of the Licence.

P Rew, who is a chartered accountant and was a partner in PricewaterhouseCoopers LLP (PwC) from 1987 until 2010, where he was lead partner for a diverse range of FTSE 100 clients and for PwC's UK energy, utilities and mining sector practice. He is a non-executive Director of the Met Office, DEFRA and the Care Quality Commission and chairs their Audit Committees. P Rew has been a Director of NWL since 2010. He is Chairman of the Audit Committee and the Risk & Compliance Committee and is also a member of the Remuneration Committee.

Dr S Lyster, who is a lawyer by training, qualified in both the UK and the USA, was Chief Executive of LEAD International from 2005 to 2011. Before joining LEAD, he was Director General of The Wildlife Trusts and previously worked for World Wildlife Fund for nine years, where he was responsible for its global policy work on international conventions. He is Chairman of the World Land Trust and a Trustee of Conservation International–UK, the Kilverstone Wildlife Conservation Trust and the Rural Community Council of Essex. In July 2014 Dr Lyster was appointed to the Board of Natural England. Dr Lyster has been a Director of NWL since 2006 and is a member of the Audit Committee and the Risk & Compliance Committee.

CORPORATE GOVERNANCE (continued)

INEDs and the Company's Licence (continued)

M Fay, who was Managing Director of Tyne Tees Television until December 2003 when she became Chairman of One North East, a position she held until August 2010. She is Deputy Chairman of The Sage Gateshead, a Governor of the University of Sunderland, Patron of Tees Valley Community Foundation and the Prince of Wales' Ambassador for the north east of England. M Fay has been a Director of NWL since 2010 and is a member of the Remuneration Committee.

M Nègre, who was, between April 2000 and April 2001, the CEO of the former Northumbrian Water Group plc and the chief corporate representative of its parent company, Suez, in the UK. He currently chairs Ecofin Vista Hedge Fund Limited, is a non-executive Director of listed Investment Trust EW & PO plc and holds a number of Directorships focused on utilities. He is a Director of Promethean plc, an AIM-listed investment company, and sits on the supervisory board of Messieurs Hottinger & Cie. M Nègre has been a Director of NWL since 2006 and is a member of the Audit Committee and the Risk & Compliance Committee.

The INEDs attend and participate in decisions at all NWGL Board meetings and at meetings of NWGL's Audit, Risk & Compliance and Remuneration Committees. Whilst these are formally constituted at the NWGL level, the vast majority of their work relates to the Company's activities. The INEDs therefore play a full part in all strategic decisions both at the NWL and NWGL Boards. All Directors' views are given full consideration and due weight in all proceedings of the Board and Committees. The precise membership of the Committees is set out below, as are details of their work.

Board responsibilities and processes

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

The Company has adopted terms of reference which set out the matters reserved to the Board for approval and matters which are, or can be, delegated to the Committees and management. The Company has also adopted financial approval rules which set out the authorisation processes and financial limits to be applied to financial transactions within the Company. The terms of reference and financial approval rules are reviewed regularly by the Board and, with effect from 1 April 2015, such reviews will be conducted at least annually. The Standing or Executive Committees can take decisions not delegated to specific committees between Board meetings. All Directors receive notice of Standing Committee meetings and may participate if they wish. Decisions taken by the Standing or Executive Committees are reported at the next Board meeting. The Company's Board meets at least five times each year.

Authorisation of Directors' conflicts of interest

Directors have a statutory duty, under s175 of the Companies Act 2006, to avoid a situation in which they have, or could have, a conflict of interest with the Company's interests. However, there is no breach of this duty if the Board has authorised the matter in question. The Articles permit Directors (other than the Director having the interest in question) to authorise any situation giving rise to a known or potential conflict. A register of the interests which have been authorised is maintained by the Company Secretary and is available at every Board meeting.

Board balance and independence

The composition of the Board is as follows:

A J Hunter (Chairman) and D N Macrae were appointed by CKI, which is listed on the Hong Kong Stock Exchange and is a substantial shareholder in the Company. A J Hunter is Deputy Managing Director of CKI and is an executive Director of Power Assets Holdings Limited, a listed company. D N Macrae is Head of International Business for CKI.

CORPORATE GOVERNANCE (continued)

Board balance and independence (continued)
H L Kam and T C E Ip were appointed by CKH, which is a substantial shareholder in the Company and is now wholly owned by CKHH. H L Kam is Group Managing Director of CKI and Deputy Managing Director of CKHH. T C E Ip is Deputy Chairman of CKI and Deputy Managing Director of CKHH.

F R Frame was appointed by Li Ka Shing Foundation Limited, a company limited by guarantee and a charity, which is a substantial shareholder in the Company.

The CEO, H Mottram, and the three INEDs for the purposes of the Licence (P Rew, Dr S Lyster and M Fay) were appointed on the recommendation of the Nomination Committee of Northumbrian Water Group plc when it was independently listed.

M Nègre was a founding Director of NWGL when it acquired the Group from Suez SA in 2003 and has served as a Director on the NWL Board since 2006. G Neave, the former Operations Director, joined the Board of NWL in January 2002 and retired on 31 December 2014 and A C Jones, the Assets and Assurance Director, joined in January 2004. C I Johns, Finance Director, joined on 1 January 2013.

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

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

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

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

The Board has performed an assessment of the principal risks facing the company, including those that would threaten its business model, future performance, solvency or liquidity. The Board requires management to identify and assess the impact of risks to the business using a risk model. In addition, during the period, a sub group of the Board carried out a review of strategic risks, being potentially high impact risks which are foreseeable but with a high degree of uncertainty. The Board's view of acceptable risk is based on a balanced view of all of the risks in the operating environment and it aims to ensure an appropriate balance between risk aversion and opportunities.

The management team reviews the approach to risk management in detail every year and reviews the significant risks every month. Any issues are reported by the CEO to the Board. Senior management implements policies on risk management and internal control.

The system of internal control incorporates risk management. It encompasses a number of elements, including policies and procedures, business planning and budgeting and the maintenance of a risk management framework, that together facilitate an effective and efficient operation, enabling the Company to respond effectively to a variety of challenges. The principal risks facing the Company are described on page 14 in the Strategic Report.

DIRECTORS' REPORT (continued)

CORPORATE GOVERNANCE (continued)

Board committees

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

Remuneration Committee

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

The work of the Remuneration Committee is explained in note 10 of Section B. The Company complies with its obligations under Section 35A of the Water Act 2003 by disclosing in its regulatory accounts a detailed breakdown of remuneration paid to the Executive Directors of NWL, which includes those elements linked to NWL's standards of performance.

Audit Committee

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

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

- reviewing the draft statutory and regulatory accounts, considering reports from the external auditor setting out the audit approach and plan, significant audit risks and conclusions on the Group's internal controls and risk management;
- reviewing the appropriateness of accounting policies, significant accounting judgements and evidence supporting the going concern basis for the accounts and recommending approval of both statutory and regulatory accounts to the Board;
- reviewing and commenting on the annual performance review, including the underlying assurance, reviewing evidence to support the Condition F6A.2A certificate (statement of sufficiency of financial resources) and recommending its approval to the Board;
- reviewing the approach to Board assurance for the regulatory price review process, monitoring progress of the assurance for all submissions after the initial business plan and receiving reports from the independent assurance advisor;
- monitoring the development of the effectiveness of the internal audit function, following a report carried out by an external co-sourcing partner, and continuing implementation of an action plan to build on the existing strong base;
- approving the external auditor's fees for both audit and non-audit services, by reference to the agreed policy;
- approving the internal audit work programme for the year and reviewing progress against the programme;
- approving arrangements for monitoring compliance with the Company's procedures designed to prevent bribery, having regard to the Bribery Act 2010 and the updated code of conduct 'Our Way at NWG', including receiving reports on any whistleblowing allegations;
- reviewing the risk and control framework and reporting, including management of tax compliance matters and approval of financial approval rules; and
- conducting an internal review of the effectiveness of the Audit Committee (jointly with the Risk & Compliance Committee). The findings were generally very positive and identified only a small number of items requiring further action.

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

CORPORATE GOVERNANCE (continued)

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

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

- reviewing and approving the implementation of a significantly enhanced risk management framework and corporate risk register, based on a detailed bottom-up assessment of risk across the Company and departmental risk registers developed by risk champions in each department;
- reviewing reports at each meeting on the top rated managed risks and priorities for assurance (being those risks with the biggest reduction between the business (gross) and managed (net) risk scores), representing key control areas for the Company;
- reviewing the management of specific areas of risk in relation to health and safety, the vehicle operator's licence and environmental compliance;
- reviewing cyber security and steps being taken to enhance security;
- advising the Board on risk appetite and exposure and reviewing risk assessment processes as well as keeping the effectiveness of the risk and internal control management systems under review;
- monitoring compliance with covenants and treasury risks;
- reviewing management of customer debt;
- reviewing business continuity arrangements; and
- conducting an internal review of the effectiveness of the Risk & Compliance Committee (jointly with the Audit Committee and with similar positive findings as noted above).

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

The Board is able to monitor the impact of environmental, social and governance matters on the Company's business, to assess the impact of significant risks on the business and to evaluate methods of managing these risks through reports it receives from the Audit Committee and the Risk & Compliance Committee.

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

<u>Code Provisions</u>
A.3.1: The Chairman was appointed by the Group's shareholders.

A.4.2: The Chairman has informal discussions with the Non-executive Directors as the need arises, though it has not been necessary to hold formal meetings with them without the executives present. The Non-executive Directors have not appraised the performance of the Chairman, but the Company has confirmed in its governance document, referred to below, that it intends to commence such appraisals with effect from April 2015.

B.1.1: The Board has determined that M Nègre is independent, notwithstanding that he served on the NWGL Board for more than nine years and has served on the NWL Board since 2006. M Nègre has no prior connections with the Group's shareholders. He is a very experienced Director, and brings to the Board an excellent understanding of the business coupled with sound commercial judgment. He continues to contribute a constructive and challenging perspective to Board discussions. The Board is therefore satisfied that M Nègre is independent for the purposes of the UK CGC.

DIRECTORS' REPORT (continued)

CORPORATE GOVERNANCE (continued)

The UK Corporate Governance Code (continued)

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

B.2.1, B.2.2 and B.2.4: There is not a permanent Nomination Committee. The Company has confirmed (in its governance document) that new INEDs and executive Directors will be appointed on an objective basis and by means of a formal, rigorous and transparent procedure, in which all Non-executive Directors will participate. Moreover, the Board has agreed to ensure that the recruitment process for INEDs is such that a diverse range of candidates is encouraged to apply.

B.4: INEDs receive induction on joining the Board and continually update their knowledge of and familiarity with the Company. The Chairman does not formally review with each Director their training and development needs. For Executive Directors this is managed by the CEO; Independent Directors keep up to date with developments in the sector via updates at Board meetings and external seminars.

B.6: The Company has confirmed its intention to conduct performance evaluations in accordance with principle B.6 with effect from April 2015. An internal review of the performance of the Audit and Risk & Compliance Committees was conducted in February 2015 and the findings were reported to, and discussed by, the Committees in April 2015. The performance of Executive Directors is appraised by the CEO and all Executive Directors participate in NWL's extensive 360^{o} feedback system.

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

D.1: The Company's policy on remuneration and the detailed remuneration disclosures are set out in note 10 of Section B.

D.2.1: The membership of the Remuneration Committee is disclosed on page 20, and this is considered to be appropriate given the Company's ownership.

Schedule B: There were ten Board meetings during the period, as well as six meetings of the Audit Committee, four meetings of the Risk & Compliance Committee and four meetings of the Remuneration Committee. Attendance at Board meetings was 88%, whilst attendance at the Audit, Risk and Compliance and Remuneration Committees was 87%, 90% and 100%, respectively.

Northumbrian Water Limited Board Governance Code

In March 2014, following discussions with Ofwat, the Board put in place a bespoke Governance Code (the NWL Code), which is available on the NWL website. The Company complies with the NWL Code, including the statements regarding the composition of the Board as at 1 April 2015 and the commencement of performance evaluations in 2015.

Code of Conduct

The Group has a code of conduct, 'Our Way at NWG', covering its relationships with customers, employees, suppliers, local communities, shareholders, other investors and regulators. This document was updated during the year and now provides clearer guidance to employees in relation to personal conduct, conflicts of interest and a number of other matters.

OTHER DISCLOSURES

Results and dividends

Information on results and dividends is contained in the Financial Performance section of the Strategic Report.

OTHER DISCLOSURES (continued)

Post balance sheet event

A change in the Company's ultimate parent undertaking and controlling party, which occurred after the balance sheet date, is explained in the strategic report, on page 6, and in note 28.

Financial instruments and treasury policies

Our policies in relation to the use of financial instruments and treasury operations are set out in the Strategic Report under the 'Treasury policies' heading.

Employment policies

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

Political donations

NWL does not support any political party and we do not, directly or through any subsidiary, make what are commonly regarded as donations to any political party or other political organisation. However, the wide definition of donations in the Political Parties, Elections and Referendums Act 2000 covers activities which form part of the necessary relationship between the Company and political parties and political organisations. These activities include attending party conferences, as these provide the best opportunity to meet a range of stakeholders, both national and local, to explain our activities, as well as local meetings with MPs, MEPs and their agents. The costs associated with these activities during the year were as follows:

Name of political party	£
Conservative	1,185
Labour	4,488
Liberal Democrats	1,758
Total	**7,431**

Greenhouse gas emissions

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

Our total net operational GHG emissions for the year ended 31 March 2015 were 213.6 ktonnes CO2e (31 March 2014: 199.7 ktonnes CO2e). Our emissions can be considered in terms of those we can control and those we have no influence over. In terms of the emissions under our control, by our efforts, these reduced by four ktonnes CO2e from 2013-14 to 2014-15, continuing the trend of year on year reduction since 2008. However, the emissions factor for grid electricity, which is influenced by the mix of types of generation feeding the grid, rose by 11% over the prior year, resulting in our reported emissions being around 17 ktonnes higher than they otherwise would have been if the factor had remained constant.

Our carbon management plan has the aim of reducing our GHG emissions by 35% by 2020 against a 2008 baseline, which would mean that total emissions would fall by 50% if government expectations on grid emissions reduction were met. We remain ahead of target with emissions down by 30% compared to the 2008 baseline, in spite of the emissions factor being almost 3% higher than when we established our target.

In addition to absolute emissions we also monitor the emissions intensity of our operations using three measures, one relating to the water service and two for wastewater. It should be noted that these measures can be volatile depending upon levels of rainfall and pumping requirements, therefore we focus on longer term trends.

OTHER DISCLOSURES (continued)

Greenhouse gas emissions (continued)

Annual operational GHG intensity ratio	2014-15	2013-14
Emissions/Ml of water	246	224
Emissions/Ml of sewage treated (flow to full treatment)	300	264
Emissions/Ml of sewage treated (water distribution input)	540	506

Figures in kgCO2e/Ml

Directors' indemnification

NWGL had Directors' and officers' insurance in place for the period to 31 March 2015. On 28 November 2005 NWGL entered into a deed of indemnity to grant the Directors of NWGL and its subsidiaries further protection against liability to third parties, and this remains in place.

