The next chapter.

Annual report and financial statements 2016/17

Our 16/17 overview

99.96%
drinking water quality compliance

First time zero employees off work with a work-related injury

£1.1 billion
invested in infrastructure

4.12 out of 5
Ofwat customer satisfaction rating

£19.75 million
fine for 2012-14 pollutions

42% reduction
in incidents since 2013

£14.6 million (22.5%)
reduction in bad debt charge

94.5%
written complaints resolved first time

£12.9 billion
Regulatory Capital Value (RCV)

£638.4 million
operating profit*

103 km
mains repaired/ replaced

Baa1 corporate family rating
credit rating

Missed our leakage target for the first time in
11 years

267 GWh
electricity generated from sewage – our best ever performance

*Includes Bazalgette Tunnel Limited revenues

See what's inside

Our strategic report

Our corporate governance

Our statutory financial statements

Our place in the water and wastewater industry

With **15 million** customers we serve about **25%** of the population of England and Wales

Thames Water is one of 10 regional licensed and regulated companies

providing water and wastewater services in England and Wales.

We provide almost 1/3 of the

9 billion

litres of water used by people and businesses in the UK each day.

Our importance to the UK economy

We employ around 5,000 people

and many thousands more work in partnership with us

Our services are vital to the safe and smooth running of

London

and the Thames Valley

– huge drivers of the UK economy

We look after...

31,000 km
of water pipes

98 water treatment works

to provide...

2.6 billion litres of water every day.

109,000 km
of sewer pipes

351 sewage treatment works

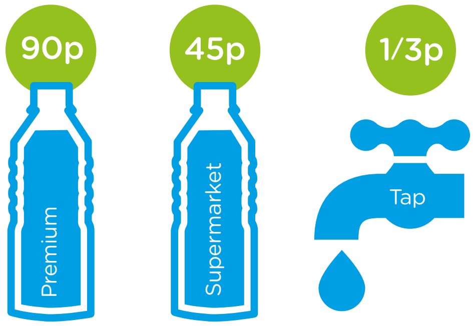
to safely remove...

4.6 billion litres of wastewater every day.

* Source: Discover Water

Value for money*

Price for 2 litres



We provide **270** litres of some of the highest quality water in the world direct to our customers' homes for the same price as two litres of supermarket bottle water.

Population growth in our region

By 2050, London is expected to grow to 11 million, the equivalent of adding both the populations of Birmingham and Edinburgh to the city.

We support thousands of vulnerable households through our social tariffs and customer assistance fund to provide them with one of life's essential ingredients

Our region stretches from...

Cirencester in the west to the edges of **Essex** in the east and includes our nation's capital city, **London**.

We are headquartered in the Thames Valley

We are regulated by

- Ofwat
- Defra
- Drinking Water Inspectorate
- Environment Agency

1 April 2017

opening of business retail market to competition

Rewards and penalties

Ofwat's outcome delivery incentive (ODI) rewards and penalties link performance to company returns

Our vision and values

In 2014, teams from across the business came together to define our vision and values. Three years on, driven by our new CEO, over 1,000 managers came together again to rejuvenate the vision and articulate what it means in practice. This has sparked a companywide conversation to further embed our vision and values in every corner of the business for the benefit of our customers.

The passionate award

The exceptional workmate award

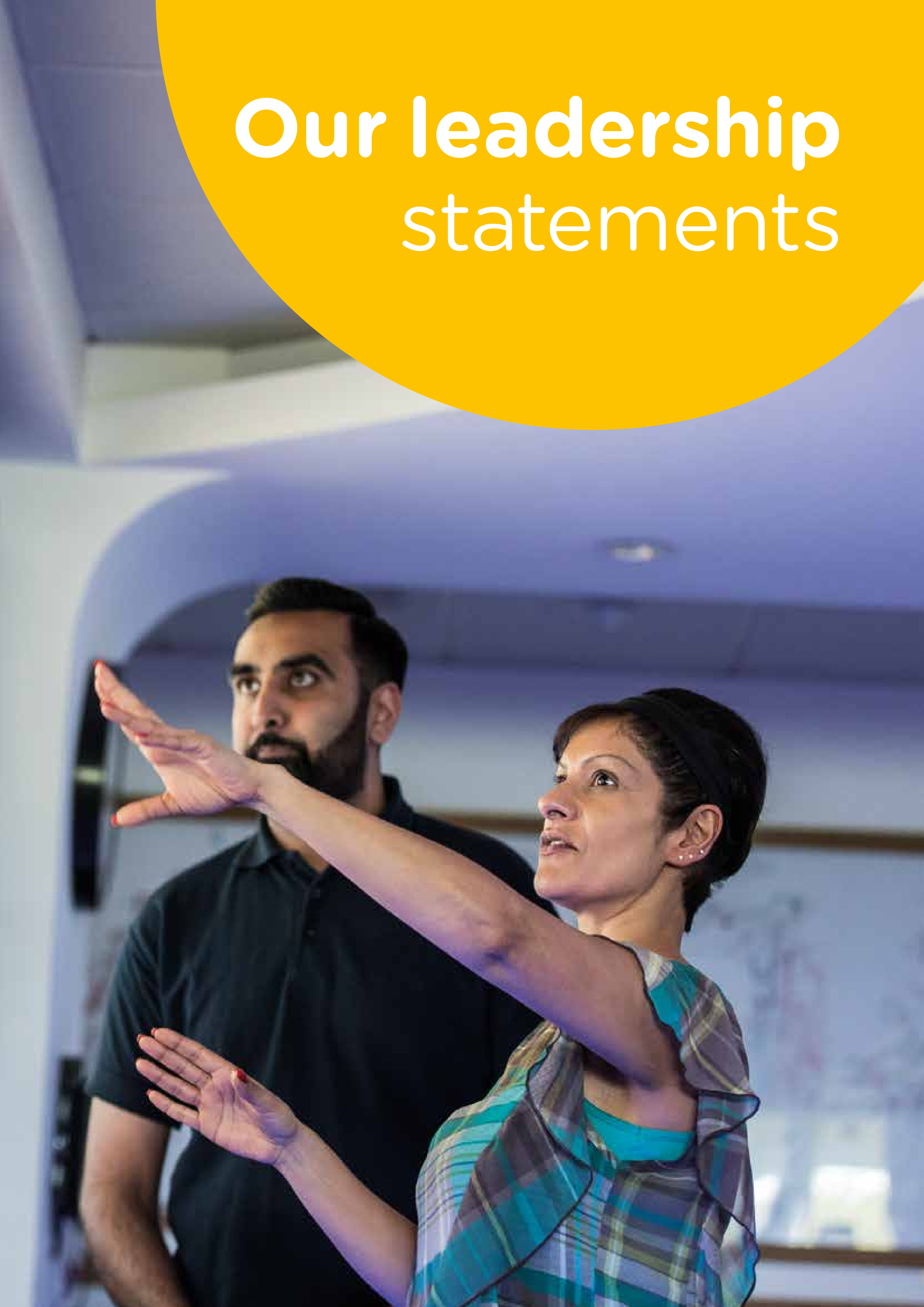
Customer service excellence award

Our Spotlight awards, which attracted over 900 nominations during 2016/17, celebrate our people when they go the extra mile to demonstrate they are living our values for the benefit of customers.

September 2016
New CEO appointed
Steve Robertson

March 2017
New CFO appointed
Brandon Rennet

Our leadership statements



Our Chairman's statement **The next chapter**

After a year of significant change, Thames Water is beginning a new chapter in its 400 year history.

Sir Peter Mason KBE
Chairman

Steve Robertson joined as our new Chief Executive Officer (CEO) in September 2016. As former CEO at Truphone and founding CEO of BT Openreach, Steve has crucial experience running essential infrastructure and high technology companies. We also welcomed our new Chief Financial Officer (CFO), Brandon Rennet, in March 2017. With 14 years in the power and utilities industries, most recently at SSE, Brandon brings a wealth of experience and another fresh perspective to our business.

To maintain our strong governance, we've appointed Nick Land, former Chairman of Ernst & Young, as our new Independent Non-Executive Director to replace Michael Pavia, who retired this year. Nick is the new Chairman of our Audit, Risk and Regulatory Committee. He has extensive boardroom experience and is currently the Chair of Vodafone's Audit and Risk Committee, as well as Chairman of the Private Equity Reporting Group and a member of the Board of the Financial Reporting Council.

2016/17 also saw the announcement of a change in our largest shareholder. Borealis Infrastructure, the infrastructure investment manager of Ontario Municipal Employees Retirement System ("OMERS"), one of Canada's largest pension plans, and Wren House, the global direct infrastructure investment arm of the Kuwait Investment Authority, acquired the 26.3% Macquarie-managed stake. The sale completed on 31 May 2017. We welcome Kenton Bradbury, Managing Director of Asset Management at Borealis, to the Board of Thames Water Utilities Limited. A chartered engineer, Kenton has many years' experience working with a range of major infrastructure and utility companies, including as a Director for Yorkshire Water and Affinity Water.

We've also seen Fiera Infrastructure (Aquila) increase their interest to nearly 5%. More than two thirds of our shareholders now represent pension funds. It is pleasing to know all our shareholders are high-quality, long-term investors who have long-term visions aligned with ours as we prepare for the future – of course, our provision of essential services doesn't stop at the end of each five-year regulatory period.

Amidst this change, we've made headway with some of our performance commitments and have been consolidating these achievements. We have also been working hard to nail down the detail of what we need to do in the coming year to drive a step change in critical areas, such as leakage and customer service, where we have not delivered our performance commitments to our customers. With Steve at the helm, we have a strong executive team in place to help Thames Water become a leading, customer-focused water and wastewater service provider.

Year in review.

We've spent over £1 billion again this year in our business, which means we've invested around £12 billion during the last 12 years. We've seen our investment in producing energy from sewage start to pay off after a slower than expected start last year, with our best performance to date in energy production in 2016/17, and we're nearing the completion of a major upgrade of one of our largest sewage treatment works. Our resolution of complaints is also at an all-time high and, as well as having the largest investment programme in the industry, our average combined bill remains the third lowest in England and Wales at just over £1 a day (£374 per year in 2016/17: £367 in 2015/16). In April 2017, the ratings agency Moody's reaffirmed our Baa1 Corporate Family Rating ("CFR") with a stable outlook, which is a strong investment grade rating and among the industry's best. Being efficient in how we deliver our investments, operate and finance our business, helps us keep bills lower for current and future generations of our customers.

Shareholders invest in companies and expect a return on their investment. We made a solid start to the regulatory period but we didn't pay an external distribution relating to 2015/16 while we supported our tender to award the delivery of the Thames Tideway Tunnel to an independent company. After another year of investing over £1 billion in our business, equivalent to about £20 million a week, we made our first distribution of this regulatory period to our external shareholders – a total of £100 million. Including the distributions we paid to the Group to service debt and working capital requirements (£57 million), this represents a cash yield of 2.6% (see page 37 for further details).

Strengthening our focus.

In March 2017 we incurred a £19.75 million fine for a group of pollution incidents, which occurred between 2012 and 2014 - during the last regulatory period - and we deeply regret these incidents. We're doing things very differently now. We've been more proactive in our wastewater network maintenance, changed our management structure in the affected region and invested heavily in our infrastructure and control systems. I'm pleased to say we've reduced our pollutions by 42% since 2013 and we know there's more we need to do. Our total expenditure on our wastewater network for 2016/17, including operational expenses and investment, was almost £900 million.

2016 was a year of re-evaluation for our water business after a cluster of significant bursts on our Victorian pipes affected customers in London and contributed to us missing our leakage target. Although there was a series of high profile bursts in a short space of time, the number in 2016/17 didn't differ hugely from previous years. Nevertheless we take each incident and its impact on our customers very seriously and there's a lot of work going on to understand why they happened - the report of an independent forensic review about these bursts is available on our website. We continue to work to refocus our priorities and we've committed to increasing our investment in 'trunk' mains replacements by £97 million over the next three years to reduce the likelihood of these devastating events as we strive to ensure we deliver our responsibilities to customers.

Between 2004 and 2015/16 we reduced our leakage by a third. We set ourselves challenging targets for this five year regulatory period as we know it's very important to our customers and the environment. Disappointingly, we weren't where we wanted to be at the end of 2016/17. Our leakage has increased by 5% since last year from 642Ml/d to 677Ml/d and we will incur an outcome delivery incentive ("ODI") penalty of £8.6 million. Next year's target is tighter and we are committed to a recovery plan aimed at bringing us back on track with our leakage targets by the end of the regulatory period.

A changing landscape.

Ahead of the opening of the business retail market to competition on 1 April 2017, all our business retail customers were moved across to Castle Water following our decision to exit the market – in July 2016 we reached an agreement with them to sell our retail non-household business, generating proceeds of £99 million. This change allows us to focus more on the delivery of our core service for our customers in the wholesale and household businesses. It also frees up funds to invest further in areas of the highest priority such as leakage and 'trunk' mains replacements.

We worked hard to ensure we were ready for the biggest change to the water industry since privatisation. The introduction of competition has brought a new dimension to the way we conduct our business – whilst we need to develop strong relationships with the retailers in our region, operationally we retain a direct relationship with business customers so we need to make sure we continue to support them and provide them with the high quality service they need and deserve. We work against an ever-changing backdrop – the water industry is poised for further change as part of Water 2020, and I believe our revised strategic priorities will put us into the best position to embrace the new opportunities and challenges this may bring.

Sir Peter Mason KBE
Chairman

We've committed to increasing our investment in 'trunk' mains replacements by £97 million over the next three years.

CEO's review
A fresh perspective

Since joining Thames Water last September, I've been regularly asked why I decided to join this industry. The answer is simple. After a career in the telecommunications industry, it's hugely exciting to be involved in another sector that touches so many lives every day - and leading a company which is starting a new chapter.

Steve Robertson
Chief Executive Officer

Every day all of us at Thames Water make decisions and take actions that affect our customers, our environment and our business. One of my most critical tasks is to make sure the cumulative effect of these decisions results in the right long-term outcomes as well as meeting our immediate needs. Ensuring the right strategic outcomes for our business, to support the long term needs of our customers, is central to the future of Thames Water.

With this in mind I've spent a significant amount of time over the last few months meeting customers and employees. The passion and commitment of our employees really stood out as well as the overwhelming desire from our customers for us to deliver the service they need and deserve. Increasing our focus to deliver a great customer experience is crucial.

I fully recognise that the privileges of running a water company come with important responsibilities, and I understand the significant impact on our customers and the environment when we fall short of the standards our customers rightly expect of us.

During the last year we've seen a series of major bursts on some of our Victorian water pipes and we've missed our leakage target. Leaks are inevitable on a network of our enormous size and age, but it's vital we invest wisely and continually to improve our resilience. This is a huge priority for us.

We're also paying a high price both financially and reputationally for major pollution incidents between 2012 and 2014. We have apologised and learned our lessons. Since the events we've put in place new procedures and personnel, invested heavily in infrastructure, training and control systems, to limit the possibility of any such repeat and strengthen our position as a good corporate citizen.

Our understanding and successful management of potential risks, which could impact the way we run our business now and in the future, will underpin our success and we have strong governance in place to ensure we do this. As well as population growth and climate change there are a host of other risks, including infrastructure and cyber security, we need to consider.

This is a new chapter for Thames Water. Our shareholders are investing in us for the long term and our refreshed executive team is committed to making the right business decisions that will benefit our customers and stakeholders over the long term.

At Thames Water, we have been innovating for more than 400 years and new technology is providing ever greater opportunities. From being pioneers with cutting edge technology to produce energy from waste to using data intelligently to predict and minimise the impact from storms, we're innovating across the business. Make no mistake - the work we all do must leave a positive legacy for future generations.

We are in a hugely privileged position with life-long investment from our customers through their bills, and everything we do impacts them, their children, their grandchildren and beyond. We're custodians of their money so we need to be smart and disciplined about how we spend it. Our customers also play an active part in operating our water and wastewater networks, every time they turn on a tap, use a washing machine or flush the toilet. So the way we engage with them and explain our business is a continuing priority.

As we take a fresh look at the business, Brandon, our new CFO, and I have been reviewing our spending, to ensure we deliver maximum value for our customers and protect the long term financial stability of the business. Making the best decisions for our customers requires us to carefully prioritise and phase our important projects.

To deliver our priorities and a strong customer proposition, everyone in the business needs to be engaged with our vision and values and the needs of our customers. This is why I've been bringing managers from all over the company together to talk about what our values mean to them, what our customers expect and what our strategy needs to deliver. As a Thames Water family, we all need to be committed to driving changes that will really deliver for our customers.

Being open and transparent with our customers and stakeholders in a two-way dialogue about how we're running their water and wastewater company is also vital. As part of our bid to enrich customer communication and experience, we've improved our social media presence during the last year, including offering a real-time 'around the clock' service.

We also need to be clear with our customers about our progress in achieving our performance commitments. This year we have incurred a total of £18.4 million in ODI penalties and we know we can – and must – do better. We also know we cannot deliver everything we want to immediately – it will take time – but we're committed to strengthening our focus so we can provide a service our customers expect and deserve. We've started an exciting new chapter, and we look forward to engaging you in our story along the way. I look forward to working with you and thank you for your continued support,

Steve Robertson
Chief Executive Officer

As we move forward I, as the CEO of Thames Water, and my executive team have agreed that everything we do will be consistent with the following five principles, which will underpin our company strategy:

1. Listening to our customers, understanding their needs and putting those needs at the forefront of our decision making
2. Being good custodians of the environment
3. Ensuring that our assets are maintained, renewed and optimised to give the very best 'whole life outcomes'
4. Operating our business with optimal efficiency and innovating continuously
5. Being crystal clear in all our activities, both internal and external, that we are responsible for the service we give our customers and the health and wellbeing of our assets

Outcome delivery incentive performance

A snapshot of how we performed against our performance commitments which can attract a penalty or reward. We incurred a total penalty of £18.4 million and received a reward of £3.2 million for 2016/17.

Condition of our below ground water network (includes supply interruptions of more than 12 hours)

Target: Stable

Performance in 16/17: Marginal

Penalty: £4.7 million

P

Condition of our above ground water network

Target: Stable

Performance in 16/17: Stable

On target

P

Drinking water compliance

Target: 99.94%

Performance in 16/17: 99.96%

On target

P

Condition of our below ground wastewater network

Target: Stable

Performance in 16/17: Stable

On target

P

Condition of our above ground wastewater network

Target: Stable

Performance in 16/17: Stable

On target

P

Security of supply index

Target: 100

Performance in 16/17: 99

Penalty: £2.3 million

P

Leakage

Target: 630 Ml/D

Performance in 16/17: 677 Ml/D

Penalty: £8.6 million

PR

Supply interruptions lasting more than four hours

Target: 0.13

Performance in 16/17: 0.12

Reward: £3.1 million

PR

Sewer flooding other causes

Target: 1,126

Performance in 16/17: 1,214

Penalty: £0.5 million

PR

Sewage treatment works discharge compliance

Target: 100%

Performance in 16/17: 98.28%

Penalty: £2.3 million

P

Pollution incidents

Target: 340

Performance in 16/17: 315

On target

PR

Reduction in the number of properties affected by odour

Target: 793

Performance in 16/17: 1,305

Reward: £0.1 million

PR

Compliance with environmental regulations - two performance commitments

End of AMP target.

P

Resilience of sites to future extreme weather events - water and wastewater

End of AMP target.

P PR

Deephams sewage treatment works upgrade and Thames Tideway Tunnel connecting works

Performance in 16/17: Deephams sewage treatment works upgrade: Delivered

Thames Tideway Tunnel connecting works: On target

P

Site security compliance (and with notes) - two performance commitments

End of AMP target.

P

Sustainable urban drainage.

End of AMP target.

PR

Implement new online account management

Target: Limited online

Performance in 16/17: Limited online

On target

P

Properties flooding from rainfall including Counters Creek

End of AMP target.

PR

Water efficiency

End of AMP target.

P

Customer Service - service incentive mechanism score

Ofwat metric: Calculated over the AMP

Performance in 16/17: 77.3

PR

Reduce the amount of phosphorus entering rivers

End of AMP target.

PR

P **Can incur penalty**

PR **Can incur penalty or reward**

The penalties we incur will be returned to customers in the form of lower bills from 2020.

Full details of our ODI performance will be published in our Annual Performance Report, alongside an independent report by our Customer Challenge Group.

Doing more for **customers**

We've made significant improvements in our resolution of written complaints with a record 94.5% being resolved first time in 2016/17

Three key principles

To improve our customer service we are revising and focusing our approach. We have appointed Kelly Macfarlane as our new Managing Director for Customer Service and Retail to challenge the status quo and drive the step change we need. Along with Steve Spencer, our new Chief Delivery Officer, Kelly is leading the launch and delivery of a three year, company-wide plan to set the trajectory for us to provide a consistently good customer experience.

Taking on board important customer feedback, the plan embraces three key principles:

- **to make things easy for our customers;**
- **to deliver on our commitments; and**
- **to put ourselves in our customers' shoes**

To honour these principles, our customer strategy focuses on bolstering our communication channels to deliver a consistently good service and enable customers to contact us via the channel of their choice. We're also using these channels to become more proactive in our management of customer impacting incidents and events. As part of this approach, we want customers to understand what our service aspirations and promises are, so they know what they can expect from us and hold us accountable - we plan to launch our new 'commitment to customers' charter in 2017/18.

Our current performance

We've made significant improvements in our resolution of written complaints with a record 94.5% being resolved first time in 2016/17 (2015/16: 90.9%). We are also pleased there was only one complaint from our 15 million customers which needed to be investigated by the Consumer Council for Water during the year.

Our complaint levels are 44% lower than they were five years ago. In 2016/17, we achieved our second best performance to date in the number of total written complaints, with 19,384, after a record-breaking year in 2015/16. However, we recognise there's still more to do and we're confident we will continue to build on this success.

Our Service Incentive Mechanism (SIM) score, Ofwat's customer service measure, moved from 76.74 to 77.26 out of 100 in 2016/17 and our Ofwat customer satisfaction (CSAT) performance went from 4.10 to 4.12 out of five, with our highest company score of 4.18 achieved in quarter four. The CSAT score is calculated quarterly following a survey of 200 of our customers and makes up 75% of our SIM score. We are proud to be part of an industry that is so committed to service improvement and we recognise there remains much to be done to ensure we're reliably and consistently delivering our responsibilities to customers.

The investment in our restructured 'one-stop-shop' wastewater service centre in Slough, which brings customer service and operational expertise under one roof, gives us confidence in our plans going forward. Our wastewater Ofwat CSAT scores have been improving each quarter and reached 4.34 at the end of the year, bringing us up to 6th out of 10 companies in the wastewater league table.

Given the problems experienced during the winter months with burst pipes and leakages we're investing to reduce the likelihood of these incidents as well as investing company-wide in our emergency responses, to provide our customers with the support and reassurance they understandably expect.

Improving communication channels.

To make things easy for our diverse demographic of customers and stakeholders we need to give them the option to choose how they interact with us and ensure high quality communication every time. We've been making some significant improvements during the last year

Thames Water

Our customers

Face-to-face engagement

We've set up a new office and field based incident management team dedicated to helping customers in emergency situations, however large or small they may be.

Phone

Our new waste 'one-stop-shop' service centre is improving customer experience and the speed of resolution.

We're investing in new telephony solutions to improve our customer experience of speed and ease of contact and to provide more reliability and resilience in our voice channel.

Text alerts

We offer customers the option of receiving text message updates relating to supply issues or interruptions.

Mail

We're striving to ensure high quality and clear written communication for the wide range of customers we serve and who choose to contact us via email or written letter.

Our digital evolution

We've been improving our digital capability as part of the launch of our new technology alliance and 2016/17 saw some investments to improve our customer experience. Our digital capability will only increase as we utilise and develop our new digital platform and as the alliance embeds

We're investing approximately £120 million before 2020 in a multi-faceted solution to update our customer relationship management and billing capabilities. Clearly being able to accurately, reliably and easily bill our customers is critical. This big investment will underpin our ability to do this going forward and support our ambition of continually improving the ease of doing this for our customers.

We've extended our social media service to become 24/7, to introduce another 'round-the-clock' communication channel for our customers. As part of this focus on social media, we have also started to monitor customer comments online so we're able to proactively respond to concerns.

We launched our new digital platform and website to provide the foundation to enrich the look and feel as well as the content to improve our customer and stakeholder experience.

The increase in the number of registered users on our online account management system continues to gather pace, with over 600,000 of our customers now signed up.

Understanding our customers

We serve one of the most diverse cross sections of the UK, both in terms of demographics and geography, and we continually work with our customers to better understand and address their needs. Last year we surveyed thousands of customers and ran numerous workshops throughout our region on a wide range of topics including 'intergenerational fairness', 'delivering a resilient service in the face of emerging threats' and 'what it is to be a good neighbour'. We continue to involve our customers in preparations for our 2020-2025 business plan around five key commitments:

- **Delivering an effortless customer experience**
- **Delivering a safe and dependable water service**
- **Delivering a safe and dependable wastewater service**
- **Planning for the future**
- **Being a responsible company**

Being socially responsible

We understand the varying personal circumstances of our customers and we are committed to doing what we can to help. For those who can't afford to pay their bills we offer support - we helped 6,161 customers with nearly £4.5 million of debt in 2016/17 through our customer assistance fund. We also help 37,975 customers remain water debt free through our social tariffs - Water Sure and Water Sure Plus.