Directors' statement

As required under s418 of the Companies Act 2006, so far as each current Director is aware, there is no relevant audit information of which the Company's auditor is unaware and each Director has taken all the steps that he or she ought to have taken as a Director in order to make himself or herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

Auditor

Pursuant to s487 of the Companies Act 2006, Deloitte LLP is deemed to be re-appointed as the Company's auditor for the ensuing year.

Financial statements preparation and going concern

The Directors confirm that, in their opinion, the Company has sufficient financial resources and facilities available to enable it to carry out its activities for at least the next 12 months. Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements. In arriving at their decision, the Directors have taken into account:

- the financial strength of the Company at the balance sheet date and financial performance, which is in line with expectations and reviewed at each Board meeting, most recently in April 2015;
- the key financial ratios over the next 12 month planning horizon, as reflected in strong investment grade credit ratings with stable outlook;
- the fact that the Company has arranged £350m of five year committed bank facilities as back up liquidity (maturing in 2019), of which £258m remains undrawn at 31 March 2015; and
- the Company's formal risk and governance arrangements which are monitored by the Audit Committee, Risk & Compliance Committee and Board.

Viability statement

The Directors believe that the Company is well placed to manage its business risks successfully and expect that the business can continue to operate effectively over the long term. In arriving at their opinion, the Directors have taken into account:

- the Licence which is in place on a rolling 25 year basis;
- the certainty on wholesale and household retail price controls to March 2020 provided by the 2014 Final Determination by Ofwat, following its acceptance by the Board;
- the financial strength of the Company at the balance sheet date and the fact that the Company has arranged £350m of five year committed bank facilities as back up liquidity (maturing in 2019), of which £258m remains undrawn at 31 March 2015;
- the key financial ratios over the planning horizon of the Company's five year medium term plan to 2019 as reflected in strong investment grade credit ratings with stable outlook; and
- the Company's formal risk and governance arrangements which are monitored by the Audit Committee, Risk & Compliance Committee and Board.

Directors' responsibilities statement

The Directors are responsible for preparing the report and the financial statements in accordance with applicable law and regulations.

DIRECTORS' REPORT (continued)

OTHER DISCLOSURES (continued)

Directors' responsibilities statement (continued)
Company law requires the Directors to prepare financial statements for each financial period. Under that law the Directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), with certain exceptions required by Ofwat which are detailed in note 1a of Section B. Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing these financial statements, the Directors are required to:
- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping proper accounting records which are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors consider that the report and financial statements, taken as a whole, is fair, balanced and understandable and provides the information necessary for stakeholders to assess the company's performance, business model and strategy. In reaching this conclusion, the Board has taken advice from the Audit Committee which has considered the process by which the report and financial statements has been produced as well as reviewing and commenting on the report.

The Directors are responsible for the maintenance and integrity of the corporate and financial information on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By order of the Board

M Parker,
Company Secretary,
13 July 2015

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

Registered in England and Wales
Registered no: 2366703

PROFIT AND LOSS ACCOUNT
for the fifteen months ended 31 March 2015

	Note	15 months ended 31 March 2015	12 months ended 31 December 2013
		£'m	£'m
Turnover	2	984.9	774.6
Operating costs	3(a)	(392.1)	(308.0)
Capital maintenance costs	3(b)	(208.5)	(135.4)
Total operating costs		(600.6)	(443.4)
OPERATING PROFIT		384.3	331.2
Net interest payable	4	(138.5)	(119.1)
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION		245.8	212.1
Taxation	8(a)	(50.6)	10.6
PROFIT FOR THE FINANCIAL YEAR	23	195.2	222.7

All results are from continuing operations in the United Kingdom.

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
for the fifteen months ended 31 March 2015

	Note	15 months ended 31 March 2015	12 months ended 31 December 2013
		£'m	£'m
Profit for the financial period		195.2	222.7
Pension liability actuarial gain in the period	25	7.6	25.2
Deferred tax related to pension adjustments	25	(1.5)	(9.6)
Total recognised gains and losses relating to the period		201.3	238.3

BALANCE SHEET
at 31 March 2015
(Registered number 2366703)

	Note	31 March 2015	31 December 2013
		£'m	£'m
FIXED ASSETS			
Tangible assets	10	3,880.6	3,783.9
Investments	11	160.9	160.9
		4,041.5	3,944.8
CURRENT ASSETS			
Stocks	12	2.3	2.8
Debtors due in less than one year	13	251.5	176.4
Debtors due in more than one year	14	1.0	1.0
Cash at bank and in hand		-	22.8
		254.8	203.0
CREDITORS			
Amounts falling due within one year	15	(387.0)	(286.6)
NET CURRENT LIABILITIES		(132.2)	(83.6)
TOTAL ASSETS LESS CURRENT LIABILITIES		3,909.3	3,861.2
CREDITORS: Amounts falling due after more than one year	16	(2,391.5)	(2,316.7)
PROVISIONS FOR LIABILITIES AND CHARGES	20	(248.7)	(179.7)
ACCRUALS AND DEFERRED INCOME	21	(398.2)	(383.7)
		(3,038.4)	(2,880.1)
NET ASSETS EXCLUDING PENSION LIABILITY		870.9	981.1
Pension liability	25	(69.4)	(69.4)
NET ASSETS INCLUDING PENSION LIABILITY		801.5	911.7
CAPITAL AND RESERVES			
Called up share capital	22	122.7	122.7
Profit and loss account	23	678.8	789.0
SHAREHOLDERS' FUNDS	23	801.5	911.7

Approved by the Board of Directors on 13 July 2015 and signed on their behalf by:

H Mottram

NOTES TO THE STATUTORY FINANCIAL STATEMENTS for the fifteen months ended 31 March 2015

1. STATEMENT OF ACCOUNTING POLICIES

These financial statements have been prepared in accordance with applicable Accounting Standards in the United Kingdom. A summary of the principal accounting policies is set out below. These have been applied consistently throughout the current and preceding periods.

(a) Basis of accounting

The financial statements have been prepared under the historical cost convention. The Company is exempt by virtue of section 400 of the Companies Act from the requirement to prepare group financial statements, as it is included in the group financial statements of NWGL. The financial statements, therefore, present information about the individual company only.

The financial statements have been prepared on a going concern basis, having considered the principal risks and uncertainties, which assumes that the Company will have adequate funding to meet its liabilities as they fall due in the foreseeable future. As at 31 March 2015, the Company had net current liabilities of £132.2m (31 December 2013: £83.6m). The Directors have reviewed cash flow requirements and are confident that they will be able to meet these from funds available, including the undrawn committed bank facilities of £258m (31 December 2013: £420m). Accordingly, the Directors believe it is appropriate to prepare the financial statements on a going concern basis.

(b) Turnover

Turnover, which excludes Value Added Tax, represents the income receivable in the ordinary course of business for services provided within the United Kingdom. All water and sewerage charges billed to customers are recognised pro-rata over the period to which they relate. For consumption by measured customers which has not yet been billed, an accrual is estimated.

(c) Cash flow statement

The Directors have taken advantage of the exemption in FRS 1 (revised) and have not included a cash flow statement on the grounds that the Company is wholly owned and its ultimate parent undertaking and controlling party publishes a consolidated cash flow statement.

(d) Tangible fixed assets and depreciation

Tangible fixed assets comprise:

(i) Infrastructure assets

Infrastructure assets comprise a network of systems which include water mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls.

Expenditure on infrastructure assets relating to increases in capacity, or enhancements of the network, and on maintaining the operational capability of the network, in accordance with defined standards of service, is treated as additions which are included at cost. Costs include external and internal costs to bring the asset into use.

The depreciation charge for infrastructure assets is based on the Company's independently certified asset management plan which has estimated the level of expenditure required to 2020 to maintain the operating capability of the network. This is adjusted if the forecast expenditure is expected to differ significantly from the amounts included in the original plan.

(ii) Non-infrastructure assets

Other assets are included at cost less accumulated depreciation and, where required, provision for impairment. Additions are included at cost.

1. STATEMENT OF ACCOUNTING POLICIES (continued)

(d) Tangible fixed assets and depreciation (continued)

(ii) Non-infrastructure assets

Freehold land is not depreciated. Other assets are depreciated evenly to their estimated residual values over their estimated economic lives, which are principally as follows:

Freehold buildings	30 – 60 years
Operational structures, plant and machinery	4 – 92 years
Fixtures, fittings, tools and equipment	4 – 10 years

Where the remaining useful economic life of the asset is estimated to be greater than 50 years, an impairment review is performed at the end of each reporting period to ensure that the carrying amount can be supported.

(iii) Assets in the course of construction

Assets in the course of construction are not depreciated until commissioned, which is when the asset is available for use.

(e) Grants and contributions

Capital grants and contributions are treated as deferred income and amortised to the profit and loss account over the expected useful economic lives of the qualifying assets. Specifically in the case of infrastructure assets, the expected useful economic lives have been determined by reference to the physical replacement cycle of these assets.

(f) Hire purchase and leasing

Where assets are financed by hire purchase or leasing arrangements which transfer substantially all the risks and rewards of ownership to the Company, the assets are treated as if they had been purchased and the corresponding capital cost is treated as a liability. Rentals or leasing payments are treated as consisting of a capital element and finance costs, the capital element reducing the outstanding liability and the finance costs being charged to the profit and loss account over the period of the hire purchase contract or lease in proportion to the reducing outstanding liability.

Rental costs arising under operating leases are charged to the profit and loss account in the period in which they are incurred.

(g) Stocks

Raw materials and consumables are stated at cost less any provision necessary to recognise damage and obsolescence.

(h) Pension costs

The Company is the principal employer of the Northumbrian Water Pension Scheme (NWPS or the Scheme), which has both a defined benefit section and a defined contribution section. The Scheme is accounted for in accordance with FRS 17 Retirement Benefits.

The defined benefit sections provide benefits based on final pensionable remuneration. The Scheme assets are measured at fair value and the scheme liabilities are measured at present value. The difference between the assets and liabilities is recognised in the balance sheet. The current service cost, past service cost, settlements and curtailments are recognised within operating costs in the profit and loss account. The expected return on plan assets and the change in present value of scheme obligations are recognised in the profit and loss account as interest receivable and interest payable, respectively. Actuarial gains and losses on experience adjustments and changes in actuarial assumptions are recognised in the statement of total recognised gains and losses.

The costs of the defined contribution section are charged to the profit and loss account in the period they arise.

1. STATEMENT OF ACCOUNTING POLICIES (continued)

(i) Taxation

The charge for current UK corporation tax is based on the profit for the period as adjusted for taxation purposes using the rates of tax enacted or substantively enacted by the balance sheet date.

Provision is made for deferred tax in respect of all timing differences that have originated but not reversed at the balance sheet date that will result in an obligation to pay more, or a right to pay less, tax in future periods. Deferred tax is calculated at the tax rates that are expected to apply in the periods in which timing differences are expected to reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date.

Deferred tax assets are recognised only to the extent that the Directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

As permitted by FRS 19, the Company has adopted a policy of discounting deferred tax assets and liabilities to reflect the time value of money over the period between the balance sheet date and the dates on which it is estimated that the underlying timing differences will reverse. The discount rates used reflect the post-tax yields to maturity that can be obtained at the balance sheet date on government bonds with similar maturity dates to those of the deferred tax assets or liabilities.

(j) Foreign currency

All transactions denominated in foreign currencies are translated into sterling at the actual rates of exchange ruling at the date of transaction. Foreign currency balances are translated into sterling at the rates of exchange ruling at the balance sheet date. Exchange gains or losses are recognised in the profit and loss account in the period incurred.

(k) Research and development

Research and development expenditure is charged to the profit and loss account in the period in which it is incurred.

(l) Fixed asset investments

Fixed asset investments are stated at their purchase cost, less provision for diminution in value.

(m) Derivative financial instruments

The Company utilises interest rate swaps, forward rate agreements and forward exchange contracts as derivative financial instruments. In accordance with the Companies Act 2006, disclosure is given of the nature and extent of each class of derivative held by the Company, along with the fair value of the derivatives, by class, at the balance sheet date. No amounts are shown in the balance sheet of the Company in respect of these derivatives at 31 March 2015.

A derivative instrument is considered to be used for hedging purposes when it alters the risk profile of an underlying exposure of the Company in line with the Company's risk management policies.

Interest rate swap agreements are used to manage interest rate exposures. Amounts payable or receivable in respect of these derivatives are recognised over the period of the contracts as adjustments to net interest payable in the profit and loss account.

When interest rate swaps and underlying debt are terminated together, the net gain or loss is taken to the profit and loss account as interest payable. When interest rate swaps are terminated but the underlying debt is retained then the gain/loss is deferred and is amortised to interest payable over the remaining life of the underlying debt.

Forward exchange contracts are used to hedge committed future transactions. Resultant gains and losses are deferred until the transaction occurs.

1. STATEMENT OF ACCOUNTING POLICIES (continued)

(n) Liquid resources

Liquid resources comprise cash and short term deposits with a maturity on acquisition of three months or less, which are held for the purpose of meeting short term cash commitments rather than for investment or other purposes.

(o) Bad debts

(i) Bad debt write offs

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

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

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

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

(ii) Bad debt provisioning

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

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

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

The provision has increased from £64.3m at 31 December 2013 to £77.3m at 31 March 2015. This reflects the additional provision made in the year as outstanding debt has aged. This has added to the existing provision for older debt which remains fully provided for as the debt is only written off in the specific circumstance outlined above.

2. SEGMENTAL INFORMATION

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

3. OPERATING COSTS, CAPITAL MAINTENANCE COSTS AND PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION

(a) Operating costs comprise:

	15 months ended 31 March 2015	12 months ended 31 December 2013
	£'m	£'m
Materials and consumables	24.9	19.9
Other external charges	95.1	79.9
Net manpower costs (note 7)	150.4	114.1
Other operating charges	164.7	127.7
Own work capitalised	(43.0)	(33.6)
	392.1	308.0

(b) Capital maintenance costs comprise:

	15 months ended 31 March 2015	12 months ended 31 December 2013
	£'m	£'m
Depreciation:		
Non-infrastructure assets	115.1	86.2
Infrastructure assets	62.0	50.2
Assets held under finance leases	5.5	4.9
Impairment of tangible fixed assets	32.6	-
Amortisation of capital grants and contributions	(5.7)	(4.3)
Profit on disposal of fixed assets	(1.0)	(1.6)
	208.5	135.4

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

(c) Profit on ordinary activities before taxation:

	15 months ended 31 March 2015	12 months ended 31 December 2013
	£'m	£'m
Profit on ordinary activities before taxation is stated after charging:		
Operating leases:		
Plant and machinery	0.1	0.1
Other assets	1.6	0.8
Costs of research and development	1.0	1.1
Directors' emoluments (note 5)	2.2	1.7

3. OPERATING COSTS, CAPITAL MAINTENANCE COSTS AND PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION (continued)

(c) Profit on ordinary activities before taxation (continued):

Auditor's remuneration in respect of the statutory audit amounted to £131k (year ended 31 December 2013: £126k), including fees for a subsidiary, Northumbrian Water Finance plc (NWF), of £6k (year ended 31 December 2013: £6k). Fees of £104k (year ended 31 December 2013: £53k) were incurred in respect of regulatory reporting for the years ended 31 March 2014 and 31 March 2015, including the audit of the regulatory accounts, agreed upon procedures required by Ofwat and the statement of sufficiency of financial resources and facilities. Fees of £60k (year ended 31 December 2013: £811k) were incurred for non-audit services comprising consultancy work in relation to workforce operations, advice on transition to new accounting standards and tax compliance advice.

4. NET INTEREST PAYABLE

	15 months ended 31 March 2015	12 months ended 31 December 2013
	£'m	£'m
Net interest payable comprises:		
Interest payable:		
Bank loans and overdrafts	23.6	19.6
Group loans	130.2	106.0
Financing charges payable under finance leases	6.6	5.7
Total interest payable	160.4	131.3
Interest receivable:		
Group interest	(12.2)	(9.8)
External interest	(4.7)	(0.4)
Total interest receivable	(16.9)	(10.2)
Other finance income relating to pension scheme (note 25)	(5.0)	(2.0)
Net interest payable	138.5	119.1

5. DIRECTORS' EMOLUMENTS

(a) Directors' remuneration

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

	15 months ended 31 March 2015	12 months ended 31 December 2013
	£'000	£'000
Emoluments (including benefits in kind)	2,218	1,665

For those Directors holding office with both NWL and NWGL, or contributing significantly to the day to day operations of NWGL, costs are apportioned between the companies to reflect the level of activity carried out for each company. This note reflects only the proportion of costs charged to NWL.

The costs for the period to 31 March 2015 include the first payment under a long term incentive plan (LTIP), which was introduced in 2012. The Directors' remuneration policy and a detailed report showing total remuneration for each Director, for the 12 months to 31 March 2015 only, are provided in note 10 of Section B to the accounts.

One of the Directors at 31 March 2015 was a member of a defined benefit pension scheme where the Company makes contributions towards the cost (31 December 2013: 1).

Two of the Directors at 31 March 2015 were members of a defined contribution scheme where the Company makes contributions towards the cost (31 December 2013: 2).

(b) Highest paid Director

The amounts for remuneration shown in note 5(a) include the following in respect of the highest paid Director:

	15 months ended 31 March 2015	12 months ended 31 December 2013
	£'000	£'000
Emoluments (including benefits in kind)	836	572

In the fifteen months ended 31 March 2015, the highest paid Director was a member of the defined contribution scheme and the payments made to that scheme of £35k (year ended 31 December 2013: £35k) are included within the emoluments figure above.

6. TRANSACTIONS WITH DIRECTORS AND OFFICERS

No transactions or arrangements with Directors and officers which are disclosable under the provisions of the Companies Act 2006 have occurred during the period.

7. EMPLOYEE INFORMATION

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

	15 months ended 31March 2015	12 months ended 31 December 2013
	£'m	£'m
Gross costs charged to the profit and loss account:		
Wages and salaries	90.8	67.7
Social security costs	8.3	6.3
Other pensions costs	15.4	12.4
	114.5	86.4
Costs recharged to other Group companies:		
Wages and salaries	3.0	1.9
Social security costs	-	0.2
Other pensions costs	-	0.3
	3.0	2.4
Net costs charged to the profit and loss account:		
Wages and salaries	87.8	65.8
Social security costs	8.3	6.1
Other pensions costs	15.4	12.1
	111.5	84.0
Costs charged to capital schemes and infrastructure renewals:		
Wages and salaries	30.9	23.9
Social security costs	2.8	2.2
Other pensions costs	5.2	4.0
	38.9	30.1
Total net employee costs	150.4	114.1

The average monthly number of employees on the payroll during the financial period was 3,053 (year ended 31 December 2013: 2,983) and the total at the period end was 3,109 (31 December 2013: 2,996).

8. TAXATION

(a) Analysis of tax charge for the financial period:

	15 months ended 31 March 2015	12 months ended 31 December 2013
	£'m	£'m
Current tax:		
UK corporation tax on profits for the 15 months ended 31 March 2015 at 21.39% (year ended 31 December 2013: 23.25%)	7.6	7.3
Adjustments in respect of prior periods	(68.3)	(1.5)
Payable in respect of group relief for the current period	45.0	37.2
Adjustments in respect of prior periods	(1.4)	0.1
Total current tax (credit)/charge (note 8b)	(17.1)	43.1
Deferred tax:		
Reduction due to opening tax rate change	-	(51.7)
Decrease in discount arising from above rate change	-	17.2
Net reduction in opening deferred tax	-	(34.5)
Adjustments in respect of prior periods	46.2	0.7
Increase in discount arising from prior period adjustments	(28.5)	-
	17.7	0.7
Movement in the 15 months ended 31 March 2015 at 20% (year ended 31 December 2013: 20%)		
Origination and reversal of timing differences in the period	0.1	1.6
Decrease/(increase) in discount arising from current period movements	49.9	(21.5)
Movement in the period	50.0	(19.9)
Total deferred tax charge/(credit) (note 20)	67.7	(53.7)
Total tax charge/(credit)	50.6	(10.6)

The rate of UK corporation tax was reduced from 23% to 21% with effect from 1 April 2014. A further reduction to 20% takes effect from 1 April 2015. The effective rate for the fifteen months to 31 March 2015 on a pro rata basis is therefore 21.39% (year to 31 December 2013: 23.25%). Deferred tax is provided at 20%, being the rate at which timing differences are expected to reverse.

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

Adjustments made in respect of current tax for prior periods include exceptional amounts relating to the implementation of a methodology agreed between the water industry and HMRC in relation to capital allowances available for certain treatment works assets following the abolition of industrial buildings allowances in 2008 (£22.3m), and reaching agreement with HMRC on several years' capital allowances claims (£42.2m).

8. TAXATION (continued)

(a) Analysis of tax charge for the financial period (continued)

The rate at which deferred tax is provided has not changed since the previous period. Accordingly, no opening adjustment is required. Adjustments made in respect of deferred tax for prior periods reflect the exceptional capital allowances items referred to above (£46.2m). The impact of the adjustments in prior periods on brought forward deferred tax discount is £28.5m.

Discount has decreased in the period due to falling gilt rates.

(b) Reconciliation of the current tax charge:

	15 months ended 31 March 2015	12 months ended 31 December 2013
	£'m	£'m
Profit on ordinary activities before tax	245.8	212.1
Profit on ordinary activities multiplied by standard rate of corporation tax of 22.811% (year ended 31 December 2013: 23.828%)	52.6	49.3
Effects of:		
Expenses not deductible for tax purposes	0.2	0.1
Non-taxable income and other tax reliefs	(1.9)	(2.0)
Depreciation in respect of non-qualifying items	3.1	4.7
Capital allowances in excess of depreciation	(5.3)	(3.8)
Pension scheme deficit	1.6	2.3
Other timing differences	3.6	(0.4)
Adjustments in respect of prior periods	(69.7)	(1.3)
Consortium relief paid for at less than the standard rate	(1.3)	(5.8)
Transfer pricing adjustments	(0.8)	(0.8)
Balancing payment payable	0.8	0.8
Total current tax (credit) / charge (note 8a)	(17.1)	43.1

(c) Factors that may affect future tax charges:

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

Deferred tax is provided on a discounted basis using post-tax yields on UK government gilts. In future deferred tax will be provided on an undiscounted basis as discounting is not permitted under FRS101 which the Company will adopt with effect from 1 April 2015.

9. DIVIDENDS

	15 months ended 31 March 2015	12 months ended 31 December 2013
	£'m	£'m
Equity:		
Dividends paid:		
Interim paid for the period ended 31 March 2015 of 84.18p (year ended 31 December 2013: 74.28p) per share on an aggregated basis	103.2	91.1
Interim paid for the period ended 31 March 2015 of 84.18p (year ended 31 December 2013: 80.80p) per share on an aggregated basis	103.3	99.1
Interim paid for the period ended 31 March 2015 of 85.61p (year ended 31 March 2015: nil) per share on an aggregated basis	105.0	-
Total dividends paid in the period	311.5	190.2

No final dividend was proposed for the period ended 31 March 2015 (year ended 31 December 2013: nil), the Company's statutory accounting reference date.

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

Accordingly, the level of dividend has been declared by reference to:

- the Company's ability to finance its functions;
- the Company's cumulative financial performance and past outperformance; and
- maintaining the Company's stable strong investment grade credit ratings.

10. TANGIBLE FIXED ASSETS

	Freehold land and buildings	Infrastructure assets	Operational structures, plant and machinery	Fixtures, fittings, tools and equipment	Assets in the course of construction	Total
	£'m	£'m	£'m	£'m	£'m	£'m
Cost:						
At 1 January 2014	128.0	2,349.9	2,514.0	209.7	224.8	5,426.4
Additions	-	-	-	-	311.9	311.9
Schemes commissioned	17.8	227.1	181.5	30.7	(457.1)	-
Disposals	-	(5.1)	(2.0)	-	-	(7.1)
At 31 March 2015	145.8	2,571.9	2,693.5	240.4	79.6	5,731.2
Depreciation:						
At 1 January 2014	47.0	482.1	952.6	160.8	-	1,642.5
Charge for the year	3.8	62.6	101.1	15.1	-	182.6
Impairment losses	0.7	-	31.9	-	-	32.6
Disposals	-	(5.1)	(2.0)	-	-	(7.1)
At 31 March 2015	51.5	539.6	1,083.6	175.9	-	1,850.6
At 31 March 2015	94.3	2,032.3	1,609.9	64.5	79.6	3,880.6
At 31 December 2013	81.0	1,867.8	1,561.4	48.9	224.8	3,783.9
Leased assets included above:						
At 31 March 2015	-	45.3	18.6	-	-	63.9
At 31 December 2013	-	45.9	20.6	-	-	66.5

The impairment of tangible fixed assets includes an exceptional charge of £30.7 million in relation to sludge drying plant at Bran Sands, which is explained in more detail in note 3(b).

11. FIXED ASSET INVESTMENTS

	Loans to Group companies
	£'m
At 1 January 2014 and 31 March 2015	160.9

The Company holds 100% of the nominal value of issued ordinary £1 shares of NWF, whose principal activity is to hold certain finance instruments on behalf of the Company.

The Company holds 100% of the nominal value of issued ordinary £1 shares of Reiver Holdings Limited, which in turn has a wholly owned subsidiary, Reiver Finance Limited, whose principal activity is as a special purpose financing vehicle.

The Company also has two quasi-subsidiary special purpose entities, Bakethin Holdings Limited, which is wholly owned by Bakethin Charitable Trust, and Bakethin Finance plc, which is a wholly owned subsidiary of Bakethin Holdings Limited. The principal activity of Bakethin Finance plc is as a special purpose financing vehicle.

In May 2004, the Company made a loan of £159.0m to Northumbrian Services Limited (NSL), maturing in January 2034.

In May 2004, the Company made a loan of £1.5m to Bakethin Holdings Limited, maturing in January 2034**.** The interest on the loan is capitalised and at 31 March 2015 the balance was £1.9m (31 December 2013: £1.9m).

12. STOCKS

	31 March 2015	31 December 2013
	£'m	£'m
Raw materials and consumables	2.3	2.8

There is no material difference between the balance sheet value of stocks and their replacement cost.

13. DEBTORS DUE IN LESS THAN ONE YEAR

	31 March 2015	31 December 2013
	£'m	£'m
Trade debtors	93.2	77.0
Corporation tax repayable	73.3	8.4
Amounts owed by other group companies	6.1	12.0
Other debtors	7.0	5.3
Prepayments and accrued income	71.9	73.7
	251.5	176.4

Trade debtors are shown net of bills raised in advance and provision for doubtful debts.

Corporation tax repayable reflects the adjustments arising from changes to capital allowances referred to in note 8 (b).

14. DEBTORS DUE IN MORE THAN ONE YEAR

	31 March 2015	31 December 2013
	£'m	£'m
Loan facility prepayments	1.0	1.0

15. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

	31 March 2015	31 December 2013
	£'m	£'m
Bank overdraft	0.7	-
Obligations under finance leases (note 18)	5.1	7.4
Loans (note 17)	124.6	60.6
Trade creditors	8.5	2.9
Amounts owed to other Group companies	106.6	28.0
Amounts owed to related parties	9.5	7.1
Taxation and social security	2.5	2.4
Other creditors	11.3	14.0
Receipts in advance	17.9	47.3
Accruals and deferred income	100.3	116.9
	387.0	286.6

Accruals and deferred income includes accruals related to capital projects of £34.0m (31 December 2013: £29.4m).

Included in amounts owed to other Group companies is £21.5m (31 December 2013: £22.7m) payable in respect of tax losses surrendered from fellow Group companies and £82.5m (31 December 2013: £nil) for short term working capital requirements. Amounts owed to related parties of £9.5m (31 December 2013: £7.1m) are payable in respect of tax losses surrendered as consortium relief from associated companies outside of the Group.

16. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR

	31 March 2015	31 December 2013
	£'m	£'m
Obligations under finance leases (note 18)	101.2	101.6
Loans (note 17)	407.8	347.6
Amounts owed to other Group companies (note 19)	1,882.5	1,867.5
	2,391.5	2,316.7

Amounts owed to other group companies is net of £17.2m (31 December 2013: £17.9m) of related gilt locks being amortised over the term of the loans.

17. LOANS

	31 March 2015	31 December 2013
	£'m	£'m
Loans are repayable as follows:		
Within one year (note 15)	124.6	60.6
Between one and two years	38.2	32.6
Between two and five years	117.6	107.3
After five years	252.0	207.7
	532.4	408.2

Loans wholly repayable within five years amount to £125.3m (31 December 2013: £79.3m).

Loans not wholly repayable within five years amount to £407.1m (31 December 2013: £334.3m) and bear interest rates in the range 0.94% to 5.186%.

The fair value loss on the Company's outstanding interest rate swaps in the period to 31 March 2015 was £9.3m (31 December 2013: £9.4m) in relation to an interest rate swap with a notional principal of £70.0m (31 December 2013: £85.0m).

18. OBLIGATIONS UNDER FINANCE LEASES

Obligations under hire purchase contracts and finance leases are as follows:

	31 March 2015	31 December 2013
	£'m	£'m
Amounts due:		
Within one year	5.1	7.4
Between one and two years	7.1	7.0
Between two and five years	61.0	64.2
After five years	82.6	75.7
	155.8	154.3
Less:		
Finance charge allocated to future periods	(49.5)	(45.3)
	106.3	109.0
Disclosed as due:		
Within one year (note 15)	5.1	7.4
After more than one year (note 16)	101.2	101.6
	106.3	109.0

The aggregate gross amount of obligations under hire purchase contracts and finance leases, any part of which falls due for repayment in five years or more, is £102.6m (31 December 2013: £96.3m).

19. AMOUNTS DUE TO OTHER GROUP COMPANIES

Amounts due to other Group companies include loans repayable as follows:

	31 March 2015	31 December 2013
	£'m	£'m
Within one year	82.5	-
Between two and five years	300.1	300.2
After five years	1,582.4	1,567.3
	1,965.0	1,867.5

NWF issued £200m and £150m Guaranteed Eurobonds in February 1998 and September 2001 respectively, maturing February 2023, with an annual coupon of 6.875%. The issues were guaranteed by the Company who received the issue proceeds by way of inter-company loans of £194.2m and £163.2m respectively. Finance costs allocated during the period amounted to £0.3m (year ended 31 December 2013: £0.2m). Amortisation of loan issue receipts during the period amounted to £0.4m (year ended 31 December 2013: £0.3m).