We work with the communities in our catchment area to do what we can to accommodate the particular needs of our customers. For those customers who require extra assistance in an emergency, for example people on dialysis, we have a priority services register. With London in our catchment, many of our customers don't have English as their first language and we've introduced a new audio translation service so we can better understand their individual requirements.

Dealing with our customers in a fair way is something which we are passionate about. Most 'bad debt' actually comes from those who choose not to pay rather than those who genuinely can't, and money is added to customer bills to account for it. We remain committed to taking measures to help ensure the vast majority who pay their bills, on time, are not penalised by those who don't pay their fair share. This includes being accurate in our billing and disciplined in collecting bills and outstanding debts. Following its launch in 2015, we're pleased to see our award-winning debt management team – underpinned by a new system and improved processes – is continuing to drive positive results, including a £14.6 million reduction in bad debt in 2016/17. A reduction in refusal to pay means we have more money to invest in our business for the benefit of all our customers.

We helped 6,161 customers with nearly £4.5 million of debt through our customer assistance fund in 2016/17 and we also help 37,975 customers through our social tariffs

We set ourselves 55 performance commitments for the 2015-2020 regulatory period, which were designed to deliver what is important to our customers in the most effective way. You can find further information about our performance against our commitments in our Annual Performance Report, which will be published by 15 July 2017.

On the subject of fairness, we've increased our resources to prevent people illegally connecting to our network, which could also affect water quality. Following the investigations we carried out and completed in 2016/17 we expect to save 23.5 million litres of 'stolen' water over the next ten years, which would otherwise have been attributed to leakage.

Engaging the community

We continue to be an active member of the community in which we operate. In 2016/17, we met with over 20,000 school children as part of our extensive education programme promoting campaigns such as 'Bin it - don't block it' to encourage good habits from childhood. We also do what we can to promote enjoyment of our sites – after vandalism at our Nunhead reservoir in 2016, we worked with local residents to arrange special open days to enable them to continue enjoying this much-loved South London site.

Engaging our stakeholders

We run an extensive stakeholder engagement programme to build strong relationships and we play an active role in the public debate about important issues affecting the water industry. We regularly engage with political representatives and stakeholders so they can find out more about what we do, and raise concerns on behalf of the people they represent. We ensure their views are considered in our plans and seek their support around smart metering and drainage strategies, for example.

Our independent Customer Challenge Group, made up of customer representatives and stakeholders, has continued to challenge and advise us on the development of our business plan and how it can better reflect the needs of our customers. They will publish an independent report about how we report our performance alongside our Annual Performance Report.

We met with over 20,000 school children as part of our extensive education programme in 2016/17

Innovating for life

'Here for you - innovating for life in a changing environment' is our vision. We're implementing new technology to drive efficiencies, improve health and safety, reduce costs and ensure sustainability. Innovation isn't just about new technology - it's about doing things in new ways for a better outcome and we're innovating across the business. Here we highlight just some of the ways we're innovating to drive improvements:

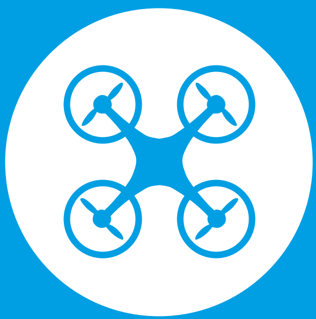
Storm chasing

We use the latest data and analytics, monitor weather reports and river and ground water levels to help deliver a proactive and preventative response to adverse weather before it happens to mitigate the risk of it impacting our customers.

Part of our response is to deploy equipment to protect customers before they flood and dispatch tanker crews to predicted flood locations to proactively manage flooding during storm events.

Designer bugs

To improve the efficiency of the wastewater treatment process, we're starting to use 'designer' bacteria for the wastewater treatment process. The use of these bacteria will help us reduce the space we need to treat wastewater and the energy required to power the operations. With a smaller processing footprint, there is less pressure to build new or larger treatment works to accommodate the growing population.



Eye in the sky

We're reducing health and safety risks and saving money by using drones to inspect cranes and other equipment which reduces the number of inspections needed to be performed by our employees.

Algae filters

Algal blooms can severely impact water production and in some cases reduce water treatment capabilities by a third. In an attempt to combat this problem we're trialling new algae filters at reservoirs.

Deephams upgrade

We are investing over £250 million to upgrade our Deephams sewage treatment works to increase capacity and reduce odour.

Investing in infrastructure

Investing in our infrastructure is critical to enable us to reliably serve our customers. With thousands of ageing pipes across our network, improvement can only be made with a regular and targeted programme of investments. We've invested over £12 billion in the last 12 years in our business.

Strengthening our network

The landmark Thames Tideway Tunnel construction project, which is being delivered by an independent company – Bazalgette Tunnel Limited ("BTL"), is progressing well and will transform the health of London's rivers. After buying the land along the tunnel's path and preparing for the project, our responsibility now is for the connections to the tunnel, which we are delivering ahead of schedule. By the end of this regulatory period (2015-2020), we expect to have spent £1.4 billion in total on our share of the works. From 1 April 2016 we started recognising revenue on the arrangement with BTL as agreed with Ofwat. As cash is collected, it is passed on to BTL to fund the construction of the tunnel. Our first super sewer, the Lee Tunnel was commissioned during the previous financial year 2015/16, and was awarded the Greatest Contribution to London award by the Institution of Civil Engineers in 2016/17.

As well as ambitious projects to ready London for the future, with our alliance partners we're also investing heavily in equally important schemes in our other regions to help local communities – the £30 million Axford pipeline near Swindon, the £24 million Angelinos pipeline near Abingdon and a £8.4 million sewer in Didcot to name just a few.

As enduring and committed custodians of the natural environment we've invested £4.4 million in screens to protect endangered eels from entering our network and reduce the likelihood of pollutions, as well as £ 6.7 million on a major sustainable urban drainage project for the Nine Elms development in Battersea in 2016/17.

Water

An exceptional product

We deliver 2.6 billion litres of clean drinking water direct to our customers' homes, 365 days a year for an average of just over £1 a day and our water quality achieved 99.96% compliance for 2016. Performing 475,000 tests a year on water samples, we ensure our water quality remains among the highest in the world.

Improving water network resilience

We've invested heavily in our ageing water infrastructure in recent years, and have committed to spending an extra £97 million during the next three years to improve the resilience of our largest water mains for the benefit of our customers, the environment and future generations. Renewing our water network, which could stretch three quarters of the way around the world, is a mammoth task.

Although we missed our leakage target for 2016/17, we increased our investment in leakage reduction during the year and we're trialling a raft of new technologies to improve our performance and reduce our susceptibility to extreme weather. Although the major bursts are a visible reminder that some of our pipes are fragile, most leakage actually comes from leaks below the ground that we can't see and are more difficult to locate and repair.

Reducing supply interruptions continues to be a challenging commitment to meet, but we have improved our performance since 2015/16. 1 in 7 of our water complaints relate to an interruption in the water supply, so we know it's something we need to get right. We have performed well in minimising the number of interruptions lasting for more than four hours (0.12 hours per property served) so we have beaten our performance commitment and achieved a reward of £3.1 million in 2016/17. We have also minimised the occurrence of low water pressure experienced by our customers. Disappointingly, we have missed our 1,354 properties target for supply interruptions of over 12 hours. As a result, the health ('asset

We've appointed Sarah McMath as the new Managing Director for Water.

health') of our underground network, including pipes, will be categorised as 'marginal' and we will incur a penalty of £4.7 million. The health of our above ground assets remains 'stable'. We performed well against our security of supply index ("SOSI") commitment which represents our ability to supply water in extreme conditions, with 99, however, as the target is 100, we will incur a penalty of £2.3 million for 2016/17.

As this year reminded us, mains replacements are vital to ensure our network is resilient now and in the future. Despite replacing over 2,800 km of our pipes since 2004, 25% of our pipes are still over 100 years old, so there's much more to do and we must do it in ways which are efficient, affordable and minimise disruption to our customers' daily lives. We plan to invest in the maintenance and renewal of 650 km of mains during this regulatory period and we've replaced and repaired 103 km of pipes this year. We've just completed a £4.4 million refurbishment of a 1.6 km pipe in Swiss Cottage by inserting a robust plastic pipe inside the existing main to reduce disruption. We're also using this technique to re-line pipes in Leigham Vale and Islington, which flooded properties in December 2016. With two thirds of our network sitting under London, a densely populated and developed area, we need to strike the right balance between creating a resilient network and keeping disruption to a minimum for our customers. Large scale mains replacements are disruptive, can impact water supplies and increase customer bills.

Wastewater

Our customers rely on us to remove wastewater safely from their homes, treat it and return clean water back to the environment.

Pollutions and treatment works compliance

We saw 315 pollution incidents in 2016, which, although up on last year, is a 42% decrease since 2013, when we experienced significant problems. We were fined for some of these historical pollutions in March 2017 and other historical incidents are still being investigated. We've continued to invest in our network with new pump monitoring technology and the installation of new inlet screens to reduce the likelihood of problems. We've also improved our site monitoring technology so we can respond quickly when problems do occur.

We must pass every discharge quality test to meet our sewage treatment works compliance commitment of 100%. We failed six in 2016/17, so we incurred an ODI penalty of £2.3 million. Although some of the problems were the result of human error, extreme wet weather and unconsented discharge of effluent into our sewers by customers also contributed to us missing our target.

Keeping our waste network flowing

We saw an improvement in our sewer flooding performance with a 13% reduction in sewer flooding incidents and a 4.6% reduction in sewer blockages compared to the previous year. Despite the reduction in sewer flooding incidents, the number of incidents still exceeded the penalty threshold and we incurred a penalty of £0.5 million (2015/16: £11.7 million). Knowing prevention is better than cure we've continued to be proactive in our approach to sewer cleaning and in promoting what our customers can do too.

Our extensive customer education programme has continued to gather pace. In 2016/17 we spent £1.4 million on targeted 'Bin it – don't block it' campaigns across our region and, following a pilot study of Oxford restaurants in 2015, we launched a new project in 2016/17 to educate fast food establishments across the region about cooking fat disposal. We also formed a successful partnership with the Marine Conservation Society to highlight the problems caused by wet wipes, which has captured the media's attention.

Reducing odour considerately

As the population grows and housing developments get closer to our sewage treatment works, we've made headway in recent years in reducing odour for those local communities. In 2016/17 we made further improvements at two sewage treatment works in Aldershot and Esher. This work has led to a reduction of 1,305 properties being affected by odour as assessed through odour modelling. Our major upgrade of Deephams sewage treatment works, involving 500 construction workers, will take this one step further, with an expected reduction in a further 3,850 properties being affected by odour.

The £250 million plus upgrade at Deephams will be completed in 2018 and will increase the capacity of this major treatment works from 887,000 to just less than 990,000 people. In recognition for the way we limited local disruption, the scheme won two 'National Bronze awards' as part of the Considerate Constructors Scheme.

Bin it - don't block it literature, which included a free fat trap, was mailed to 223,000 customers last year.

Custodians of the **environment**

We recognise that we have a huge responsibility to protect our natural environment and to transition our business towards using more renewable energy. We are committed to taking major precautionary measures to ensure the safety of local ecosystems while also helping us meet our pollution targets.

The provision of essential services is energy intensive. It costs over £50 million a year to power our water treatment process alone and this is one of our largest single operational costs. Our customers provide us with valuable fuel every day, in the form of sewage, and through the use of innovative new technology, we're making huge progress in our bid to realise its full potential to reduce our energy costs. Alongside this, we're doing what we can to drive energy efficiency across the business including:

- Finding the most energy efficient route to deliver water to our customers
- Committing £3.6 million of investment in energy efficient pumping systems.

Europe's largest floating solar panel array on our QE2 reservoir.

Record-breaking energy production

We generated a record 267GWh of electricity from sewage in 2016/17, enough to power 86,000 homes a year, and this will only increase in future years. Combining this with the 6.4GWh we generated and used from other sources, one fifth of our electricity came from renewable sources, including our own generation, during 2016/17. This saved us £24 million off our annual energy bill.

We're also exploring other innovative ways to produce energy close to our sites, similar to last year's construction of Europe's largest floating solar panel array on our Queen Elizabeth II reservoir, which part powers Hampton water treatment works. Where we're not able to produce our own green energy, we've been buying in renewable electricity following an agreement with Haven Power.