NWF issued £300m Guaranteed Eurobonds in December 2001, maturing October 2017, with an annual coupon of 6.0%. The issue was guaranteed by the Company who received the issue proceeds by way of an inter-company loan of £301.0m. Amortisation of loan receipts during the period amounted to £0.1m (year ended 31 December 2013: £0.1m).

NWF issued £250m and £100m Guaranteed Eurobonds in December 2002 and December 2004, maturing April 2033 with an annual coupon of 5.625%. Both issues were guaranteed by the Company who received the issue proceeds by way of inter-company loans of £246.6m and £100.8m respectively. Finance costs allocated during the period amounted to £0.3m (year ended 31 December 2013: £0.2m).

NWF issued £150m Guaranteed Index Linked Eurobonds in September 2005, maturing July 2036, with a real coupon of 2.033%. The issue was guaranteed by the Company who received the issue proceeds by way of an inter-company loan of £150.0m. Indexation accretion during the period amounted to £5.2m (year ended 31 December 2013: £5.6m).

NWF issued £60m Guaranteed Index Linked Eurobonds in January 2006, maturing January 2041, with a real coupon of 1.6274%. The issue was guaranteed by the Company who received the issue proceeds by way of an inter-company loan of £60.0m. Indexation accretion during the period amounted to £2.0m (year ended 31 December 2013: £2.2m).

NWF issued two £100m Guaranteed Index Linked Eurobonds in June 2006 with real coupons of 1.7118% and 1.7484% and with maturities of 2049 and 2053 respectively. Both issues were guaranteed by the Company who received the issue proceeds by way of two inter-company loans of £100.0m. Indexation accretion during the period amounted to £6.7m (year ended 31 December 2013: £3.6m).

NWF issued £360m Guaranteed Eurobonds in January 2012, maturing January 2042, with an annual coupon of 5.125%. The issue was guaranteed by the Company who received the issue proceeds by way of an inter-company loan of £338.8m. Finance costs allocated during the period amounted to £0.9m (year ended 31 December 2013: £0.7m).

20. PROVISIONS FOR LIABILITIES AND CHARGES

	£'m
Pension provision for former employees:	
At 1 January 2014	2.0
Utilised during the period	(0.2)
At 31 March 2015	1.8
Deferred tax:	
At 1 January 2014	177.7
Total movement in the period (note 8a)	67.7
Included above relating to pensions (note 25)	1.5
At 31 March 2015	246.9
Total provisions for liabilities and charges	248.7

The pension provision for former employees relates to pensions payable mainly to former employees of water-only companies which have since merged with the Company. The provision of £1.8m represents the full future amounts payable, based on an actuarial assessment, for which the Company is directly liable.

The provision for deferred tax comprises:

	31 March 2015	31 December 2013
	£'m	£'m
Accelerated tax depreciation	428.3	377.1
Other timing differences	(41.3)	(37.9)
Held-over gains	1.0	1.0
Undiscounted provision for deferred tax	388.0	340.2
Discount	(141.1)	(162.5)
Discounted provision for deferred tax	246.9	177.7

21. ACCRUALS AND DEFERRED INCOME

	Capital grants and contributions	Proceeds from Kielder securitisation	Total
	£'m	£'m	£'m
At 1 January 2014	240.0	143.7	383.7
Additions	29.0	-	29.0
Amortised during the period	(5.7)	(8.8)	(14.5)
At 31 March 2015	263.3	134.9	398.2

The Kielder securitisation involved the assignment of the right to the future income stream associated with the Kielder operating contract to Reiver Finance Limited, a subsidiary company, up to 2034 in return for consideration of £212.1m. This income is amortised to the profit and loss account of the Company over the life of the assignment.

22. CALLED UP SHARE CAPITAL

	31 March 2015	31 December 2013
	£'m	£'m
Authorised:		
122,650,000 Ordinary Shares of £1 each (31 December 2013: 122,650,000)	122.7	122.7

	31 March 2015	31 December 2013
	£'m	£'m
Allotted, called-up and fully paid:		
122,650,000 Ordinary Shares of £1 each (31 December 2013: 122,650,000)	122.7	122.7

NWL is a company limited by shares.

23. RECONCILIATION OF MOVEMENTS IN EQUITY SHAREHOLDERS' FUNDS AND MOVEMENT ON RESERVES

	Profit and loss account	Total shareholders' funds	
	31 March 2015	31 March 2015	31 December 2013
	£'m	£'m	£'m
At beginning of period	789.0	911.7	863.6
Profit for the period	195.2	195.2	222.7
Actuarial gain on pension liability in the period (note 25)	7.6	7.6	25.2
Deferred tax related to actuarial gain on pension liability in the period (note 25)	(1.5)	(1.5)	(9.6)
Dividends paid (note 9)	(311.5)	(311.5)	(190.2)
At end of period	678.8	801.5	911.7

24. COMMITMENTS

(a) Capital expenditure:

	31 March 2015	31 December 2013
	£'m	£'m
Expenditure contracted but not provided for	89.5	105.0

24. COMMITMENTS (continued)

(b) Lease commitments:
The Company has entered into non-cancellable operating leases in respect of land and buildings, plant, machinery and motor vehicles. The total amount payable under these leases in the next year is as follows:

	31 March 2015	31 December 2013
	£'m	£'m
Land and buildings:		
Leases which expire:		
In less than one year	0.1	0.1
In five years or more	0.6	0.6
	0.7	0.7

	31 March 2015	31 December 2013
	£'m	£'m
Other:		
Leases which expire:		
In less than one year	-	0.1
Between two and five years	0.1	-
	0.1	0.1

(c) Foreign exchange contracts:
At 31 March 2015 the Company held forward foreign exchange contracts of £2.7m (31 December 2013: £2.1m) for the purpose of hedging the foreign currency risk of committed future purchases.

25. PENSIONS

NWL participates in the Group defined benefit pension scheme, NWPS, providing benefits based on final pensionable remuneration to 1,604 active members at 31 March 2015 (31 December 2013: 1,705). The assets of the NWPS are held separately from those of the Group in independently administered funds.

The most recent actuarial valuation of the NWPS was at 31 December 2010. At that date the value of assets amounted to £680.1m and the funding level was 84.7%. The future service contribution rate jointly payable by members and the employers from 31 December 2010 was 24.2% of pensionable salaries. Members’ contributions are 7.3% on average with the employers paying 16.9%.

The employer contribution rate was assessed using the projected unit method and the following actuarial assumptions:

Pre-retirement discount rate	5.8%
Post-retirement discount rate	4.9%
Pay increases	3.85%
Price inflation (RPI)	3.6%
Price inflation (CPI)	2.9%
Pension increases linked to RPI	3.6%
Pension increases linked to CPI	2.9%

With the agreement of the NWPS Trustee, the employers made capital contributions of £70m to cover the period 1 January 2011 to 31 March 2015. These payments comprised employers’ contributions, the deficit recovery funding assumed in the final determination and employees contributions under a salary sacrifice arrangement. Contributions for the current period amounted to £3.7m, including a one off lump sum contribution of £3.1m due in April 2015 but paid in March 2015.

25. PENSIONS (continued)

With effect from 1 April 2015, the Company will recommence payment of monthly employer contributions at 16.9% of pensionable salaries, plus a further 1.5% for scheme expenses, and will also pay an average of 7.3% contributions for employees participating in a salary sacrifice arrangement. In addition, under the schedule of contributions agreed for the 31 December 2010 actuarial valuation, the Company will pay deficit contributions of £12.4m per annum, increasing annually with RPI. The schedule of contributions also required the Company to pay an additional £3.1m one off lump sum contribution, to reflect the increased cost for accruing benefits indicated in the 31 December 2010 actuarial valuation and not factored into the £70m capital contributions. This amount was paid in March 2015.

An actuarial valuation as at 31 December 2013 has been carried out and the outcome is close to being finalised. In January 2015, the Company commenced a consultation with members on proposed changes to the Scheme, which is ongoing. Contributions for the year to 31 March 2016 will be determined by the outcome of the consultation process, the finalisation of the December 2013 actuarial valuation and agreement of a new schedule of contributions.

The Scheme also has a defined contribution section which had 1,356 active members at 31 March 2015 (31 December 2013: 1,180). Members can choose to contribute either 3%, 4% or 5% of salary, with employers contributing at either 6%, 7% or 8% depending on the member contribution rate. The contributions paid to the defined contribution section by the Company in the period totalled £4.5m (year ended 31 December 2013: £1.8m).

The additional disclosures regarding the defined benefit scheme as required under FRS 17 Retirement benefits and the relevant impact on the financial statements are set out below. A qualified actuary, using revised assumptions that are consistent with the requirements of FRS 17, has updated the actuarial valuation described above as at 31 March 2015. Investments have been valued, for this purpose, at fair value.

FRS 17 actuarial assumptions:	31 March 2015	31 December 2013
Discount rate	3.3%	4.6%
Pay increases[1]	3.00%	3.95%
Price inflation (RPI)	2.9%	3.3%
Price inflation (CPI)	1.9%	2.3%
Pension increases linked to RPI	2.9%	3.3%
Pension increases linked to CPI	1.9%	2.3%
Mortality assumptions[2]	PCMA00/PCFA00	PCMA00/PCFA00
- Life expectancy for a member aged 65 - female (years)	24.7	24.5
- Life expectancy for a member aged 65 - male (years)	22.4	22.2

1. including promotional salary scale

2. 115% of PCMA00/PCFA00 (year of birth with medium cohort improvements).

25. PENSIONS (continued)

The fair value of the assets in the NWPS, the present value of the liabilities in the Scheme and the long term expected rate of return at 31 March 2015 are shown below. The long term expected rate of return for each class of assets reflects market rates for equivalent investments, with an appropriate risk premium added for higher risk asset types such as equities and property.

	Long term expected rate of return 31 March 2015	31 March 2015	Long term expected rate of return 31 December 2013	31 December 2013
	%	£'m	%	£'m
Equities	5.8	372.8	7.1	359.1
Corporate bonds	3.3	183.0	4.6	153.1
Government bonds	2.3	98.7	3.6	80.1
Property	5.8	96.0	6.1	80.4
Cash	2.0	39.0	3.0	36.0
Other	5.2	94.7	6.1	76.8
Total fair value of assets		884.2		785.5
Present value of liabilities		(970.9)		(872.2)
Deficit under FRS17		(86.7)		(86.7)
Related deferred tax[1]		17.3		17.3
Net pension liability		(69.4)		(69.4)

1. The movement in the related deferred tax of £nil (2013: £6.1m) comprises a increase of £1.5m relating to the actuarial gain in the period (which is recognised in the statement of total recognised gains and losses) and a decrease of £1.5m relating to other items which are recognised in the profit and loss account.

Analysis of the amount that has been charged to the profit and loss account under FRS 17:

	31 March 2015	31 December 2013
	£'m	£'m
Current service cost	16.1	12.9
Past service cost	0.2	0.8
Recognised in operating costs in arriving at operating profit	16.3	13.7

	31 March 2015	31 December 2013
	£'m	£'m
Interest cost on plan obligations	49.4	36.0
Expected return on plan assets	(54.4)	(38.0)
Recognised in net interest payable (note 4)	(5.0)	(2.0)

Analysis of the actuarial (loss) / gain that has been recognised in the statement of total recognised gains and losses:

	31 March 2015	31 December 2013
	£'m	£'m
Net actuarial gain by NWL	7.6	25.2
Cumulative amounts recognised since adopting the standard	(64.2)	(71.8)

25. PENSIONS (continued)

History of experience gains and losses:

	31 March 2015	31 December 2013	31 December 2012	31 March 2012	31 March 2011
Fair value of assets	884.2	785.5	745.4	738.3	713.3
Present value of defined benefit obligation	(970.9)	(872.2)	(847.2)	(822.4)	(759.3)
Deficit	(86.7)	(86.7)	(101.8)	(84.1)	(46.0)
Experience adjustments arising on plan assets	82.5	32.4	2.3	(42.2)	10.7
Experience adjustments arising on plan liabilities	0.6	-	-	31.0	-

Changes in the present value of the defined pension obligations are analysed as follows:

	31 March 2015	31 December 2013
	£'m	£'m
At start of period	872.2	847.2
Current service cost	16.1	12.9
Past service cost	0.2	0.8
Interest cost	49.4	36.0
Contributions by plan participants	0.2	0.2
Actuarial losses on obligations	74.9	7.2
Benefits paid	(42.1)	(32.1)
At end of period	970.9	872.2

Changes in the fair value of plan assets are analysed as follows:

	31 March 2015	31 December 2013
	£'m	£'m
At start of period	785.5	745.4
Expected return on plan assets	54.4	38.0
Actuarial gains on plan assets	82.5	32.4
Contributions by employer	3.7	1.6
Contributions by plan participants	0.2	0.2
Benefits paid	(42.1)	(32.1)
At end of period	884.2	785.5

Nature of benefits, regulatory framework and other entity's responsibilities for governance of the scheme

The Scheme is a registered defined benefit final salary scheme subject to the UK regulatory framework for pensions, including the scheme specific funding requirements. The Scheme is operated under trust and as such, the Trustee of the Scheme is responsible for operating the Scheme and they have a statutory responsibility to act in accordance with the Scheme's Trust Deed and Rules, in the best interest of the beneficiaries of the Scheme, and UK legislation (including Trust law). The Trustee has the power to set the contributions that are paid to the Scheme.

25. PENSIONS (continued)

Risks to which the scheme exposes the Company
The nature of the Scheme exposes the Company to the risk of paying unanticipated additional contributions to the Scheme in times of adverse experience. The most financially significant risks are likely to be:

- members living for longer than expected;
- higher than expected actual inflation and salary increase experience,
- lower than expected investment returns, and
- the risk that movements in the value of the scheme's liabilities are not met by corresponding movements in the value of the Scheme's assets.

Asset-liability matching strategies used by the scheme or the Company
The Scheme does not currently use any asset-liability matching strategies. The Trustee's current investment strategy, having consulted with the Company, is to invest the majority of the Scheme's assets in a mix of equities and corporate bonds, in order to strike a balance between:

- maximising the returns on the scheme's assets, and
- minimising the risks associated with the lower than expected returns on the Scheme's assets.

The Trustee is required to regularly review their investment strategy in light of the revised term and nature of the Scheme's liabilities.

Sensitivity to key assumptions
FRS 17 encourages disclosure of the sensitivity of the results to the methods and assumptions used.

The costs of a pension arrangement require estimates regarding future experience. The financial assumptions used for FRS 17 reporting are the responsibility of the Directors of the Company. These assumptions reflect market conditions at the balance sheet date. Changes in market conditions which result in changes in the net discount rate (essentially the difference between the discount rate and the assumed rates of increases of salaries, deferred pension revaluation or pensions in payment), can have a significant effect on the value of the liabilities reported.

A reduction in the net discount rate will increase the assessed value of liabilities, as a higher value is placed on benefits paid in the future. A rise in the net discount rate will have an opposite effect of similar magnitude. The overall effect of a change in the net discount rate of 0.1% would change the liabilities by around £18m.

There is also uncertainty around life expectancy for the UK population. The value of current and future pension benefits will depend on how long they are assumed to be in payment. The disclosures have been prepared using the mortality assumptions basis used in the 2010 formal valuation. Specifically, the post-retirement mortality assumptions use a base table of 115% of PCMA00/PCFA00 with an allowance for future improvements in line with the medium cohort projections, lagged to apply ten years later, based on each individual's year of birth. This is subject to a minimum improvement of 1.0% per annum.

These assumptions imply an assumed life expectancy for a member aged 65 at 31 March 2015 of 22.4 years (31 December 2013: 22.2 years) for males and 24.7 years (31 December 2013: 24.5 years) for females. The effect of increasing the assumed life expectancies by one year would be to increase the value of liabilities by around £29.1m (3.0%).

26. RELATED PARTY DISCLOSURES

The Company is a wholly owned subsidiary of NWGL, whose publicly available consolidated financial statements include the Company. Accordingly, the Company is exempt under the terms of FRS 8 'Related Party Disclosures' from disclosing transactions with other members of the Group headed by NWGL.

Transactions with related parties outside of the NWGL group comprised purchases of £2.4m (year ended 31 December 2013: £1.9m), sales of £0.1m (year ended 31 December 2013: £0.1m) and consortium tax relief of £10.6m (year ended 31 December 2013: £7.1m). There were no amounts due from or to these companies at 31 March 2015 (year ended 31 December 2013: £nil) in respect of sales or purchases. £9.5m (year ended 31 December 2013: £7.1m) is owed in respect of tax losses surrendered to Hutchison 3G UK Limited (note 15).

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

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

27. ULTIMATE PARENT UNDERTAKING AND CONTROLLING PARTY

At the balance sheet date, the Company's immediate parent undertaking was NWGL, which is incorporated in England and Wales. In the Directors' opinion, the Company's ultimate parent undertaking and controlling party, at the balance sheet date, was NWGL. NWGL is indirectly wholly owned by CKI, CKH and Li Ka Shing Foundation Limited.

After the balance sheet date, CKHH became the ultimate parent undertaking and controlling party, as described in note 28.

Copies of NWGL's Group financial statements, which include the Company, are available from Northumbria House, Abbey Road, Pity Me, Durham, DH1 5FJ.

28. POST BALANCE SHEET EVENT

On 3 June 2015, CKHH, a company listed on the Hong Kong Stock Exchange, acquired CKH and (indirectly) HWL. As a consequence, CKHH gained control of both CKH and HWL's controlling interests in CKI, meaning that, in the Directors' opinion, CKHH became the ultimate parent undertaking and controlling party of NWGL and, therefore, NWL.

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

We have audited the group financial statements of Northumbrian Water Limited for the period ended 31 March 2015 which comprise the Profit and Loss Account, the Statement of Total Recognised Gains and Losses, the Balance Sheet and the related notes 1 to 28. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditor

As explained more fully in the Directors' Responsibilities Statement, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

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

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the group and Company's affairs as at 31 March 2015 and of its profit for the period then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Directors' Report for the financial period for which the financial statements are prepared is consistent with the financial statements.

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

Matters on which we are required to report by exception

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

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

Paul Feechan (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Newcastle Upon Tyne, United Kingdom,
13 July 2015

HISTORICAL COST PROFIT AND LOSS ACCOUNT
for the year ended 31 March 2015

Analysis of historical cost financial information between appointed and non appointed business.

		2015			2014		
		Appointed business	Non-appointed business	Aggregated basis	Appointed business	Non-appointed business	Aggregated basis
	Note	£'m	£'m	£'m	£'m	£'m	£'m
Turnover	A	761.5	26.2	787.7	750.3	26.1	776.4
Operating costs		(298.5)	(15.5)	(314.0)	(293.1)	(15.5)	(308.6)
Infrastructure renewals charge		(49.8)	(0.1)	(49.9)	(50.8)	(0.1)	(50.9)
Historical cost depreciation		(126.2)	(0.7)	(126.9)	(87.8)	(0.8)	(88.6)
Operating income		0.9	-	0.9	1.6	-	1.6
OPERATING PROFIT	A	287.9	9.9	297.8	320.2	9.7	329.9
Other income		0.1	2.9	3.0	0.2	2.5	2.7
Net interest (payable) / receivable		(123.3)	9.7	(113.6)	(130.0)	9.7	(120.3)
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION		164.7	22.5	187.2	190.4	21.9	212.3
Taxation - current		31.5	(3.4)	28.1	(39.4)	(3.5)	(42.9)
- deferred	A	(65.2)	(0.3)	(65.5)	(1.6)	0.1	(1.5)
PROFIT FOR THE FINANCIAL YEAR		131.0	18.8	149.8	149.4	18.5	167.9
Dividends		(297.2)	(14.3)	(311.5)	(144.0)	(46.2)	(190.2)
RETAINED (LOSS) / PROFIT FOR THE YEAR		(166.2)	4.5	(161.7)	5.4	(27.7)	(22.3)

HISTORICAL COST STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES FOR THE APPOINTED BUSINESS

for the year ended 31 March 2015

	2015	2014
	£'m	£'m
Profit for the financial year	131.0	149.4
Pension liability actuarial gain in the period	31.1	(6.3)
Deferred tax related to pension adjustments	(6.2)	(3.0)
Total recognised gains and losses relating to the year	155.9	140.1

HISTORICAL COST BALANCE SHEET
at 31 March 2015
(Registered number 2366703)

Analysis of historical cost financial information between appointed and non appointed business

		2015			2014		
	Note	Appointed business	Non-appointed business	Aggregated basis	Appointed business	Non-appointed business	Aggregated basis
		£'m	£'m	£'m	£'m	£'m	£'m
FIXED ASSETS							
Tangible assets	A	3,494.5	101.1	3,595.6	3,434.7	100.6	3,535.3
Investments - loans to group companies		-	160.9	160.9	-	160.9	160.9
		3,494.5	262.0	3,756.5	3,434.7	261.5	3,696.2
Infrastructure renewals prepayment/ (accrual)		16.8	(2.0)	14.8	21.2	(1.9)	19.3
Other current assets		261.7	3.8	265.5	196.4	4.1	200.5
CREDITORS: Amounts falling due within one year							
Borrowings		(129.7)	-	(129.7)	(38.1)	-	(38.1)
Other creditors		(258.6)	(9.3)	(267.9)	(170.5)	(7.6)	(178.1)
Total creditors: amounts falling due within one year		(388.3)	(9.3)	(397.6)	(208.6)	(7.6)	(216.2)
NET CURRENT (LIABILITIES) / ASSETS		(109.8)	(7.5)	(117.3)	9.0	(5.4)	3.6
TOTAL ASSETS LESS CURRENT LIABILITIES		3,384.7	254.5	3,639.2	3,443.7	256.1	3,699.8
CREDITORS: Amounts falling due after more than one year							
Borrowings		(2,391.5)	-	(2,391.5)	(2,359.1)	-	(2,359.1)
Other creditors		-	-	-	(1.7)	-	(1.7)
TOTAL CREDITORS: amounts falling due after one year		(2,391.5)	-	(2,391.5)	(2,360.8)	-	(2,360.8)
PROVISIONS FOR LIABILITIES AND CHARGES	A	(332.4)	(139.5)	(471.9)	(280.7)	(146.0)	(426.7)
NET ASSETS EMPLOYED		660.8	115.0	775.8	802.2	110.1	912.3
CAPITAL AND RESERVES		660.8	115.0	775.8	802.2	110.1	912.3

Approved by the Board of Directors on 13 July 2015 and signed on their behalf by:

H Mottram

(A) RECONCILIATION BETWEEN STATUTORY ACCOUNTS AND HISTORICAL COST REGULATORY ACCOUNTS for the year ended 31 March 2015

The Company has prepared its statutory financial statements for the fifteen month period to 31 March 2015. These regulatory accounts are prepared for the year ended 31 March 2015. Where there is also a difference relating to accounting treatment, the table below shows the impact of these timing differences.

In preparing its statutory accounts, the Company has followed common industry practice and adopted the infrastructure renewals accounting basis as set out in FRS 15 ‘Tangible Fixed Assets’. However, for the purpose of the regulatory accounts, Ofwat’s Regulatory Accounting Guidelines require that FRS 15 is not applied for infrastructure renewals accounting. In addition, Ofwat has instructed that the provisions of FRS 5 ‘Reporting the Substance of Transactions Application Note G – Revenue Recognition’, which states that turnover should not include amounts that the Company does not expect to collect, be disapplied. A reconciliation of accounting treatment differences between the statutory and historical cost regulatory accounts is set out below:

	Note	Statutory UK GAAP financial statements at 31 December 2013	Historical cost regulatory accounts at 31 March 2015	Analysis of difference		
				Total difference	Timing	Accounting
		£'m	£'m	£'m	£'m	£'m
PROFIT AND LOSS ACCOUNT						
Turnover	1	984.9	787.7	197.2	192.3	4.9
Operating Profit	2	384.3	297.8	86.5	80.9	5.6
Deferred tax credit	3	67.7	65.5	2.2	0.5	1.7
BALANCE SHEET						
Tangible fixed assets	4	3,880.6	3,595.6	285.0	n/a	285.0
Provisions for liabilities and charges:						
Deferred tax	5	246.9	204.7	42.2	n/a	42.2
Capital grants and contributions	6	263.3	61.7	201.6	n/a	201.6
Post employment liability	7	86.7	86.0	0.7	n/a	0.7

Note	Explanation of accounting differences
1	Statutory accounts include provision for revenue recognition of £1.9m in accordance with of FRS 5 Application Note G, which is disapplied for regulatory purposes. Rental income of £3.0m is disclosed within other income below operating profit in the regulatory accounts as required by RAG 4.04.
2	Adjustments relating to amortisation of infrastructure income (£1.9m) in the statutory accounts, an additional charge in statutory accounts for VLS pension scheme (£0.7m) and disclosure of rental income (£3.0m) within other income below operating profit in the regulatory accounts.
3	Adjustment relating to amortisation of infrastructure income (£0.4m) and discount (£1.3m).
4	Adjustments relating to infrastructure grants and contributions netted off (£229.8m), Section 19 ‘overlap’ (£40.4m) and infrastructure renewals prepayment (£14.8m).
5	Adjustments relating to amortisation of infrastructure income (£5.2m), Section 19 ‘overlap’ (£8.0m) and discount (£29.0m).
6	Adjustments relating to gross up (£229.8m) and amortisation ((£28.2m)) of infrastructure grants and contributions.
7	Adjustment relating to additional credit in statutory accounts for VLS pension arrangements in NWPS (£0.7m).

CURRENT COST PROFIT AND LOSS ACCOUNT
for the year ended 31 March 2015

	2015			2014		
	Water	Sewerage	Total	Water	Sewerage	Total
	£'m	£'m	£'m	£'m	£'m	£'m
Turnover						
Unmeasured - household	220.5	161.7	382.2	220.4	165.0	385.4
- non-household	2.6	4.1	6.7	2.9	4.6	7.5
Measured - household	126.0	59.7	185.7	112.1	53.9	166.0
- non-household	66.9	61.0	127.9	67.1	61.9	129.0
Trade effluent	-	3.0	3.0	-	2.6	2.6
Bulk supplies / inter company payments	0.8	-	0.8	0.6	-	0.6
Other third party services (inc potable water)	9.3	0.2	9.5	10.5	0.3	10.8
Other sources	28.4	17.3	45.7	28.8	19.6	48.4
Total turnover	454.5	307.0	761.5	442.4	307.9	750.3
Current cost operating costs - wholesale	(276.0)	(183.2)	(459.2)	(269.7)	(178.5)	(448.2)
Current cost operating costs - retail	(43.5)	(17.1)	(60.6)	(41.7)	(16.5)	(58.2)
Operating income	(0.2)	0.7	0.5	0.9	(0.7)	0.2
Working capital adjustment	(0.2)	(0.1)	(0.3)	(0.6)	(0.4)	(1.0)
CURRENT COST OPERATING PROFIT	134.6	107.3	241.9	131.3	111.8	243.1
Other income			0.1			0.2
Net interest			(123.3)			(130.0)
Financing adjustment			17.1			46.7
CURRENT COST PROFIT BEFORE TAXATION			135.8			160.0
Net revenue movement out of tariff basket	-	(0.2)	(0.2)	-	(0.2)	(0.2)

No back-billing amounts were identified. This information will be included in the Revenue Correction Mechanism for the PR14 Business Plan.

CURRENT COST CASH FLOW STATEMENT
for the year ended 31 March 2015

	2015	2014
	£'m	£'m
Current cost operating profit	241.9	243.1
Working capital adjustment	0.3	1.0
Movement in working capital	(19.7)	8.4
Receipts from other income	0.1	0.2
Current cost depreciation	171.5	162.5
Current cost profit on sale of fixed assets	(0.5)	(0.2)
Infrastructure renewals charge	49.8	50.8
Other non-cash movements	9.0	4.2
Contributions in respect of retirement benefits	(3.5)	(1.0)
Net cash flow from operating activities	448.9	469.0
Returns on investment and servicing of finance	(116.0)	(113.6)
Taxation paid	(35.7)	(34.2)
Capital expenditure and financial investment		
Gross cost of purchase of fixed assets	(202.1)	(158.4)
Receipt of grants and contributions	23.1	14.1
Infrastructure renewals expenditure	(45.4)	(61.2)
Disposal of fixed assets	1.0	2.2
Net cash flow from investing activities	(223.4)	(203.3)
Equity dividends paid	(297.2)	(144.0)
Net cash flow from management of liquid resources	15.0	(10.0)
NET CASH FLOW BEFORE FINANCING	(208.4)	(36.1)
Net cash inflow from financing	190.8	67.4
(DECREASE) / INCREASE IN CASH	(17.6)	31.3

NOTES TO THE REGULATORY ACCOUNTS
for the year ended 31 March 2015

1. STATEMENT OF REGULATORY ACCOUNTING POLICIES

(a) Historical cost information

(i) Basis of accounting and consolidation

These regulatory accounts have been accounts prepared in accordance with Regulatory Accounting Guidelines (RAGs) issued by Ofwat. They have been prepared in accordance with the accounting policies set out on pages 28 to 31 with the exception of:

- capital grants and contributions to infrastructure assets which is not in accordance with the Companies Act 2006 as described in note (iv) below.
- infrastructure renewals accounting which, in accordance with RAG 3.07 Guideline for the format and disclosure of the regulatory accounts has been accounted for in accordance with RAG 2.04 Guideline for classification of Capital Expenditure. RAG 2.04 is not in accordance with FRS 12 'Provisions, Contingent Liabilities and Contingent Assets' and FRS 15 'Tangible Fixed Assets' as described in note (iii) below.
- recognition of income relating to energy generation and rental income as described in note (ii) below.

The Appointed business consists of regulated activities, defined in Condition A of the Licence to be 'functions of' and the 'duties imposed on' a water and sewerage undertaker by the Water Industry Act 1991. Such duties are consequently those necessary for the Company to fulfil its duty as a water and sewerage undertaker.

Non-appointed activities are those for which the Company is not a monopoly supplier, such as the sale of laboratory services to external organisations or recreation and holiday letting facilities at Leaplish Waterside Park, Kielder.