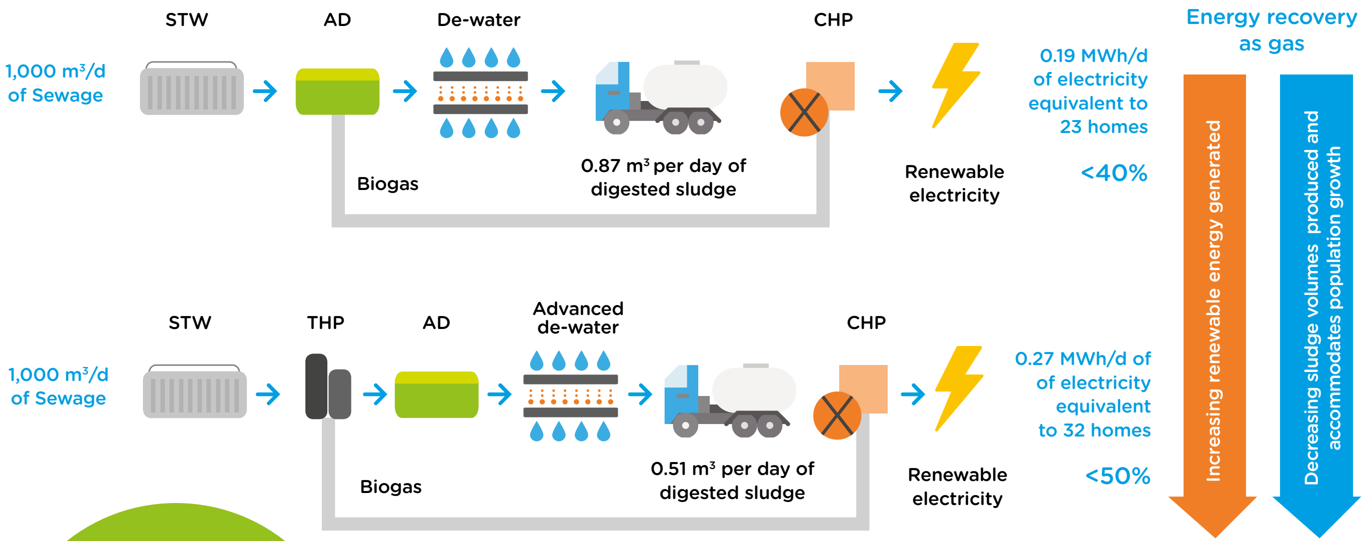
To drive costs down and help us become a more environmentally sustainable organisation, we aim to source 33% of our energy from embedded renewables by 2020.

In 2016/17 our greenhouse gas emissions fell by around one third to 507.4 kTCO2e/Ml (kilotons of carbon dioxide equivalent). We reduced our water greenhouse gas emissions intensity from 273.0 kgCO2e/Ml (kilograms of carbon dioxide equivalent per megalitre) by almost one half to 141.3 kgCO2e/Ml. We reduced our wastewater greenhouse gas emissions intensity from 303.1 kgCO2e/Ml by one quarter to 225.4 kgCO2e/Ml.

We're pushing new boundaries and ramping up energy production due to CHP and THP technology working efficiently. Mogden, for example, had new CHP engines in 2016/17.

Energy recovery from sewage sludge

STW - Sewage treatment works
THP - Thermal hydrolysis process
AD - Anaerobic digestion
CHP - Combined heat and power



Use of the thermal hydrolysis process and advanced de-watering increases the amount of electricity we can produce.

Protecting water resources

We continue to drive programmes to protect water resources for the future and we're currently working on our next Water Resources Management Plan. It is due to be submitted to the Department for Environment, Food and Rural Affairs ("DEFRA") later in 2017 and published in draft early in 2018 for consultation. Every five years the Secretary of State requires water companies to submit 25 year plans to develop an efficient and economic water supply system which will maintain security of supply for customers. With climate change and population growth forecast to result in a substantial supply and demand imbalance in our area, some areas will require significant capital investment, such as mains replacement, wastewater recycling, new storage reservoirs and inter-regional transmission pipelines. In London, water demand is forecast to outstrip supply by approximately 150 million litres of water per day by 2025, and without appropriate action the situation is only going to get worse. As well as strong governance to ensure a 'whole of life' and cost efficient investment plan, we have been engaging with external shareholders for the last three years to help inform our plans.

We have also continued to install meters at our customers' homes and on our network, including 146,000 smart meters, to increase customers' awareness of their water usage and help us detect leaks.

Helping households, business sites, schools, local authorities and housing associations become more 'water smart', our hugely successful water efficiency programme is the largest in the industry, saving over 11 million litres of water each day. Awarded the 'Water Resource Management Award' by the Water Industry Achievement Awards, our Smarter Home Visits initiative installed 200,000 water efficiency devices in 60,000 households, helping our customers reduce their metered water and energy bills. We're leading by example – our water saving toilets and taps at our head office in Reading have helped the entire building use 50% less water – winning the 'Sustainable Water Management Award' by the Institution of Civil Engineers.

A safe work environment

The safety and health of our employees and customers is of paramount importance and in 2016/17 we reached two major health and safety milestones. We saw our first ever day when no employees or contractors across our entire business were off work with a work related injury. Also, twice during the year we clocked up 2,000,000 consecutive hours worked without a lost time injury. Over the year we have seen a 17% reduction in the Lost Time Injury Frequency Rate (LTIFR) and a 21% drop in RIDDOR (serious) Injury Frequency Rate.

As part of our health and well-being strategy, we have been encouraging employees to look after their physical and mental health. Benefits such as confidential personal medical assessments for all, education courses and other well-being initiatives collectively led to a 30% decrease in work-related mental health referrals during the year.

In 2016/17 we saw a further 46% increase in the number of hazards being reported by our employees, which prevents incidents before they occur - our health and safety stand-down meetings have also been effective in highlighting potential areas of concern. To help increase the number of safety inspections and provide a 'fresh pair of eyes', senior managers from across the business have also been conducting health and safety inspections. Over 800 inspections were carried out in 2016/17 with the number of management inspections increasing by 57%.

We have continued to increase the competency of our workforce through new and innovative training such as our industry leading water safety course. There was an 11% increase in health and safety training days delivered to our employees during 2016/17.

Giving back

We have a culture of giving back to the community and environment we serve through our 'time to give' programme. From litter picks, to helping in schools and decorating furniture to sell for charity, employees spent 6,632 hours taking part in 962 volunteering opportunities for local causes in 2016/17.

We also help those further afield. After raising £2 million for Bangladesh through numerous projects, we have committed to raising £2 million to change the lives of people in two villages in Malawi, who don't currently have running water. We raised £350,147, with a further £93,000 of income pledged in 2016/17 for our WaterAid 'Thames loves Malawi' campaign, with some projects, including our summer raft race on the River Thames, raising significant sums.

Natural environment

As part of our operations we work alongside a lot of different species of wildlife and we are fully committed to protecting local ecosystems. We've invested £4.4 million in screens to protect endangered eels entering our network alongside £740,000 in other biodiversity projects. They include creating an osprey tower at Pinkhill Reservoir, putting up barn owl boxes at Beckton sewage treatment works and creating mixed species hedgerows at various sites across our region.

We have committed to raising £2 million to change the lives of people in two villages in Malawi, who don't currently have running water.

Caring for our people

Without our people Thames Water couldn't exist. We need the best people in our business to enable us to deliver our commitments to our customers, stakeholders and the environment.

Our people strategy sets out how we will support our internal investors, the Thames Water family, on this journey by building a working environment and culture in which we inspire them to live our values and do their very best for every one of our customers, every day.

Engagement

Having an engaged workforce who understand what is happening in the business and their role in our success is really important to us and we ensure that we do this on a regular basis whether through team meetings or through our internal social media channels.

Every year our employees are invited to complete our 'hear for you' survey so we can measure our progress in a range of areas.

Diversity and inclusion

It's important to us that all our employees can be themselves at work and are able to give their best. Being diverse in our approach isn't about ticking boxes - it's about hiring the right people for the job regardless of their background and we are working hard to become a more inclusive organisation. In recent months, the percentage of women in our executive team has increased from 10% to 30%, which is more in line with the percentage of women throughout the company – 32% of employees and 33% of managers are women. We have extended our internal diversity networks, introduced unconscious bias training, updated our facilities, and extended our recruitment pipelines and practices to attract a wider audience, including a returner's to work programme. We continue to be sponsors of the Pride events across our region.

We are committed to fulfilling our obligations under the Equality Act 2010 and have policies and procedures in place to ensure both applicants and employees have equality of opportunity, are treated fairly and have a safe workplace, free from discrimination, bullying, harassment and victimisation. We seek to promote a culture of honesty and integrity in everything we do and will not tolerate acts of fraud, dishonesty, bribery, corruption or theft of assets or data. Our code of conduct, alongside our Honest and Ethical Behaviour policy, expresses our approach to business activities and how we work, providing a clear, ethical and legal framework for our employees, customers and stakeholders. It covers a wide range of human rights issues including discrimination, working conditions, modern slavery and human trafficking and equal opportunities. We have a confidential 24-hour whistleblowing helpline available where any employees can ask questions or raise concerns. Our contractors and alliance partners have agreed to follow the provisions of this code. You can find our latest Modern Slavery Act statement, and the steps we are taking, on our website, alongside our Honest and Ethical Behaviour policy.

Reward and recognition

We celebrate success and when our people go the extra mile to demonstrate they are living our values. This year's Spotlight Awards attracted over 900 nominations which highlighted some great achievements by our people. To promote a healthy work life balance we also offer initiatives such as 'Benefits on Tap', which offers high street discounts, a cycle to work scheme and a free health assessment for every employee.

Talent pipeline

We need to ensure that we continue to attract talent to our organisation and we have great apprentice and graduate schemes that support our longer term resourcing needs. In 2016/17 we brought another 32 apprentices and 38 graduates into the Thames Water family. We also work closely with schools and colleges in our region to develop an early passion for science, technology, engineering and mathematics ("STEM") subjects and careers with us. We are a key sponsor of the London Design and Engineering University Technical College, a college dedicated to educating engineers of the future and our HR Director, Janet Burr, is a Governor. Linking across our pipeline our graduates share their experiences and mentor students at the college.

1 Employee awards attracted over 900 nominations in 2016/17

2 In the last few months the number of women in our executive team has increased from one to three

3 Over 24,000 days of training completed by employees in 2016/17

4 12% of our employees have worked at Thames Water for more than 25 years

CFO’s review Managing our finances

To support the efficient delivery of our long-term investment programme, which has exceeded £12 billion over the last 12 years, we remain highly focused on the strength of our financial position.

Brandon Rennet
Chief Financial Officer

Our Class A debt is rated as A3 (stable) with Moody’s and A- (negative outlook) with Standard & Poor’s (“S&P”), and our Class B debt is rated as Baa3 (stable) with Moody’s and BBB (negative outlook) with S&P. We have successfully issued £568.1 million of new debt in the year to 31 March 2017, and a further £550.0 million in April 2017. Our weighted average cost of debt is 4.86%, and the average maturity of our debt book is 18 years.

Underlying revenue for the financial year ended 31 March 2017 was generally in line with the previous year at £2,027.1 million (2015/16: £2,039.5 million), and underlying operating cash flows (note 28) were reduced in comparison with the previous financial year at £1,046.0 million (2015/16: £1,157.9 million). Underlying operating profit fell year-on-year to £605.4 million (2015/16: £742.2 million), primarily due to an increase in operating expenses of £96.0 million, driven by higher depreciation charges and transformation costs, and a £44.4 million reduction in profits on the sale of properties. Underlying profit before taxation is significantly lower year-on-year at £38.1 million (2015/16: £511.2 million), with the majority of this reduction being attributable to the £205.5 million net loss on financial instruments and the £104.6 million increase in the net finance expense, driven by lower capitalisation of interest and higher RPI accretion on debt. We continue to invest more than any other water and wastewater company in England and Wales to improve our vast network and create a sustainable service for the benefit of our customers, stakeholders and the environment. In order to achieve this, our focus is on efficiency and disciplined delivery.

Relationship with Bazalgette Tunnel Limited (“BTL”)

From 1 April 2016 we started recognising revenue on the arrangement with BTL, as agreed with Ofwat. As cash is collected, it is passed on to BTL to fund the construction of the Thames Tideway Tunnel. We have presented all amounts associated with this arrangement separately within these financial statements. This non-appointed revenue is excluded from our key performance indicators, which is consistent with our banking covenants. The cash collected and paid over to BTL during the period of construction represents a prepayment for the use of the tunnel once the project is complete. As a result of this unique arrangement and the resultant accounting treatment, our revenues and profits will increase during the period of construction, but such profits will not be supported by cash – instead an asset is created on the balance sheet. Once construction is complete, BTL will lease the tunnel to us under a finance lease agreement.

Revenue

As a result of our arrangement with BTL, our total revenue has increased by £33.0 million compared to 2015/16. Excluding the effect of this revenue, underlying revenue for the year has decreased compared to the previous year by 0.7% to £2,027.1 million. As a

Key financial performance indicators

	Underlying 2017	BTL 2017	Total 2017	Underlying 2016	BTL 2016	Total 2016
Revenue (£m)	2,027.1	33.0	2,060.1	2,039.5	-	2,039.5
Operating expenses (£m)	(1,515.4)	-	(1,515.4)	(1,419.4)	-	(1,419.4)
Operating profit (£m)	605.4	33.0	638.4	742.2	-	742.2
Net finance expense (£m)	(361.8)	-	(361.8)	(257.2)	-	(257.2)
Net (losses)/gains on financial instruments (£m)	(205.5)	-	(205.5)	26.2	-	26.2
Profit before tax (£m)	38.1	33.0	71.1	511.2	-	511.2
Profit after tax (£m)	51.1	26.4	77.5	566.4	-	566.4
Capital expenditure excluding intangibles (£m)	1,115.3	n/a	1,115.3	1,198.7	-	1,198.7
Net debt (£m) (statutory basis)	10,749.4	-	10,749.4	10,152.9	-	10,152.9
Dividends paid (£m)*	157.0	-	157.0	82.4	n/a	82.4
Interest cover**	1.7	n/a	n/a	1.8	n/a	n/a
Gearing (%)***	81.5	n/a	n/a	81.0	n/a	n/a
Credit rating****	n/a	n/a	Baa1 stable	n/a	n/a	Baa1 stable

* Includes £100.0 million (2016: £nil) paid to external shareholders
** Based on interest payable – excludes accretion on RPI debt
*** Ratio of covenant net debt to Regulatory Capital Value ("RCV")
**** Representing the consolidated Corporate Family Rating assigned by Moody's

regulated business, our revenue is not subject to significant variances year-on-year, but is affected by variables such as consumption, inflation and population growth. Our underlying revenue is shown after a deduction of £45.9 million (2015/16: £37.7 million), relating to amounts billed in 2016/17 and considered to be irrecoverable (bad debt) from our customers.

Bad debt

Our focus on reducing bad debt, particularly the debt which arises from customers who are unwilling (as opposed to unable) to pay, has delivered a year-on-year reduction in total bad debt cost of £14.6 million to £50.4 million (2015/16: £65.0 million). Of the total cost of £50.4 million, £46.5 million (including £0.6 million in respect of BTL revenue) (2015/16: £37.7 million) is shown as a deduction to revenue and £3.9 million (2015/16: £27.3 million) within operating expenses.

Operating expenses

Our net operating costs increased by £96.0 million (6.8%) to £1,515.4 million from 2015/16. £40.6 million of the increase is attributable to higher depreciation and amortisation charges on our operational assets. The remainder of the increase is driven by one-off transition costs associated with our technology and transformation alliance, additional investment in customer service and higher spend levels targeted at a number of key performance commitments.

Net finance expense (borrowing costs)

In order to ensure our investment programme is affordable for customers, we spread the cost of investment in these long-term assets by borrowing through public and private debt capital markets or through loans from relationship banks. We are required to pay interest on any amounts we borrow. Our strong investment grade credit ratings mean that we continue to be able to obtain financing at favourable interest rates. Our net finance expense consists of:

	2017 (£m)	2016 (£m)
Finance income	94.5	86.1
Gross finance expense	(532.6)	(457.7)
Capitalised borrowing costs	76.3	114.4
Finance expense	(456.3)	(343.3)
Net finance expense	(361.8)	(257.2)

Our gross finance expense has increased by £74.9 million from the prior year primarily due to higher RPI accretion costs. Some of our borrowing costs are incurred in relation to the delivery of certain major capital projects. As a result, we are able to capitalise these borrowing costs, which reduces the finance expenses recognised in the income statement. The reduction in borrowing costs eligible for capitalisation this year was primarily driven by the commissioning of the Lee Tunnel at the end of 2015/16.

Fair value of derivatives

As we borrow money from a variety of external sources, we are exposed to fluctuations in interest and inflation rates as well as foreign exchange rates. Our revenue, operational expenditure and capital expenditure are also exposed to fluctuations in inflation rates. We manage these exposures by entering into certain derivative contracts. We have approximately £4.1 billion of derivative financial instruments (face value), which include £1.35 billion of forward starting interest rate swaps that have fixed a significant element of the cost of debt we expect to borrow between 2017 and 2020. A net loss of £205.5 million on financial instruments has been recognised in the income statement during the year (2015/16: gain of £26.2 million), primarily driven by higher forecast RPI (inflation) rates.

Profit before tax

A summary of the movement in our profit before tax is summarised below:

	31 March 2017 £m
Profit before tax for the year ended 31 March 2016	511.2
Decrease in underlying revenue	(12.4)
Net BTL revenue	33.0
Increase in operating expenses	(96.0)
Decrease in profit on sale of property, plant and equipment	(44.4)
Increase in other operating income	16.0
Increase in net interest payable	(104.6)
Movement in (losses)/gains on financial instruments	(231.7)
Profit before tax for the year ended 31 March 2017	71.1

Capital expenditure

During the year, we invested a total of £1,115.3 million (2016: £1,198.7 million) in our network and infrastructure. This spend included the following key projects:

	31 March 2017 £m
Thames Tideway Tunnel – development and interface works	37.1
Deephams sewage treatment works upgrade	65.0
Our new customer relationship management and billing ("CRMB") system*	38.2

*including spend on intangible assets

Spend on the Thames Tideway Tunnel is limited to the cost of work required to connect our network to the tunnel and land acquisition costs. Capital spend relating to the Thames Tideway Tunnel reduced by £91.3 million compared to 2015/16.

Net debt and cash flow

Net debt (the total of external borrowings less cash at bank and in hand) has increased by £596.5 million to £10,749.4 million, as we continue to fund our capital investment programme. In order to fund ourselves efficiently we have significantly reduced our cash and short-term investment balances to £57.5 million (2016: £812.0 million). Net debt includes accrued interest on debt and excludes derivative accretion and foreign exchange net debt. In the prior year financial statements, we disclosed net debt of £10,154.2 million. This net debt excluded £197.3 million of accrued interest on debt and included £198.6 million relating solely to accretion on index-linked swaps and the effect of movement in foreign exchange rate on one cross currency swap held by TWUL. After including interest on debt and excluding derivative accretion and foreign exchange net debt as at 31 March 2016 would have been £10,152.9 million.

Gearing and interest cover

As we use external funding, we have to operate within certain financial parameters (covenants) that are set by the institutions we borrow from. Our two major covenants are gearing (the ratio of covenant net debt to Regulatory Capital Value ("RCV")) and interest cover (the ratio of our profits to interest payable).

Our gearing ratio of 81.5% (2016: 81.0%) was comfortably below the mandated maximum of 85% and our interest cover (the ratio of our profits to interest payable), at 1.7x, was well above the minimum level mandated of 1.1x.

Regulatory Capital Value ("RCV")

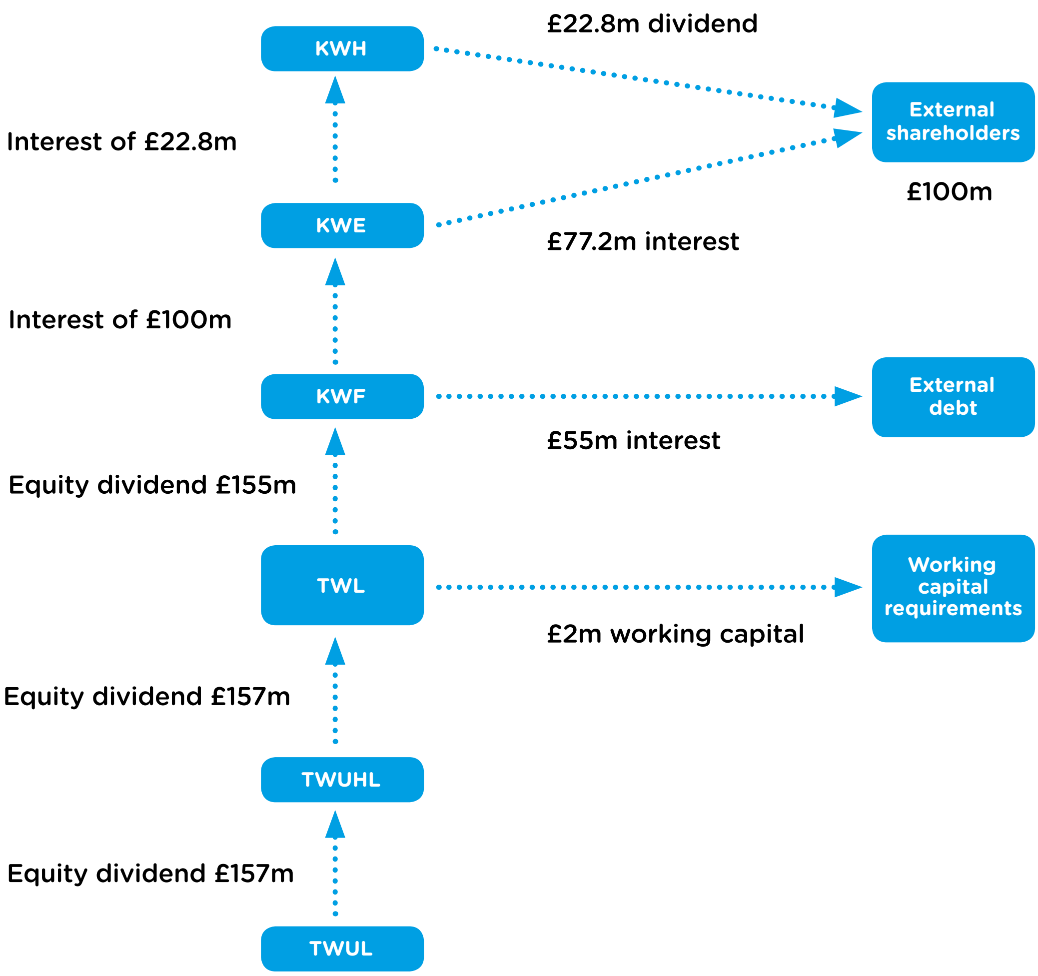
We finance this investment through a combination of cash flows generated by, and retained in, the business and borrowing (debt). At 31 March 2017, our RCV was £12.9 billion (2016: £12.3 billion). Our RCV reflects the investment we've made in delivering water and wastewater services to our customers.

Dividends and distributions to external shareholders

Our shareholders provide another source of funding to enable us to invest in our network and they expect a return on their investment, which we pay in the form of dividends. The level of dividends is influenced by operational and financial performance.

During the year, we paid dividends of £157.0 million (2016: £82.4 million) to our parent company Thames Water Utilities Holdings Limited ("TWUHL"). £57.0 million of dividends paid in respect of the current year were made to other companies within the Kemble Water Holdings Ltd Group ("the Group"), to service their own debt obligations and working capital requirements (2016: £82.4 million). External shareholders have received distributions relating to this financial year totalling £100.0 million (2016: £nil).

The following diagram summarises how the dividends the Company paid during 2016/17 have been utilised and distributed by the Group:



Credit rating

In accordance with our Instrument of Appointment, we continue to maintain a strong investment grade credit rating, as assigned by external ratings agencies Moody’s and S&P. The assessment by these two agencies provides an independent view of our performance and future prospects.

In April 2017, Moody’s reaffirmed our Baa1 Corporate Family Rating (“CFR”) with a stable outlook. This supports specific ratings of A3 and Baa3 for our Class A and Class B debt respectively. Moody’s cited our low business risk profile and the relatively stable and predictable cash flows generated under a well-established and transparent regulatory framework as drivers which support the rating, as well as the creditor protections incorporated within the financing structure. Moody’s do, however, recognise that these strengths are somewhat offset by the relatively high gearing we employ.

In their most recent credit opinion in September 2016, S&P assigned ratings of A- (Class A) and BBB (Class B) and maintained a negative outlook. Whilst S&P recognised positive developments in operating performance over the previous two years, S&P assessed these improvements as lagging behind our peers and retained a negative outlook reflecting their assessment of the limited headroom at current leverage levels. We continue to focus on improving operational performance and delivering further improvements over the course of the remainder of the regulatory period.