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

(ii) Turnover and revenue recognition

The revenue recognition policy is the same in the regulatory and statutory accounts, except where Ofwat has decided to depart from UK GAAP and disapply the provisions of FRS 5 Application Note G, which states that turnover should not include amounts that the Company does not expect to collect. Income relating to energy generation is recorded as turnover in the statutory accounts but as negative operating expenditure in the regulatory accounts (Note A).

In addition, rental income is recognised within turnover in the statutory accounts but in the regulatory accounts is recognised within other income below operating profit, as required by RAG 4.04 Guideline for the definitions for the regulatory accounts tables (Note A).

An accrual is made for unmeasured consumption not yet billed at year end.

In respect of measured income, an accrual is also made for the amount of mains water and sewerage charges unbilled at the year end. This is estimated using a defined methodology based upon weighted average water consumption by tariff, calculated using historical information, and is recognised in turnover.

Invoices raised or payments received where the service has not been provided are not recognised in turnover in the year but are treated as payments in advance.

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

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

1. STATEMENT OF ACCOUNTING POLICIES (continued)

(a) Historical cost information (continued)

(ii) Turnover and revenue recognition (continued)

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

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

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

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

Appointed business turnover for the year ended 31 March 2015 of £761.5m was £21.6m lower than the 2009 price review final determination target of £783.1m. Of this variance, £12.5m related to the water service and £9.1m to the sewerage service. The lower income is largely due to lower tariff basket income as a result of fewer new properties being constructed and lower average consumption per measured property. In addition, non-household demand has declined over the five year period as a result of the difficult prevailing economic conditions.

A retrospective review has confirmed that there were no significant differences between the measured income accrual of £53.9m at 31 March 2014 and the amounts subsequently billed to customers of £54.4m.

(iii) Infrastructure assets

Infrastructure assets comprise a network of systems which include water mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls.

Expenditure on infrastructure assets relating to increases in capacity or enhancements of the network is treated as additions which are included at cost after deducting capital grants and contributions.

Expenditure on maintaining the operating capability of the network in accordance with defined standards of service is charged as an operating cost. No depreciation is charged on infrastructure assets because the network of systems is required to be maintained in perpetuity and, therefore, has no finite economic life.

In accordance with RAG 3.07 the Company has not applied FRS 12 and FRS 15, in respect of infrastructure renewals accounting and has continued to charge infrastructure renewal costs (calculated in accordance with our Asset Management Plan (AMP)) to the profit and loss account. Expenditure during the year is charged to the provision.

Under FRS 12 it is not permitted to recognise a provision for the costs of renewals expenditure. Adoption of FRS 12, taken together with FRS 15, would require:

- restatement of the cost and accumulated depreciation of infrastructure fixed assets to reflect infrastructure renewals expenditure, depreciation and retirement of assets since renewals accounting was first adopted. Accordingly, infrastructure renewals prepayments and provisions at years ended 31 March 2014 and 31 March 2015 would have been included within infrastructure fixed assets.
- the depreciation of infrastructure assets and the inclusion of the infrastructure renewals charge as a component of the depreciation charge for the year.

1. STATEMENT OF ACCOUNTING POLICIES (continued)

(a) Historical cost information (continued)

(iii) Infrastructure assets (continued)

- restatement of the cost of infrastructure fixed assets to reflect the treatment of Section 19 'overlap' expenditure. The objective of the Section 19 quality programme was to address water discolouration through relining or replacing pipes. The 'overlap' represented the extra cost of replacing pipes rather than relining them where their structural condition was insufficient to withstand the relining process. Such expenditure was included in the infrastructure renewals charge in the regulatory accounts. The statutory financial statements classified such expenditure as capital in nature, included in infrastructure assets in the fixed asset note.

(iv) Grants and contributions

Grants and contributions relating to infrastructure assets have been deducted from the cost of those assets, in accordance with RAG 3.07. This is not in accordance with the Companies Act 2006 which requires fixed assets to be stated at their purchase price or production cost without deduction of grants and contributions which are accordingly accounted for as deferred income. The effect of the departure on the value of tangible fixed assets is disclosed in note (A). The statutory financial statements reflect grants and contributions as deferred income and amortise them to profit and loss account over the expected useful economic lives of the assets, resulting in a higher operating profit in the statutory financial statements.

Capital grants and contributions relating to other assets are treated as deferred income and amortised in the profit and loss account over the expected useful economic lives of the qualifying assets.

(v) Capitalisation policy

The capitalisation policies applied in the regulatory accounts comply with FRS 15, other than for infrastructure renewals accounting for which FRS 15 is disapplied in accordance with RAG 1.05 Guideline for accounting for capital maintenance charges and current costs.

Construction or purchase of new assets is capitalised. Subsequent maintenance expenditure is treated as an operating cost unless it provides an enhancement of economic benefits in excess of the expected standard of performance such as an extension in the estimated useful life or an increase in capacity, in which case it is capitalised.

Replacement of assets, including full pipe lengths, stop taps, valves, meter chambers and manhole covers, are capitalised. Repair work and cleaning are charged to operating costs, as are all 'find and fix' leakage costs. CCTV work is charged to operating costs unless it leads specifically to a capital job.

Activities such as zonal studies or catchment studies, which are integral to the capital planning and prioritisation process, are capitalised.

Increases in operating costs incidental to a capital project are not capitalised, for example, higher treatment costs resulting from a works being taken out of service for refurbishment.

Direct labour costs are initially charged as operating costs and, for staff working on capital schemes, time is allocated by timesheets and recharged to the capital project based on an hourly rate reflecting actual costs.

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

(b) Current cost information

The accounting policies used are the same as those adopted in the historical cost regulatory accounts, except as set out below. This financial information has been prepared for the appointed business of NWL in accordance with guidance issued by Ofwat for modified real time financial statements suitable for regulation in the water industry. They measure profitability on the basis of real financial capital maintenance in the context of assets which are valued at their current cost value to the business.

(i) Tangible fixed assets

Assets in operational use are valued at the replacement cost of their operating capability. To the extent that the regulatory regime does not allow such assets to earn a return high enough to justify that value, no adjustment is made in arriving at the replacement cost. No provision is made for the possible funding of future replacements of assets by contributions from third parties, although some of those assets would on replacement be so funded. Therefore, replacement cost again differs from value to the business. Redundant assets are valued at their recoverable amounts.

1. STATEMENT OF ACCOUNTING POLICIES (continued)

(c) Current cost information (continued)

(i) Tangible fixed assets (continued)

A process of continuing refinement of the AMP, based on serviceability, will result in adjustments to the existing valuation of assets at the end of the regulatory review period. In intervening years, values are restated to take account of changes in the general level of inflation as measured by changes in RPI inflation over the year.

- **Land and buildings**
  Non-specialised operational properties were valued at 31 March 2008 on the basis of open market value for existing use and subsequently, annually revalued to take account of changes in the general level of inflation as measured by changes in the RPI. Specialised operational properties are valued at the lower of depreciated replacement cost and recoverable amount.

- **Infrastructure assets**
  Mains, sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls are valued at replacement cost determined principally on the basis of data provided by the AMP.

- **Other fixed assets**
  All other fixed assets are valued periodically at depreciated replacement cost.

- **Surplus land**
  Surplus land is valued at recoverable amount taking into account that part of any proceeds to be passed on to customers under Condition B of the Licence.

- **Grants and contributions**
  Grants and contributions are revalued to take account of changes in the general level of inflation as measured by changes in the RPI over the year.

(ii) Real financial capital maintenance adjustments

The real financial capital maintenance adjustments are calculated by applying depreciation to the current cost value of fixed assets.

(iii) Working capital adjustment

The working capital adjustment is calculated by applying the change in the RPI over the year to the opening balance of working capital.

(iv) Financing adjustment

The financing adjustment is calculated by applying the RPI change over the year to the opening balance of net finance which comprises all monetary assets and liabilities in the balance sheet except those included in working capital.

(v) Accounting separation policy

Cost allocations have been prepared in accordance with RAG 4.04 Guideline for the definitions for the regulatory accounts tables. All costs are recorded in the accounting records by cost centre. Cost centres are defined as either direct departments, comprising operational and customer functions, or support departments. Direct departments are mostly directly allocated to service activities based on the nature of the function, although some costs require apportionment on an appropriate basis. Support departments are apportioned to direct departments either based upon a specific analysis of the costs or by apportionment by an appropriate cost driver. Once allocated to the direct departments the costs are then allocated to service activities pro-rata to the direct cost allocations of the direct department costs.

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

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

2. OPERATING COST ANALYSIS for the year ended 31 March 2015

Wholesale Business only

	Water					**Sewerage**					
	Resources	Raw water distribution	Treatment	Treated distribution	Water sub-total	Sewage collection	Sewage treatment	Sludge treatment	Sludge disposal	Sewerage sub-total	Total
	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m
Operating expenditure											
Power	5.0	1.3	2.8	10.2	19.3	4.9	8.3	(0.2)	-	13.0	32.3
Income treated as negative expenditure	(0.1)	(0.2)	-	-	(0.3)	-	-	(1.6)	-	(1.6)	(1.9)
Service charges	19.7	-	0.2	-	19.9	1.1	1.5	-	-	2.6	22.5
Bulk supply imports	2.2	-	-	-	2.2	-	-	-	-	-	2.2
Other operating expenditure	10.8	1.1	29.4	41.2	82.5	20.4	18.5	16.9	1.4	57.2	139.7
Local authority rates	-	-	22.6	-	22.6	0.2	9.4	-	-	9.6	32.2
Total operating expenditure excluding third party services	37.6	2.2	55.0	51.4	146.2	26.6	37.7	15.1	1.4	80.8	227.0
Capital maintenance											
Infrastructure renewals charge	1.4	0.8	-	31.3	33.5	15.4	0.9	-	-	16.3	49.8
Current cost depreciation	5.3	2.5	34.5	46.8	89.1	12.3	52.5	16.9	0.1	81.8	170.9
Recharges to other business units	-	-	-	(6.5)	(6.5)	(0.1)	-	-	-	(0.1)	(6.6)
Recharges from other business units	0.8	0.1	1.2	0.2	2.3	0.8	1.3	0.3	-	2.4	4.7
Amortisation of deferred credits	(0.2)	-	(0.1)	(1.3)	(1.6)	(0.9)	(0.1)	-	-	(1.0)	(2.6)
Total capital maintenance excluding third party services	7.3	3.4	35.6	70.5	116.8	27.5	54.6	17.2	0.1	99.4	216.2
Third party services											
Operating expenditure	8.4	3.1	0.4	1.1	13.0	0.3	2.7	-	-	3.0	16.0
Total operating costs	53.3	8.7	91.0	123.0	276.0	54.4	95.0	32.3	1.5	183.2	459.2

2. OPERATING COST ANALYSIS for the year ended 31 March 2015 (continued)

	Retail Business only		
	Household	Non-household	Total
	£'m	£'m	£'m
Operating expenditure			
Customer services	12.2	1.9	14.1
Debt management	4.1	0.5	4.6
Doubtful debts	19.6	2.0	21.6
Meter reading	2.0	0.4	2.4
Services to developers	-	0.2	0.2
Other operating expenditure	10.3	1.3	11.6
Local authority rates	0.3	-	0.3
Total operating expenditure excluding third party services	48.5	6.3	54.8
Third party services operating expenditure	0.7	-	0.7
Total operating expenditure	49.2	6.3	55.5
Current cost depreciation	3.2	-	3.2
Recharges to other business units	(0.7)	-	(0.7)
Recharges from other business units	2.0	0.6	2.6
Total capital maintenance	4.5	0.6	5.1
Total operating costs	53.7	6.9	60.6
Debt written off	4.3	0.5	4.8

3. CURRENT COST ANALYSIS OF FIXED ASSETS

	Wholesale Business only										
	Water					Sewerage					
	Resources	Raw water distribution	Treatment	Treated distribution	Water sub-total	Sewage collection	Sewage treatment	Sludge treatment	Sludge disposal	Sewerage sub-total	Total
Non infrastructure assets	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m
Gross replacement cost											
As at 1 April 2014	296.2	221.6	1,273.3	1,538.5	3,329.6	395.0	2,026.2	468.1	0.5	2,889.8	6,219.4
AMP adjustment	-	-	(0.1)	11.8	11.7	(0.1)	(0.1)	(0.1)	-	(0.3)	11.4
Reclassification adjustment	-	-	-	(0.4)	(0.4)	(0.1)	0.1	-	-	-	(0.4)
RPI adjustment	2.6	2.0	11.4	14.1	30.1	3.8	18.4	5.3	-	27.5	57.6
Disposals	-	-	(0.1)	(5.6)	(5.7)	(0.1)	(0.2)	-	-	(0.3)	(6.0)
Additions	10.0	0.1	19.7	29.2	59.0	16.1	30.1	7.6	-	53.8	112.8
As at 31 March 2015	308.8	223.7	1,304.2	1,587.6	3,424.3	414.6	2,074.5	480.9	0.5	2,970.5	6,394.8
Depreciation											
As at 1 April 2014	114.8	76.1	690.5	747.4	1,628.8	187.7	1,040.7	215.3	0.2	1,443.9	3,072.7
AMP adjustment	-	-	(0.5)	(3.2)	(3.7)	(0.1)	(0.2)	68.6	-	68.3	64.6
RPI adjustment	0.8	0.5	5.6	6.2	13.1	1.7	8.8	1.8	-	12.3	25.4
Disposals	-	-	(0.2)	(5.1)	(5.3)	(0.1)	(0.2)	-	-	(0.3)	(5.6)
Charge for the year	5.3	2.5	34.5	46.8	89.1	12.3	52.5	16.9	0.1	81.8	170.9
As at 31 March 2015	120.9	79.1	729.9	792.1	1,722.0	201.5	1,101.6	302.6	0.3	1,606.0	3,328.0
Net book amount at 31 March 2015	187.9	144.6	574.3	795.5	1,702.3	213.1	972.9	178.3	0.2	1,364.5	3,066.8
Net book amount at 1 April 2014	181.4	145.5	582.8	791.1	1,700.8	207.3	985.5	252.8	0.3	1,445.9	3,146.7
Infrastructure assets											
Gross replacement cost											
As at 1 April 2014	1,130.9	790.2	-	5,178.0	7,099.1	13,036.2	164.8	-	-	13,201.0	20,300.1
AMP adjustment	-	-	-	(0.2)	(0.2)	-	-	-	-	-	(0.2)
RPI adjustment	10.2	7.1	-	46.6	63.9	117.3	1.5	-	-	118.8	182.7
Additions	7.0	-	-	16.0	23.0	64.8	-	-	-	64.8	87.8
As at 31 March 2015	1,148.1	797.3	-	5,240.4	7,185.8	13,218.3	166.3	-	-	13,384.6	20,570.4

3. CURRENT COST ANALYSIS OF FIXED ASSETS (continued)

	Retail Business only		
	Household	**Non-household**	**Total**
	£'m	£'m	£'m
Gross replacement cost			
As at 1 April 2014	69.7	-	69.7
Reclassification adjustment	0.3	-	0.3
RPI adjustment	1.0	-	1.0
Disposals	(0.1)	-	(0.1)
Additions	4.0	-	4.0
As at 31 March 2015	74.9	-	74.9
Depreciation			
As at 1 April 2014	44.7	-	44.7
RPI adjustment	0.5	-	0.5
Disposals	(0.1)	-	(0.1)
Charge for the year	3.2	-	3.2
As at 31 March 2015	48.3	-	48.3
Net book amount at 31 March 2015	26.6	-	26.6
Net book amount at 1 April 2014	25.0	-	25.0

4. ANALYSIS OF CAPITAL EXPENDITURE, GRANTS AND LAND SALES for the year ended 31 March 2015

	2015			2014		
	Gross	Grants & contributions	Net	Gross	Grants & contributions	Net
	£'m	£'m	£'m	£'m	£'m	£'m
Capital expenditure - water						
Base						
Infrastructure renewals expenditure (IRE)	31.3	(1.0)	30.3	39.9	(2.9)	37.0
Maintenance non-infrastructure (MNI)	45.4	-	45.4	53.8	(0.1)	53.7
Enhancements						
Infrastructure enhancements	23.0	(9.4)	13.6	21.6	(7.7)	13.9
Non-infrastructure enhancements	12.4	(2.7)	9.7	7.0	(2.3)	4.7
Total capital expenditure - water	112.1	(13.1)	99.0	122.3	(13.0)	109.3
Grants and contributions - water						
Developer contributions (ie Enhancement requisitions, grants and contributions)		(7.2)			(5.9)	
Infrastructure charge receipts - new connections		(4.9)			(4.1)	
Other Contributions		(1.0)			(3.0)	
Total grants and contributions - water		(13.1)			(13.0)	
Capital expenditure - sewerage						
Base						
Infrastructure renewals expenditure (IRE)	17.2	(2.1)	15.1	25.2	(1.0)	24.2
Maintenance non-infrastructure (MNI)	44.2	(0.7)	43.5	46.8	(0.1)	46.7
Enhancements						
Infrastructure enhancements	64.8	(6.0)	58.8	30.0	(2.2)	27.8
Non-infrastructure enhancements	14.8	(1.7)	13.1	5.9	(1.4)	4.5
Large projects capex						
Total capital expenditure - sewerage	141.0	(10.5)	130.5	107.9	(4.7)	103.2
Grants and contributions - sewerage						
Developer contributions (ie Enhancement requisitions, grants and contributions)		(3.6)			(0.9)	
Infrastructure charge receipts - new connections		(3.1)			(2.5)	
Other Contributions		(3.8)			(1.3)	
Total grants and contributions - sewerage		(10.5)			(4.7)	
Total capital expenditure - water and sewerage	253.1	(23.6)	229.5	230.2	(17.7)	212.5
Land sales - Proceeds from disposals of protected land			2.6			3.5

5. WORKING CAPITAL

	2015	2014
	£'m	£'m
Stocks	2.0	2.5
Trade debtors:		
-measured household	26.0	21.7
-unmeasured household	49.8	49.7
-measured non-household	10.0	9.8
-unmeasured non-household	0.7	0.8
-other	4.5	4.7
Measured income accrual	58.2	55.1
Prepayments and other debtors	28.8	17.4
Trade creditors	(8.2)	(5.6)
Deferred income - customer advance receipts	(13.6)	(17.0)
Capital creditors	(33.8)	(33.2)
Accruals and other creditors	(72.2)	(73.4)
Total working capital	52.2	32.5
Total revenue outstanding:		
Household	75.8	71.4
Non-household	10.7	10.6

6. ANALYSIS OF NET DEBT, GEARING AND INTEREST COSTS FOR THE APPOINTED BUSINESS

	Fixed rate	Floating rate	Index linked	Total
	£'m	£'m	£'m	£'m
Borrowings (excluding preference shares)	1,683.6	280.9	646.7	2,611.2
Preference share capital				-
Total borrowings				2,611.2
(Cash)/Overdraft				(9.6)
Short term deposits				(15.0)
Net debt				2,586.6
Regulatory capital value				3,915.3
Gearing				0.66
Full year equivalent nominal interest cost	97.4	5.6	25.5	128.5
Full year equivalent cash interest payment	97.4	5.6	10.3	113.3
Indicative interest rates:				
Indicative weighted average nominal interest rate	5.79%	1.99%	3.94%	4.92%
Indicative weighted average cash interest rate	5.79%	1.99%	1.59%	4.34%
Weighted average years to maturity	13	7	27	16

7. REGULATORY CAPITAL VALUE

	2014-15
	£'m
Closing Regulatory Value at 31 March 2014 (March 2014 prices)	3,883.4
RPI from March 2014 to March 2015 (0.9%)	35.1
Opening regulatory capital value at 1 April 2014	3,918.5
Infrastructure renewals expenditure (IRE)	52.1
Infrastructure renewals charge	(53.6)
Capital expenditure (excluding IRE)	200.8
Grants and contributions	(20.3)
Current cost depreciation	(179.2)
Outperformance adjustment	(3.0)
Closing regulatory capital value at 31 March 2015	3,915.3
Year average regulatory capital value	3,910.8

Note the average year regulatory capital value is in the average year price base, all other figures are in the year end price base. Differences between the above figures and actual capital expenditure, infrastructure renewals expenditure, infrastructure renewals charge, grants and contributions and current cost depreciation do not affect the price limits set for the period 2010-15. They were taken into account in the calculation of outperformance adjustments at the Periodic Review in 2014. The figures above are consistent with Appendix 4 of the Ofwat publication: 'Future Water and Sewerage Charges 2010-15: Final Determinations'.

8. NON-FINANCIAL INFORMATION for the year ended 31 March 2015

	2015		2014	
	Water	Sewerage	Water	Sewerage
Number of properties	'000	'000	'000	'000
Total company				
Households billed	1,788	1,123	1,777	1,117
Non-households billed	95	55	97	56
Household voids	81	53	80	53
Non-household voids	15	12	16	12
Properties served by new appointee in supply area as at 1 April 2009	-	-	-	-
Per capita consumption (excluding supply pipe leakage)	l/h/d		l/h/d	
Northumbrian Water				
Unmeasured household	143.82		143.07	
Measured household	135.45		136.63	
Essex and Suffolk Water				
Unmeasured household	157.89		159.49	
Measured household	142.89		142.23	
Volume	Ml/d		Ml/d	
Northumbrian Water				
Bulk supply export	0.71		0.71	
Bulk supply import	0.01		0.01	
Distribution input	670.49		664.97	
Essex and Suffolk Water				
Bulk supply export	2.24		2.21	
Bulk supply import	83.43		84.16	
Distribution input	428.81		428.31	

9. DISCLOSURE OF TRANSACTIONS WITH ASSOCIATES

Services supplied by the appointee to associated companies:

Associate	Service	Turnover	Terms of Supply	Value 2014/15
		£'m		£'m
AquaGib	Sale of materials	16.7	Negotiated	0.1
Northern Gas Networks Limited (NGN)	Mains repairs	411.3	Negotiated	0.1
Vehicle Lease and Service Limited (VLS)	Rental of garage and service charges	15.8	Negotiated	0.1

Services supplied to the appointee by associated companies:

Associate	Service	Turnover	Terms of Supply	Value 2014/15
		£'m		£'m
HWL	Oracle licensing	21,302.4	Negotiated	1.6
NGN	Gas main diversions	411.3	No market	0.4
NWGL	Holding company charges	7.5	No market	0.8
Three Rivers Insurance Company Limited (TRICL)	Public liability insurance (deductible infill policy)	0.6	No market	0.5
VLS	Vehicle maintenance and capital finance charge	15.8	Competitive letting	7.8

Turnover data for AquaGib, NWGL and TRICL relates to the 15 months to 31 March 2015. Turnover data for NGN relates to the 12 months to 31 March 2015. Turnover data for VLS and HWL relates to the 12 months to 31 December 2014.

Information in relation to allocations and apportionments

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

Turnover is separately recorded between water services and sewerage services and no apportionment has been necessary. Operating costs have been allocated between water and sewerage services in accordance with the guidance set out in RAG 4.04.

Overhead costs incurred in the appointed business which relate to the non-appointed business have been allocated using an activity based approach to comply with RAG 5.04.

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

Amounts borrowed by the appointee from associated companies

The Company has loans amounting to £1,965.0m due to NWF, a subsidiary company. Details of these loans and the associated guarantees are provided in note 19 of the historical cost regulatory accounts.

The Company acquires vehicles from VLS, an associated company, on a finance lease basis. During the year, new finance leases of £1.9m were entered into and capital repayments of £3.2m were made. The year end finance lease creditor was £8.2m. All leases are at a fixed interest rate of 6%.

Guarantees or other forms of security

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

9. DISCLOSURE OF TRANSACTIONS WITH ASSOCIATES (continued)

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

	£'m
Dividends paid:	
Interim paid for the period ended 31 March 2015	98.7
Interim paid for the period ended 31 March 2015	98.8
Interim paid for the period ended 31 March 2015	99.7
Total dividends paid in the period	297.2

No final dividend was proposed for the period ended 31 December 2013 (31 December 2013: nil).

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

Accordingly, the level of dividend has been declared by reference to:

- the Company's ability to finance its functions;
- the Company's cumulative financial performance and past outperformance; and
- maintaining the Company's stable strong investment grade credit ratings.

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

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

The information in this note has been produced to comply with the requirements of RAG 5.04 Transfer Pricing in the Water Industry and the disclosures required by paragraph 6 of Condition F of the Company's operating licence.

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

10. STATEMENT ON DIRECTORS' PAY AND STANDARDS OF PERFORMANCE

(a) Compliance with legislation

The following statement on Directors' remuneration is disclosed in accordance with section 35A of the Water Act 2003. It also has regard to the requirements of the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 in respect of Directors' remuneration reporting for quoted companies, albeit in the context of a company which is not a listed public limited company. The information in section (d) below has been audited.

(b) Statement by the Chairman of the Remuneration Committee

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

The work of the Remuneration Committee comprises the adoption of principles and standards in relation to executive remuneration and benefits, as well as agreeing individual remuneration packages. All decisions regarding Directors' remuneration are taken by the Committee, other than where stated.

During the year, the Committee:
- agreed bonuses for the 2014 calendar year;
- set performance targets for executive Directors and senior managers for the 2015 calendar year; and
- agreed the level at which the Long Term Incentive Plan (LTIP) award in respect of the 2014 calendar year would vest.

A J Hunter
Chairman of the Remuneration Committee

(c) Remuneration Policy

The policy of the Remuneration Committee is to pay no more than necessary to attract and retain good quality Directors, and to ensure that policy is aligned with market practice.

Executive Directors
The remuneration of the Executive Directors comprises:
- basic salary;
- benefits (including pension);
- a performance related annual bonus;
- annual LTIP awards; and
- pension benefits.

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

Basic salary
Basic salary is reviewed annually based on individual contributions, periodic benchmarking to the external market and with regard to the expected pay award for other groups of employees.

The basic salaries payable to Directors of NWL are not directly linked to specific standards of performance in connection with the carrying out of functions of a 'relevant undertaker'. There is no variable performance related element.

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

10. STATEMENT ON DIRECTORS' PAY AND STANDARDS OF PERFORMANCE (continued)

(c) Remuneration Policy (continued)

Bonus
The annual bonus is related to performance in the year, and is assessed on a calendar year basis. The performance targets are firmly linked to NWL's strategic themes (customer, competitiveness, people, environment and communities). Stretching targets are set which are aligned to the Company's vision of being the national leader in the provision of sustainable water and waste water services.

Bonuses are paid in cash with no deferral. A clawback applies in the event that results on which the bonus is paid are subsequently found to be inaccurate or there has been relevant misconduct on the part of the employee. The bonus is structured with three elements, determined by the Committee:

- up to 50% payable on financial targets;
- up to 40% payable on balanced scorecard targets; and
- up to 10% payable on performance against personal targets.

The maximum bonus payable, as a percentage of basic salary, is 70% for the CEO and 50% for the other Executive Directors.

LTIP
Executive Directors participate in a cash based LTIP assessed against financial, customer service and asset performance targets. The purpose of the LTIP is to reward a balanced approach between finance and performance, encourage a one team approach, engender a longer term view, remain competitive in the executive market and encourage retention of key people. Vesting is based on performance in the first calendar year after award. However, payment is deferred until the completion of three years from the start of the performance period.

The LTIP is structured with three elements, determined by the Committee:

- up to 70% payable on financial performance;
- up to 15% payable on customer service performance; and
- up to 15% payable on asset performance.

Financial performance is assessed through the generation of sufficient profits to make distributions to Group shareholders in line with the Board approved plan. There is no vesting if the distribution target is not achieved. If the target is achieved then 50% of the 70% vests. Vesting would increase on a sliding scale such that 100% of the 70% would vest if 105% of the target is achieved.

Customer service performance is assessed by comparing NWL's SIM score (quantitative and qualitative combined) with those of the other water and sewerage companies in England and Wales in the relevant regulatory year. There is no vesting of this part of an award unless fifth position in the rankings is achieved. If the position achieved is fifth or higher, vesting is on a sliding scale with 50% of the 15% awarded for fifth place and 100% of 15% awarded for first place.

50% of the 15% available in respect of asset performance vests for stable serviceability assessments in the relevant regulatory year in three of the four asset classes (water non-infrastructure, water infrastructure, sewerage non-infrastructure and sewerage infrastructure). All of the 15% available vests for stable assessments in all four asset classes.

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

Pension
The Company operates the Northumbrian Water Pension Scheme (NWPS) which has defined benefit and defined contribution (money purchase) sections. The defined benefit section closed to new entrants on 31 December 2007.

A C Jones participates in a defined benefit section, making an employee contribution of 8% of basic salary (under a salary sacrifice arrangement) and receiving an employer contribution equivalent to 16.9% of salary. Benefits relate to final salary and currently accrue at 1/45th for each year of service.

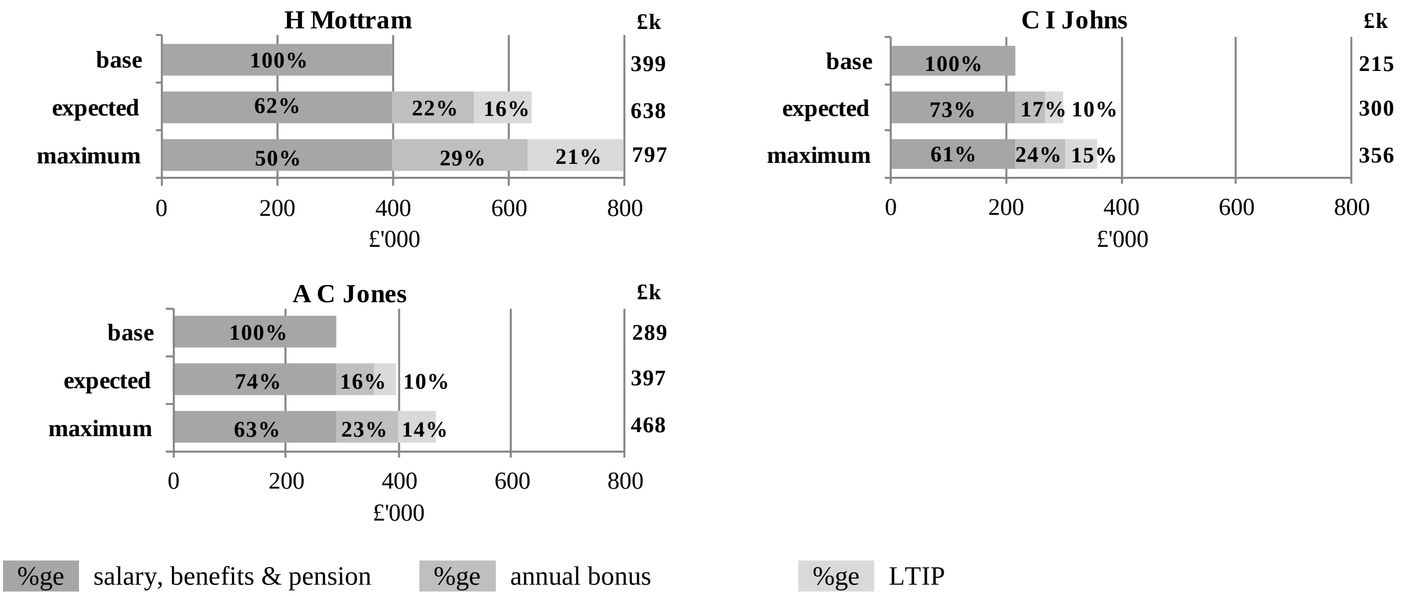
10. STATEMENT ON DIRECTORS' PAY AND STANDARDS OF PERFORMANCE (continued)

(c) Remuneration Policy (continued)

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

More details of the NWPS are provided in note 25 of Section A. There is no variable performance related element.