Pensions

We operate three pension schemes for our employees - two defined benefit schemes and one defined contribution scheme.
The latest actuarial valuations for the two defined benefit schemes, dated March 2013, have been updated to 31 March 2017 on our behalf by independent and professionally qualified consulting actuaries, PricewaterhouseCoopers LLP. The valuation shows that overall, the net pension deficit has increased by £119.8 million to £379.8 million (2016: £260.0 million). This increase has been primarily caused by use of a lower discount rate in the actuarial calculation, driven by lower yields on AA-rated corporate bonds, which is consistent with other companies that operate a defined benefit pension scheme.

There is a recovery plan in place (based on the latest actuarial valuation dated March 2013), as agreed between our Directors and the scheme trustees. The March 2013 actuarial valuation and agreed recovery plan has committed the Company to making additional contributions to each scheme annually. These additional amounts, calculated by a qualified and independent actuary working on behalf of the scheme trustees, have averaged £20 million per year, since 2013, across the two schemes.

The updated triennial valuation, dated 31 March 2016, is expected to be finalised by the scheme actuary by the end of June 2017. As part of the March 2016 actuarial valuation, we are engaging with the Trustees to agree an updated recovery plan. The Company works closely with the scheme trustees throughout this process and remain committed to maintaining a strong and viable pension scheme for members.

During 2016/17, we contributed £6.8 million (2016: £5.2 million) to the defined contribution scheme.

Taxation

In 2016/17 we paid around £170 million in taxes, including central and local government business rates, PAYE and National Insurance. As in recent years we did not pay any corporation tax to HMRC during 2016/17. As a result of the Government’s capital allowances scheme, to encourage investment in UK infrastructure, our corporation tax payments are delayed while we invest so heavily in our business. If this scheme was not in place, average combined customer bills would be higher.

We are committed to being transparent about our finances. We published the latest edition of ‘Our finances explained’ on our website in October 2016.

On 6 September 2016 Parliament enacted a reduction in the future corporation tax rate from 18% to 17% which will be effective from 1 April 2020. This has reduced our deferred tax liabilities by £51.6 million, of which £59.8 million is included in the income statement. This represents a reduction in the level of corporation tax payable in future years and therefore does not constitute a refund from HMRC. Ultimately this will benefit our customers in the form of lower bills in future years.

Our aim is to be clear and transparent about our approach to tax and our tax profile and this year we have incorporated the Financial Reporting Council's recommendations on tax disclosures. We will be publishing our tax strategy on our website at the end of June. In summary our tax strategy has five key principles:

- We will comply with all tax legislation requirements at all times, both within the letter and spirit of the law;
- We will not use tax avoidance schemes or aggressive tax planning;
- We will engage fully and transparently with HMRC and other Governmental bodies, and seek to resolve disputes in a co-operative manner;
- We will adopt a conservative approach to tax risk management and apply a strong tax governance framework; and
- We will accept only a low level of risk in relation to taxation.

Capital and financial risk management policies and objectives

The Company's operations expose it to a variety of capital and financial risks. The Group's treasury operations are managed centrally by a specialist team. The team operates with delegated authority of, and under policies approved by, the Group's Board of Directors. Risks are therefore managed on a Group wide basis.

The operation of the treasury function is governed by specific policies and procedures that set out guidelines for the management of liquidity, credit and market risks associated with the financing activities of the Group. The treasury policy and procedures are incorporated within the financial control procedures of the Group.

Capital risk management

Capital risk primarily relates to whether the Company is adequately capitalised and financially solvent. The key objectives of the funding strategy are to maintain customer bills at a level which is both affordable and sustainable, retain the Company's investment grade credit rating and provide liquidity sufficient to fund ongoing obligations.

The Board reviews the Company's exposure to these risks and actively oversees the treasury activities, reviewing the treasury policy and approving the treasury strategy and funding plan.

The capital structure of the Company consists of net debt and equity as disclosed in note 19. The Company's net debt is comprised of cash and cash equivalents, short-term investments, bank loans and intercompany loans from subsidiary undertakings that issue secured bonds.

The Company is part of a Whole Business Securitisation ("WBS") Group of companies. The Company guarantees the funding activity of subsidiary companies established to raise debt finance in international capital markets under the terms of the Whole Business Securitisation. The Securitisation Group is required to comply with certain financial and non-financial covenants. The financial covenants include an interest cover ratio and a net debt to RCV ratio. The Securitisation Group complied with these ratios throughout the financial year. Further details of these covenants are shown on page 37.

The Group's funding policy is to maintain a broad portfolio of debt (diversified by source and maturity in order to protect the company profits against risks arising from adverse movements in interest rates and currency exposure) and to maintain sufficient liquidity to fund the operations of the business for a minimum of a 15-month forward period on an on-going basis. Derivative financial instruments are used, where appropriate, to manage interest rate risk, inflation risk and foreign exchange risk. No open or speculative positions are taken.

The securitisation includes covenant obligations to manage the maturity profile of debt arrangements; the nominal value of debt maturing within any 24 month period cannot exceed 20% of RCV and maturing debt within a single regulatory period cannot exceed 40% of RCV.

Financial risk management

(i) Market risk

Market risk is the risk that changes in market variables, such as inflation, foreign currency rates and interest rates, will affect the Company's income or the value of its holdings of financial instruments. Financial instruments entered into by the Company include RPI linked bonds, loans and swaps. These instruments are exposed to movements in the UK RPI index. The Company is a regulated water company with RPI linked revenues. Therefore the Company's index linked borrowings form a partial economic hedge as the assets and liabilities partially offset.

The Company's foreign currency risk exposure results from debt raised in currencies other than Sterling. The Company uses cross currency swaps to hedge the foreign currency exposure of debt issued in a foreign currency. All hedges are undertaken for commercial reasons with the objective of minimising the impact of exchange rate fluctuations. The Company has no material unhedged monetary assets and liabilities denominated in a currency different from the local currency of the Company. Further disclosures regarding financial instruments can be found in note 19. Interest rate risk arises on interest-bearing financial instruments. Fixed rate borrowings are exposed to a risk of change in their fair value due to changes in interest rates. Floating rate borrowings are exposed to a risk of change in interest cash flows due to changes in interest rates.

The Company uses interest rate swaps which economically hedge future cash flows to protect against interest rate movements.

The securitisation includes covenant obligations to manage the interest rates risk of the Securitisation Group within specific parameters. At least 85% of total outstanding debt liabilities in the current regulatory period and at least 75% in the next period should be in either index-linked or fixed rate form.

In mid-2014 the Company executed £2.25 billion of forward-starting pay fixed/receive floating interest rate swaps of a five to seven year maturity with various financial institutions to fix the future interest costs of an element of the anticipated new debt issuance in this regulatory period. This protects the Company against adverse movements in underlying interest rates by matching projected future debt issuance against a derivative instrument with a fixed cash flow. Derivatives are revalued to fair value at the end of each reporting period.

(ii) Credit risk
Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's trade receivables, its loan with its immediate parent entity Thames Water Utilities Holdings Limited, short-term investments and cash flows receivable from counterparties to the derivative financial instruments. Under the terms of the Whole Business Securitisation agreement, counterparties to the Company's short term investments and derivative transactions have to meet minimum credit rating criteria as assigned by both Moody's and S&P. In respect of the derivative counterparties there is also a mechanism for the counterparty to post collateral when amounts due to the Company under outstanding derivative contracts exceed a contractually agreed threshold amount or the counterparty fails to meet the necessary credit rating criteria.

The Company has a statutory obligation to provide water and sewerage services to customers within its region. Due to the large area served by the Company and the significant number of household and business customers within this area, there is considered to be no concentration of trade receivables credit risk, however, the Company's credit control policies and procedures are in place to minimise the risk of bad debt arising from its trade receivables. Amounts provided against trade receivables and movements in the provision in the year are disclosed in note 15. Management have considered and taken action for the Company's exposure to credit risk arising from the opening of the non-household retail market to competition (effective 1 April 2017), as the bad debt risk for non-household water and wastewater services will lie with a small number of retailers and not the end user.

(iii) Liquidity risk
Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company manages long-term liquidity by maintaining continuity of funding through access to different market and debt instruments, raising funds in the capital markets and ensuring that manageable debt maturity profiles are maintained. The Company also maintains a level of committed liquidity facilities provided by a range of financial institutions. Details of the Company's borrowings and other financial instruments are disclosed in note 18 and 19, respectively.

Actuarial risk management

The two defined benefit pension schemes are exposed to actuarial risks including investment risk, inflation risk and longevity risk. Details of these risks are disclosed in note 23 of the financial statements. The trustees have taken a number of steps to control the level of investment risk within the schemes over the last year, including reducing the schemes' exposures to higher risk assets and increasing the level of protection against adverse movements in interest rates and inflation. The trustees of both schemes continue to review the risk exposures in light of the longer term objectives of the respective schemes.

Viability statement

The Directors have assessed the viability of the Company over a three year period to 31 March 2020. In making this assessment, the Directors have considered the current position of the Company, its ability to effectively and efficiently manage its finances, the current regulatory regime, its continued access to the debt markets, and ability to maintain a strong investment grade credit rating, whilst having regard to the principal risks and uncertainties as described on pages 42 to 50.

As part of the Company's recurring Price Review process, five year Company Business Plans ("CBP"s) are developed, the latest of which covers the five year period ending 31 March 2020. As part of the Company's financial resilience assessment, management has designed a number of 'stress tests' which subject the Company's existing model, that underlies the Company's planning processes, to a number of different scenarios and tests its sensitivity to these. The stress tests consider factors, both individually and in combination.

These include:

- Fluctuations in interest rates, which could affect the cost of financing the business;
- Fluctuations in inflation rates, which could affect the cost of investment and day-to-day operations, in addition to impacting amounts we bill our customers;
- Increase in operating expenditure, which would reduce profits and cash flow;
- Inability to secure new finance and/or delays in raising finance, reducing the cash available to deliver our investment programme; and

- Unforeseen maintenance and capital expenditure, which would increase costs and decrease cash flow.

Management have prepared a detailed methodology statement that sets out the approach taken to assessing the long-term viability of the Company, including specifics of the variables tested and their effect on the financial covenants of the Company. Taking account of the range of scenarios, the Directors consider that the Company has sufficient mitigating actions in place to address particular circumstances and events, should they arise.

The Directors consider that a three year period is reasonable given the nature of the industry in which the Company operates and to more closely align with the regulatory planning process given the changes in the regulatory framework that are being proposed.

Taking account of the range of severe, but plausible scenarios, the Company's current position and its principal risks, the Directors have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the next three years.

Principal risks and uncertainties

Management of our risks is key to ensuring the successful delivery of our strategic objectives and plans. We are committed to continuing to develop a practical and flexible framework that effectively identifies, assesses and manages risks and opportunities.

Our governance framework

Responsibility for the effectiveness of our risk management and governance framework sits with the Board. Regular oversight is delivered through the Audit, Risk and Regulatory Committee ("ARRC").

Principal risks are reviewed in detail by the ARRC at each Committee meeting and there is a rolling agenda for each Executive team member to present to the Committee key risks within his/her business area. In addition, we carry out 'deep dives' into the management of specific risks.

The quarterly Risk, Opportunity and Controls Committee ("ROCC"), chaired by Nick Fincham, the Strategy and Regulation Director, is responsible for reviewing and challenging the key risks, opportunities and controls identified by business area.

Our approach to risk management

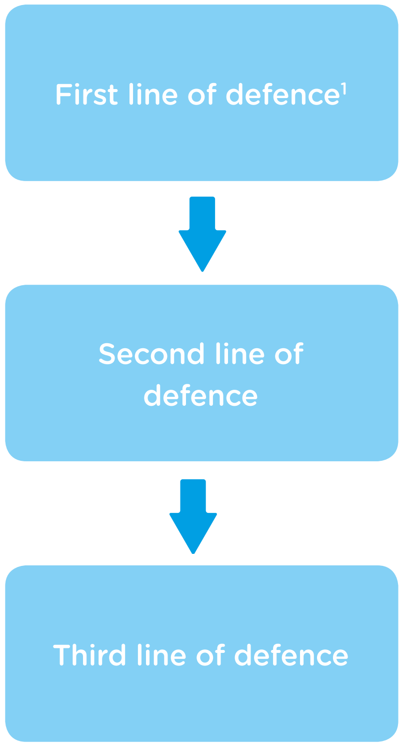
The system of internal controls and risk management recognises that the risk of failure to meet business objectives cannot be eliminated entirely. Any framework can only provide reasonable not absolute, assurance against the impact of risk events.

We align our risk management approach to ISO 31000 to support continuous improvement and review the effectiveness of the systems of risk management and internal control.

During 2016/17 we refined our focus and the terms of reference of the ROCC (formerly known as the Risk and Controls Committee) to more explicitly focus on managing current and emerging risks, and increasing the visibility of current mitigations and future action plans.

We prioritise risks according to our defined risk scoring criteria which takes into consideration both impact and likelihood.

Note 1: The three lines of defence model explains the relationship and responsibilities between business functions in effective risk management frameworks. The first line of defence covers business functions that own and manage risk, the second line oversees the first line with the third line providing independent assurance (Internal Audit/external assurance provider).



Our principal risks and uncertainties

We continually monitor the principal risks facing the Company, including those that would threaten our business model, future performance, solvency or liquidity.

Movement in the period

The most notable movements across the risk profile relate to our customer service, asset availability and performance, and information systems cyber security risks.

During the year, we reviewed the principal risks identified in 2015/16 and determined that the risks relating to bad debt and pension commitments are no longer considered significant.

Bad debt costs have reduced during the year, both in absolute terms, and as a percentage of gross revenue (2016/17: 2.4% versus 2015/16: 3.1%). This has been achieved by effective control mitigations including the implementation of a new debt management system and focus on improving data quality to enable more effective targeting of support and investigation of non-payment.

With respect to pension commitments, we are confident that there are sufficient and appropriate mitigating controls in place. The 31 March 2016 pension valuation is currently being concluded with the scheme trustees. Thames Water is a long-term business with a strong financial covenant to support future pension deficit payments. A recovery plan is in place based on the actuarial valuation dated March 2013, as agreed between our Directors and the Trustees. Under this plan, additional contributions are made to each of our two defined benefit schemes, totalling around £20 million annually. As part of the March 2016 actuarial valuation, we are engaging with the Trustees to agree an updated recovery plan.

During the year we experienced a series of trunk mains bursts, which impacted a number of customers in London, and which consequently caused reputational damage for our key stakeholders. The resilience of our infrastructure is an area of significant focus and attention for the Board and Executive team.

The terror attacks this year, worldwide cyber incidents and corporate information systems failures have increased focus on ensuring we have adequate and effective systems of prevention, detection and response.

Lastly, we have consolidated our risks associated with inflation, financing and credit ratings and review them holistically as part of a broader financial market risk.

We continue to identify, assess and manage current and emerging risks within our risk categories.

Risk Categories	Principal Risks 2015/16	Principal Risks 2016/17
Operational Loss resulting from inadequate or failed internal processes, systems, controls and people	**Customer service** Failure to improve and then maintain service levels **Economic and efficient delivery of services and capital projects** Inability to economically and efficiently deliver services and capital projects through alliance partnerships **Key assets and processes** Inability to provide water or treat wastewater due to failure of key assets and/or processes **Health, safety and wellbeing** The environment in which the Company operates, and the work it undertakes, exposes the workforce, business partners and the community to hazards that could harm their health, safety and wellbeing **Data and key business systems** Loss of data or interruptions to key business systems	**Customer service** Failure to improve and then maintain service levels **Economic and efficient delivery of services and investment projects** Inability to deliver services and investment projects economically and efficiently through supply chain and Alliance partnerships **Asset availability and performance** Interruptions to supply and services resulting from repairs, maintenance, operational issues, weather or security **Health, safety, environment and security** Failure to manage risks that may result in injuries, environmental damage, crime and/or sabotage **Information systems and cyber security** Failure to protect information technology and operational technology potentially causing data loss and systems/service failure
Compliance Compliance with laws, regulations and ethical standards	**Competition regulation** Failure to adapt to changes in the regulatory landscape due to the introduction of competition **Key legislation and regulation** Failure to comply with key regulation and legislation	**Competition regulation** Failure to adapt to changes in the regulatory landscape due to the introduction of competition **Legal and regulatory compliance** Failure to comply with and prepare for relevant regulation and legislation

Risk Categories	Principal Risks 2015/16	Principal Risks 2016/17
Financial Risks associated with exposure to financial markets, meeting financial obligations and accuracy of financial reporting	**Financing and credit rating** Inability to finance the Company and maintain target credit ratings. We are subject to a financial covenant that requires us, at each periodic review, to apply to Ofwat for a price determination which, in the reasonable opinion of the our Directors, would allow, at a minimum, a credit rating the same as the original credit rating at the establishment of the securitisation (A3/ BBB+) **Inflation rates** Consistently low inflation or deflation could lead to pressure on covenants and financing structures **Pension commitments** Inability to fund pension commitments **Bad debt recovery** The law prohibits the disconnection of a water supply from certain premises including domestic dwellings as a method of enforcing payment. This results in high levels of bad debt which cannot be recovered and need to be written off.	**Financial market (consolidation of relevant risks from 2015/16)** Volatility in interest rates and inflation, and maintaining ability to refinance effectively

Key

Risk profile has increased — No change in risk climate — Risk profile has decreased

Customer service	Risk category: operational
What the risk means to us Providing consistently high quality customer service is central to our overall strategy. Unacceptable customer service levels or the perception that we are failing to maintain and improve service quality will have a detrimental effect on customer satisfaction and the level of complaints. Some of the highest financial penalties and rewards are attached to the service incentive mechanism ("SIM") which is used by Ofwat to assess our customer service performance relative to other companies in the industry.	**What we are doing to manage the risk** We recognise that there is still much to do to meet customers' increasing expectations. To support this we: • are investing in a 'one-stop-shop' customer service centre, bringing together customer service and wastewater operational expertise under one roof to enhance our service and response level to customers; • have a new customer experience plan focusing on improving our customer communication channels, including our digital platforms, and online account management system and give customers more options to choose how they interact with us; and • are continuing to develop our customer case management capability to manage and resolve queries speedily, reduce complaints and proactively assist our most vulnerable customers. **Looking forward** • We are engaging with customers in preparation for our 2020-2025 business plan to support our understanding of customer needs and expectations; • We continue to focus on developing our new customer relationship management and billing system, as well as stabilising existing IT architecture; and • We are developing and implementing a company-wide customer experience plan under the leadership of the new Managing Director for Customer Services and Retail.
Movement in the year To improve our customer service we are revising and focusing our approach. W exited the non-household retail market to allow for greater focus on our core retail household customers. We have seen an improvement in complaint resolution with 94.5% being resolved first time (90.9% in 2015/16). Whilst our SIM score has moved from 76.74 to 77.26 in 2016/17, we recognise that much remains to be done and is in part driving the risk profile.	

Economic and efficient delivery of services and investment projects	Risk category: operational
What the risk means to us We have an investment programme of over £4 billion to deliver between 2015 and 2020. Failure to deliver the investment programme to time, cost and quality could affect customers, profitability and our reputation.	**What we are doing to manage the risk** • We are seeking to drive operational and financial efficiency and effectiveness through targeted improvement projects sponsored by Executive members with assurance provided by the Chief Delivery Officer; • We are refreshing our governance and investment case appraisal process under the leadership of the Chief Financial Officer to support effective allocation of economic capital onto key projects and priorities; and • We are reviewing our technology strategy through the Technology and Transformation Alliance to support increased investment in our infrastructure to improve system availability and stability. **Looking forward** • We are focused on the delivery and execution of our business-wide improvement projects with a significant focus on our customers, while stabilising our technology architecture and systems; and • We are considering the most efficient and effective delivery routes as part of planning for our 2020 to 2025 business plan submission due in September 2018.
Movement in the year Technology services were transferred to the Technology and Transformation Alliance during the year. Activities associated with the transition, stabilisation and enhancement of services have caused disruption and affected availability. In addition, the wider operating businesses including other alliances have yet to deliver expected levels of efficiency and transformation.	

Asset availability and performance	Risk Category: Operational
What the risk means to us Asset failure may lead to supply and service interruptions, environmental breaches, failure to meet regulatory targets and/or health and safety incidents. In addition, certain specific assets are critical to the provision of water and wastewater services to large populations. These require continued high levels of investment to ensure security and resilience.	**What we are doing to manage the risk** • We have established high operational standards for our significant assets; • We have an extensive customer education programme in place; • We inform investment decisions using asset based risk assessments, forecasting, quality assurance procedures and structural integrity monitoring reports; and • We have the largest investment programme in the industry to maintain and improve network and asset resilience. **Looking forward** • We are looking to further improve insight and innovation in asset performance; • We are reviewing our business contingency plans for asset based incidents including site monitoring technology on our wastewater sites to allow us to respond quickly when an incident occurs; and • We are investing heavily in mains replacements and will be replacing approximately 500km of mains by 2020 We've committed to spending an additional £97 million during the next three years to replace 'trunk' mains.
Movement in the year We have suffered a series of high-profile trunk mains bursts as well incurring an ODI penalty in respect of failure of sewage treatment works discharge compliance.	

Health, safety, environment and security ("HSES") — Risk category: operational

What the risk means to us

If we fail to manage risks associated with our operations it could result in fatality or injury, significant environmental damage, interruption to production or services, personal health and safety incidents, crime and sabotage and/or internal security related attacks.

The wider consequences of significant HSES events include precautionary closures, suspension of activities, or breach of applicable Health and Safety Executive ("HSE") regulations. This could lead to loss of licence, legal liability, regulatory enforcement, criminal proceedings and damage to our reputation.

What we are doing to manage the risk

- We have a zero tolerance approach when safeguarding the health, safety and wellbeing of employees, partners and the public;
- We continually review our HSES risks and the effectiveness of controls to manage them;
- We have continued to increase the competency of our workforce through new and innovative training such as our industry leading water safety course. There was an 11% increase in health and safety training days delivered to our employees during 2016/17;
- We have increased the numbers of employees in key operational roles and are investing heavily to improve reliability of sewage treatment works;
- We added £1.5 million to our Community Investment Fund to improve the river and surrounding environment at pollution affected locations; and
- We have robust security intelligence and operating procedures in place, and regularly evaluate and test crisis management and business continuity.

Looking forward

- We will continue to regularly review performance levels, including asset defect management; and
- We will review the potential threat from terrorism to our people, assets and operations is kept under review by our Security Board.

Movement in the year

We were fined £19.75 million plus costs for pollution incidents that took place at our sewage treatment works in Aylesbury, Didcot, Henley, Little Marlow and Arborfield, and Littlemore sewage pumping station between 2012 and 2014. We have also focused, in particular, on occupational process and safety, and business continuity. We reduced to zero the reservoirs presenting unacceptable levels of risk, and twice achieved two million consecutive man-hours without a lost time injury. We also achieved for the first time, a day when zero employees were absent with a work-related injury.

Information systems and cyber security — Risk category: operational

What the risk means to us

The effectiveness of our operations and the safeguarding of personal, commercial and operational data rely on the availability, integrity and security of complex information systems and networks. This includes those of our third-party service providers and alliance partners.

There can be no guarantee that our response, recovery and contingency plans will be sufficient to prevent and respond to all possible breaches. This could affect customer service delivery, security of data, performance of assets and cause reputational damage.

What we are doing to manage the risk

- We work collaboratively with working groups across the utilities industry and public and private sectors to manage security threats to our national infrastructure;
- Our information security strategy integrates data, cyber, physical and personnel security overseen by our Security Board;
- We have solutions in place to detect and investigate security threats and incidents to ensure potentially vulnerable systems are identified and vulnerability gaps closed; and
- We review the adequacy and effectiveness of our infrastructure and technology security controls, undertake employee security awareness training, and test contingency and recovery processes.

Looking forward

- With the introduction of the Technology and Transformation Alliance we are undertaking an exercise to better understand our business and future technology requirements, and our threat landscape; and
- We are increasing technology spend to modernise our infrastructure and improve system availability and stability.

Movement in the year

We monitor the cyber-threat landscape and take proactive steps to ensure, in applying industry best practice, we protect our infrastructure, operations and the data we hold.

Competition regulation

Risk category: compliance

What the risk means to us

As a wholesaler in the non-household market, we have delivered our business transformation programme, meeting all market requirements. One key requirement is providing a 'level playing field' to all retailers operating in our region. It is vital that we do not prejudice any retailer in the services we offer.

What we are doing to manage the risk

- We have designed and implemented our processes with competition and market code obligations front and central;
- We have established a Wholesale Market Services team to ensure we fulfil our market obligations; and
- We are actively engaged with Market Operator Services Limited ("MOSL") to support effective and efficient operation of the market.

Looking forward

- We are satisfied that the processes and procedures we have introduced offer all retailers a fair and consistent service, however, we are aware that improvements will be necessary as the market matures in order to meet our objectives to deliver excellent service to new and existing retailers.

Movement in the year

We sold our non-household retail business to Castle Water to focus on our retail household and wholesale businesses. We continue to ensure we follow the market codes and fulfil our market obligations. We have not revised the risk profile in light of the market opening on 1 April 2017.

Legal and regulatory compliance

Risk category: compliance

What the risk means to us

The water industry is subject to a wide range of regulations, laws and rules that are overseen by statutory and regulatory bodies in the UK and, currently, the EU.