Illustration of remuneration policy



For the purposes of the graph, annual bonus and LTIP have been assumed to achieve 60% of their maximum potential value, though awards are dependent upon actual performance. Information on actual awards for bonus and LTIP in respect of 2014 is provided on pages 76 to 77.

Non-executive Directors
The Company's policy is that the Independent Non-executive Directors receive fees for their duties. The level of fees is set by reference to the market. An additional fee is paid to the Chair of the Audit Committee to reflect the additional responsibilities and time commitment involved. The Non-executive Directors do not receive benefits in kind and do not participate in bonus, LTIP or pension schemes operated by the Company.

The Independent Non-executive Directors do not receive any other remuneration from the Company, the Group or its shareholders.

In respect of the Non-executive Directors appointed by the Group's shareholders, F R Frame receives the same base fee for performing his duties as a Director of both the Company and NWGL. This fee is shared with NWL paying a 30% proportion and NWGL paying the remaining 70%. The other Non-executive Directors receive no remuneration from the Company.

10. STATEMENT ON DIRECTORS' PAY AND STANDARDS OF PERFORMANCE (continued)

(d) Directors' remuneration in 2014-15

The table below shows the total remuneration paid by the Company to Directors during the 12 month periods to 31 March 2014 and 2015. The table has been produced in accordance with the requirements of Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 and, as a result of this and the different time periods covered, the total remuneration differs from that reported in note 5 of Section A.

	salaries and fees		benefits in kind		bonus		LTIP		pension		total remuneration	
	2015	2014	2015	2014	2015	2014	2015	2014	2015	2014	2015	2014
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
H Mottram	319	303	10	11	206	196	99	94	60	58	694	662
C I Johns	159	155	9	14	48	52	31	30	42	41	289	292
A C Jones	212	209	14	13	60	67	40	38	56	74	382	401
G Neave	189	249	11	14	68	75	45	42	22	28	335	408
M Fay	42	41	-	-	-	-	-	-	-	-	42	41
F R Frame	12	12	-	-	-	-	-	-	-	-	12	12
Dr S Lyster	42	41	-	-	-	-	-	-	-	-	42	41
M A B Nègre	42	41	-	-	-	-	-	-	-	-	42	41
P Rew	54	52	-	-	-	-	-	-	-	-	54	52
	1,071	1,103	44	52	382	390	215	204	180	201	1,892	1,950

The table shows only the proportion of remuneration borne by the Company. For two of the Directors, H Mottram and C I Johns, NWL pays 70% of the remuneration and NWGL pays the remaining 30%. For F R Frame, NWL pays 30% of his remuneration and NWGL pays the remaining 70%. For the other Directors reported in the table, NWL paid 100% of their remuneration in both 2013-14 and 2014-15.

G Neave resigned from the Board on 31 December 2014.

In 2012, after the change in ownership, the Committee agreed to restructure the remuneration of the Executive Directors by reducing the value of bonus and LTIP awards and offsetting this with an adjustment to basic pay. Specialist support was provided by Hay at that time to ensure jobs were sized correctly and a review of the market took place. This policy has remained in place for the calendar years 2013 and 2014.

Basic salary
In 2012 the Committee agreed to restructure the remuneration of the executive Directors by reducing the value of bonus and LTIP awards and offsetting this with an adjustment to basic pay (with advice from Hay Group, independent external reward consultants). This became effective from January 2013. For 2015, senior executives were awarded an annual increase in their basic salaries of 2.6%, which was in line with the level awarded to other employee groups.

Benefits
Taxable benefits provided to the Executive Directors comprise car and fuel allowance, healthcare and professional subscriptions. The values are not significant in the context of overall remuneration.

10. STATEMENT ON DIRECTORS' PAY AND STANDARDS OF PERFORMANCE (continued)

(d) Directors' remuneration in 2014-15 (continued)

Bonus

The annual bonus for the calendar year 2014 was structured by the Committee, in accordance with the policy outlined above, as follows:

- up to 50% payable on Balanced Scorecard financial targets;
- up to 40% payable on Balanced Scorecard targets; and
- up to 10% payable on performance against personal targets.

The Balanced Scorecard targets and performance were as follows:

Strategic theme	Scorecard measure	Target 2014	Performance 2014	% of total bonus potential	% of total awarded
Competitiveness	Group EBIT	budget	achieved	25	13.59
(financial targets)	Group cash available for distribution	budget	achieved	25	12.5
Customer	Customer satisfaction				
	- SIM quantitative score	90	91.66	2	0
	- SIM qualitative score	4.7	4.59	2	0
	Water supply interruptions >6 hours (average per property (minutes))	7.30	4.56	4	4
	Coliform incidents (no.)	8	13	4	0
People	Employee engagement score (Sunday Times 'Best Companies' survey)	2*	1*	4	0
	Lost time reportable accidents (no.)	4	7	4	0
Environment	Leakage (Mld)				
	- NW	144	134.0	2	2
	- ESW	66	58.4	2	2
	STW failing LUT consent (%)	0	0	4	4
	Pollution incidents (categories 1 & 2)	2	3	4	0
Communities	BITC Platinum Plus accreditation	retain status	status retained	4	4
	Just an Hour (employee participation)	50%	55%	4	4
Total bonus related to Balance Scorecard				**90**	**46.09**

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

- H Mottram had targets including delivering expected financial performance, specifically to ensure retention of existing credit ratings, delivery of outstanding customer service, a continued focus on improving sewer flooding performance and leading the regulatory business planning process through the year.
- C I Johns had targets including delivering expected financial performance, specifically to ensure retention of existing credit ratings, assessing the outcome of the December 2013 pension actuarial valuation and assessing the potential impact of changes in accounting standards and developing a transition plan.
- A C Jones had targets including planning for the impacts of retail separation and ensuring delivery of the 2014 Health & Safety Plan.
- G Neave had targets in relation to delivery of the capital investment programme, establishment of a Programme Management Office to drive future capital efficiencies and achievement of PAS55 certification for the Company's asset management processes.

A number of these targets related to NWL's performance as a relevant undertaker. In assessing overall performance, the Committee takes into account the Company's position in Ofwat reports. The relevant performance data published by Ofwat is also used by the CEO to assess G Neave's and A C Jones' performance and this informs the bonus recommendation put to the Committee.

For the CEO, in addition to the bonus calculation explained above, a further discretionary award was made by the Committee to reflect the Board's continued satisfaction with the CEO's performance and, in particular, the reputational impact of the significant external recognition achieved by the Company. This remained within the limit of the overall potential maximum bonus award.

10. STATEMENT ON DIRECTORS' PAY AND STANDARDS OF PERFORMANCE (continued)

(d) Directors' remuneration in 2014-15 (continued)

Bonus (continued)
The total annual bonus awards for 2014 were as follows:

	Bonus awarded (out of 100%)	Maximum bonus (% of basic salary)	Bonus awarded (% of basic salary)
H Mottram	91.28%	70%	63.89%
C I Johns	56.09%	50%	28.05%
A C Jones	55.09%	50%	27.55%
G Neave	56.09%	50%	28.05%

LTIP
A cash based LTIP was awarded by the Committee in 2014, structured in accordance with the policy outlined above, as follows:

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

The scheme related to the period January 2014 to December 2016. Performance targets were to be assessed in the first year of the scheme. However, payment will be deferred until early 2017, after the end of the three year scheme period.

The Committee assessed the performance against the scheme criteria in January 2015. In respect of financial performance, 35% out of the maximum of 70% available vested.

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

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

The Committee therefore approved that the 2014 LTIP should vest at 61.25%. This is not dependent upon any future performance conditions being met.

Pension
Pension arrangements operated in accordance with the policy outlined on pages 73 to 74 above.

10. STATEMENT ON DIRECTORS' PAY AND STANDARDS OF PERFORMANCE (continued)

(e) Implementation of remuneration policy in 2015-16

There have been no changes made by the Committee to the remuneration policy to be implemented in 2015-16.

Bonus

The Balanced scorecard targets for the calendar year 2015 bonus are as follows:

Strategic theme	**Scorecard measure**	**Target 2015**	**% of total bonus potential**
Competitiveness (financial targets)	Group EBIT	budget	25
	Group cash available for distribution	budget	25
Customer	Customer satisfaction		
	- SIM qualitative score	4.65	3
	- SIM quantitative score	63.75	1
	Water supply interruptions >6 hours (mins)	5.00	4
	Mean zonal compliance	99.9	4
	Repeat sewer flooding (properties)	269	4
People	Employee engagement score	81%	4
	Lost time reportable accidents (no.)	3	4
Environment	Leakage (Mld)		
	- NW	141	2
	- ESW	66	2
	STW failing LUT consent (%)	0	4
Communities	BITC Platinum Plus accreditation	retain status	4
	Just an Hour (employee participation)	50%	4
Total bonus related to Balance Scorecard			**90**

Personal targets for 2015 have been set as follows:

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

LTIP

A new cash based LTIP was awarded by the Committee in 2015 for the period January 2015 to December 2017 structured in accordance with the policy outlined above, as follows:

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

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

DIRECTORS' RESPONSIBILITIES AND DECLARATIONS for the year ended 31 March 2015

DIRECTORS' RESPONSIBILITIES STATEMENT

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

(a) ensuring that proper accounting records are maintained by the Appointee to enable compliance with the requirements of Condition F and having regard also to the terms of guidelines notified by the Water Services Regulation Authority ('the Authority') to the Appointee from time to time;

(b) preparing on a consistent basis for each financial year regulatory accounts in accordance with Condition F, having regard also to the terms of guidelines notified by the Authority from time to time, which so far as is reasonably practicable have the same content as the annual financial statements of the Appointee prepared under the Companies Act 2006 and which are prepared in accordance with the formats, accounting policies and principles which apply to those financial statements;

(c) preparing financial statements on a current cost basis in respect of the same accounting period in accordance with guidelines issued by the Authority from time to time; and,

(d) preparing such other financial and related information as is required by Condition F having regard also to the terms of guidelines issued by the Authority from time to time.

RING FENCING

The Directors confirm that, as at 31 March 2015, the Company was in compliance with paragraph 3.1 of Condition K of the Instrument of Appointment by the which the Appointee had available to it sufficient rights and assets to enable a special administrator to manage the affairs, business and property of the Appointee, should a special administrative order be made.

By order of the Board

M Parker
Company Secretary
13 July 2015

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

We have audited the Regulatory Accounts of Northumbrian Water Limited (the Company) for the year ended 31 March 2015 on pages 54 to 79 which comprise:

- the regulatory historical cost accounting statements comprising the regulatory historical cost profit and loss account, the regulatory historical cost balance sheet, the regulatory historical cost statement of total recognised gains and losses and the historical cost reconciliation between statutory and regulatory accounts; and
- the regulatory current cost accounting statements for the appointed business comprising the current cost profit and loss account, the current cost cash flow statement and the related notes to the current cost financial statements, including the statement of accounting policies.

These Regulatory Accounts have been prepared in accordance with the basis of preparation and accounting policies set out in the Statement of Accounting Policies.

This report is made, on terms that have been agreed, solely to the Company and the WSRA in order to meet the requirements of Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water and sewerage undertaker under the Water Industry Act 1991. Our audit work has been undertaken so that we might state to the Company and the WSRA those matters that we have agreed to state to them in our report, in order (a) to assist the Company to meet its obligation under Condition F to procure such a report and (b) to facilitate the carrying out by the WSRA of its regulatory functions, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the WSRA, for our audit work, for this report or for the opinions we have formed.

Respective responsibilities of the WSRA, the Directors and auditors

As explained more fully in the Statement of Directors' Responsibilities set out on page 79, the Directors are responsible for the preparation of the Regulatory Accounts and for their fair presentation in accordance with the basis of preparation and accounting policies. Our responsibility is to audit and express an opinion on the Regulatory Accounts in accordance with International Standards on Auditing (UK and Ireland), except as stated in the 'Scope of the audit of the Regulatory Accounts' below, and having regard to the guidance contained in Audit 05/03 'Reporting to Regulators of Regulated Entities' issued by the Institute of Chartered Accountants in England and Wales. Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the Regulatory Accounts

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

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

Scope of the audit of the Regulatory Accounts (continued)

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

Opinion on Regulatory Accounts

In our opinion the Regulatory Accounts:

- fairly present in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA and the accounting policies set out on pages 28 to 31 and 59 to 62 (including the accounting separation methodology), the state of the Company's affairs at 31 March 2015 on an historical cost and current cost basis, and its historical cost and current cost profit and its current cost cash flow for the year then ended; and
- have been properly prepared in accordance with Condition F, the Regulatory Accounting Guidelines and the accounting policies (including the accounting separation methodology).

Basis of preparation

The Regulatory Accounts have been prepared in accordance with Condition F of the Appointment and the Regulatory Accounting Guidelines, the accounting policies set out in the statement of accounting policies and, in the case of the regulatory historical cost accounting statements, under the historical cost convention.

The Regulatory Accounts are separate from the statutory financial statements of the Company and have not been prepared under the basis of United Kingdom Generally Accepted Accounting Practice ('UK GAAP'). Financial information other than that prepared on the basis of UK GAAP does not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in statutory financial statements prepared in accordance with the Companies Act 2006. Furthermore, the regulatory historical cost accounting statements on pages 54 to 55 have been drawn up in accordance with Regulatory Accounting Guideline 3.07 in that infrastructure renewals accounting as applied in previous years should continue to be applied and accordingly, that the relevant sections of Financial Reporting Standards 12 and 15 be disapplied. The effect of this departure from Generally Accepted Accounting Practice and a reconciliation of the balance sheet drawn up on this basis to the balance sheet drawn up under the Companies Act 2006 is given on page 56.

Opinion on other matters prescribed by Condition F

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

- proper accounting records have been kept by the appointee as required by paragraph 3 of Condition F; and
- the Regulatory Accounts are in agreement with the accounting records and returns retained for the purpose of preparing the Regulatory Accounts.

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

Other matters

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

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

Paul Feechan (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Newcastle Upon Tyne, United Kingdom
13 July 2015