Failure to comply with relevant regulations could undermine public trust in our business and management. Furthermore, this may lead to regulatory and/or legislative action or investigation, potentially resulting in enforcement notices, licence changes, criminal proceedings, financial penalties, damage to our reputation and delivery of our operations.

What we are doing to manage the risk

- We have a clear understanding of our regulatory and key legal obligations, as well as identifying impending new legislation, and changes to existing legislation and licence conditions. Compliance is monitored through Audit and Assurance and as part of the annual company self-assessment;
- We provide training programmes to employees and service delivery partners to support compliance with key laws;
- We support industry consultations to influence regulatory and legal developments; and
- We changed our processes and procedures to support compliance within the non-household market from 1 April 2017.

Looking forward

- We continue to strengthen our regulatory and legislative compliance programme. We pay specific attention to our environmental responsibilities, including learning lessons following pollution incidents occuring between 2012 and 2014 for which we incurred a significant fine in 2017; and
- We are developing plans in response to the UK Government white paper on corporate governance, the DEFRA paper on enabling resilience in the water sector and to ensure compliance when the GDPR comes into force.

Movement in the year

We continue with preparations to adapt to changes in the regulatory landscape. This includes the introduction of non-household competition, as well as new and impending legislation that impacts our business, such as the Modern Slavery Act (MSA) and General Data Protection Regulation ("GDPR") which comes into force in May 2018 and carries a penalty per offence of up to 4% of global turnover (circa £80 million).

Financial markets	Risk Category: financial
What the risk means to us Our financial performance is dependent upon our ability to access new and competitively priced sources of debt financing and manage exposure to financial market and economic risks resulting from changes in interest rates, inflation and exchange rates. Our Regulatory Capital Value ("RCV") and wholesale revenue are linked to the underlying rate of inflation, measured by the Retail Price Index (RPI). A prolonged period of low inflation and/or deflation adversely impacts financial performance.	**What we are doing to manage the risk** • The impact of low inflation and/or high interest rates is mitigated by the fact that most of our debt is fixed rate or linked to RPI; • We have used forward starting interest rate swaps to reduce the interest rate risk associated with new debt raised; • Our annual funding strategy is approved by the Board. We successfully issued £568.1 million of new debt in the year to 31 March 2017, and a further £550.0 million in May 2017; • We swap all foreign currency debt to sterling using derivatives; • We maintain an open dialogue with credit rating agencies on financial and operational performance to support credit rating agency understanding of our plans and delivery execution; • We have £1.45 billion of committed bank facilities to provide guaranteed liquidity; • We have long-term refinancing with staggered maturity dates to minimise refinancing risk; and • We maintain a diverse portfolio of debt sources to reduce reliance on particular markets or providers of debt financing. **Looking forward** • Volatility in financial markets is expected to continue, particularly in sterling interest rate and foreign exchange markets, as the future trading and political relationship between the UK and the EU is redefined. • It is unclear whether Brexit will impact on the ability of the European Investment Bank ("EIB") to continue to lend to the UK water sector; and • We will continue to focus on improving operational performance and delivering further improvements over the course of the remainder of this regulatory period.
Movement in the year In accordance with our Instrument of Appointment, we continue to maintain a strong investment grade credit rating, as assigned by external ratings agencies Moody's and Standard & Poor's ("S&P"). The assessment by these two agencies provides an independent view of our performance and future prospects. In April 2017, Moody's reaffirmed our Baa1 Corporate Family Rating ("CFR") with a stable outlook. Moody's cited our low business risk profile and the relatively stable and predictable cash flows generated under a well-established and transparent regulatory framework as drivers which support the rating, as well as the creditor protections incorporated within the financing structure. Moody's did, however, recognise that these strengths are somewhat offset by the relatively high gearing we employ. In their most recent credit opinion in September 2016, S&P assigned ratings of A- (Class A) and BBB (Class B) and maintained a negative outlook. Whilst S&P recognise positive developments in operating performance over the previous two years, it assessed these improvements as lagging behind our peers and retained a negative outlook reflecting their assessment of the limited headroom at current leverage levels.	

Our corporate governance

Our corporate governance

Chairman's introduction

This year has been a year of significant change for our Company at Board level.

Board changes

As previously reported, Martin Baggs stepped down as Chief Executive Officer in August 2016 and Stuart Siddall retired as Chief Financial Officer in December 2016. Michael Pavia retired as Senior Independent Director in February 2017 and Mark Braithwaite resigned as Non-Executive Director in May 2017.

As I reported last year, Nick Fincham, Director of Strategy and Regulation, joined the Board in April 2016. This year we welcomed to the Board, Steve Robertson, Chief Executive Officer in September 2016, Nick Land, Independent Non-Executive Director and Chair of the Audit, Risk and Regulatory Committee ("ARRC") in February, Brandon Rennet, Chief Financial Officer in March and Kenton Bradbury, Non-Executive Director in May 2017, respectively.

Collectively, our Board of Directors have a wealth of management, financial and infrastructure experience, together with extensive specialist knowledge of the water industry and other regulated utilities and we are delighted to welcome all five Directors to the Board. Their biographies can be found on page 55 to 59.

Corporate governance

The Board believes that high standards of corporate governance are integral to its relationship with stakeholders and to the delivery of the Company's strategic aims. The Board considers that the Company has complied with the provisions and practice of the UK Corporate Governance Code where possible, with the exception of those provisions which are explained on page 64. The Board also ensures that the Company's governance processes align with Ofwat's Principles of Board Leadership, Transparency and Governance and as part of its principles Ofwat considers that the Disclosure and Transparency Rules ("DTR") set out the standard of disclosure that regulated companies should operate, whether they be publicly or privately owned. The Company endeavours, where applicable, to comply with DTR.

Sir Peter Mason KBE
Chairman

Our directors

Our Chairman

Sir Peter Mason KBE
Chairman (70)

Sir Peter became our Chairman in December 2006 and brings extensive experience in engineering, construction and complex capital investment businesses. He retired as CEO of Amec plc in September 2006 and previously was Chairman and CEO of Balfour Beatty Limited.

Sir Peter was the Senior Non-Executive Director of BAE Systems plc until May 2013 and until October 2008 was a Board member of the 2012 Olympic Delivery Authority. He is currently a Non-Executive member of the Board of Spie S.A., Senior Independent Director of Subsea 7 S.A and Chairman of AGS Airports Limited.

Sir Peter was made a Knight Commander of the British Empire (KBE) in 2002 for services to international trade.

Our Executive Directors

Steve Robertson
Chief Executive Officer (59)

Steve became our CEO in September 2016, having previously held the position of Chief Executive Officer at Truphone, where he developed groundbreaking technology allowing it to become a disruptive player in the global market.

Prior to joining Truphone, Steve served as CEO of BT Openreach from its inception in 2005 until 2010.

He has gained extensive experience in the telecoms industry with a wide variety of roles in the BT Group and at COLT Telecommunications, including having responsibility for the overall performance and operation of the whole of BT's UK mainland telecommunications network, as Managing Director of Wholesale Operations.

Brandon Rennet
Chief Financial Officer (44)

Brandon joined us in March 2017 as CFO, having previously worked for energy company SSE since February 2007, where he held a number of senior finance roles before being appointed Managing Director of Finance in July 2013.

Brandon's main achievements at SSE included leading the execution of more than £7 billion of funding, primarily in the public debt capital markets, and driving its finance transformation programme.

His earlier career included finance roles in Edinburgh, London, Philadelphia and Toronto for companies including PwC, HSBC, and British Energy.

Nick Fincham
Director of Strategy and Regulation (46)

Nick was appointed to our Board in April 2016. Since April 2011 Nick has been a member of our Executive Committee as Director of Strategy and Regulation. In this role, he successfully oversaw our business planning for the PR14 price control review, ensuring that it was focused on the needs of the customer.

Before joining Thames Water, Nick spent six years as Director of Economic Regulation and Competition Policy at the Civil Aviation Authority.

Prior to that, he held senior positions at a number of economic regulators including OFFER, Ofgas, Ofgem and Postcomm.

Our Independent Non-Executive Directors

Lorraine Baldry OBE (68)
A, C

Lorraine was appointed as an Independent Non-Executive Director of Thames Water Utilities Limited in September 2014.

She is Chairman of London & Continental Railways, Schroder Real Estate Investment Trust Limited and Inventa Partners Limited and a Governor at the University of the Arts, London. Lorraine was Chief Executive of Chesterton International plc and prior to that held various senior positions at Prudential Corporation, Morgan Stanley and Regus.

She is a former Senior Independent Director of Circle Holdings plc, Chairman of London Thames Gateway Development Corporation and Central London Partnership. Lorraine was a Board Member of the Olympic Delivery Authority where she chaired the Planning Committee.

Lorraine is an Honorary Member of the Royal Institution of Chartered Surveyors and a Past President of the British Property Federation. She was awarded OBE in the Queen's Jubilee Honours.

Dame Deirdre Hutton DBE (68)
A, C*

Dame Deirdre was appointed as an Independent Non-Executive Director of Thames Water Utilities Limited in July 2010 and is the Chair of the Company's Customer Service Committee. She is Chair of the Civil Aviation Authority, Pro-Chancellor of Cranfield University and was a Non-Executive Director of Castle Trust until March 2016.

Dame Deirdre was a non-executive member of HM Treasury Board, and was previously Chair of both the National Consumer Council and Food Standards Agency and Deputy Chair of the Financial Services Authority. Dame Deirdre has held a number of positions on a variety of bodies dealing with food issues. She is currently Vice President of the Trading Standards Institute.

Nick Land (69)
A*, R, N

Nick became a Independent Non-Executive Director of Thames Water Utilities Limited in February 2017. A chartered accountant, Nick retired as Chairman of Ernst & Young LLP in 2006 after a career spanning 36 years with the firm. He became an audit partner in 1978 and held a number of management appointments before becoming Managing Partner in 1992. He was elected Chairman in 1995 and joined the Global Executive Board at that time. He was also Chairman of Ernst & Young's Northern Europe, India, Middle East and Africa Region.

Nick is a Non-Executive Director of the Financial Reporting Council and a Non-Executive Director of Vodafone Group plc. He stepped down as a Non-Executive Director of Ashmore Group plc in October 2016, BBA Aviation plc in May 2016, Alliance Boots GmbH in 2015 and Royal Dutch Shell plc in 2010. He is an adviser to the board of Dentons UKEMEA LLP and chairs the Private Equity Reporting Group of the British Venture Capital Association.

He is also Chairman of the board of trustees of the Vodafone Group Foundation.

Ian Pearson (58)
A, R, N

Ian Pearson was appointed as an Independent Non-Executive Director of Thames Water Utilities Limited in September 2014. He was Chairman of Octopus VCT2 plc for five years and is Chairman of Code Investing Ltd.

Amongst other advisory roles he is an advisor to BAI Communications and was a member of PwC's UK Advisory Board for five years. He had various roles in Government between 2001 and 2010 when he stood down as an MP. He was Economic Secretary to the Treasury between 2008 and 2010, and prior to that he had roles as Science and Innovation Minister, Minister for Climate Change and the Environment, Minister for Trade and as a Minister in Northern Ireland.

Ian studied PPE at Balliol College, Oxford, before gaining a Masters and Doctorate at the University of Warwick.

Ed Richards CBE (51)
A, C

Ed was appointed as an Independent Non-Executive Director of Thames Water Utilities Limited in July 2010. He was Chief Executive of Ofcom until December 2014, having previously been the Chief Operating Officer. He is currently a Managing Partner at Flint Global, a business advisory firm.

He was a senior policy advisor to the Prime Minister for media, telecoms, the internet and e-Government and Controller of Corporate Strategy at the BBC. He has worked in consulting at London Economics Limited, as an advisor to Gordon Brown MP and began his career as a researcher with Diverse Production Limited where he worked on programmes for Channel 4. He was previously a Vice Chairman of the Body of European Regulators for Electronic Communications (BEREC).

He is a Director of Donmar Warehouse and a Governor of the London School of Economics. Ed was awarded the CBE for services to the communications industry in the Queen's birthday Honours list in 2015.

Key to Committees

A = Audit, Risk and Regulatory Committee

R = Remuneration Committee

N = Nominations Committee

C = Customer Service Committee

* = Chair of Committee

Our Non-Executive Directors

Kenton Bradbury
(47)

Kenton was appointed a Non-Executive Director of Thames Water Utilities Limited in May 2017. He is currently Managing Director, Asset Management at Borealis Infrastructure where he is responsible for the asset management of OMERS's investments, with a focus on Europe.

Kenton previously served as a Non-Executive Director of Yorkshire Water and Affinity Water and was a Director at Infracapital (the infrastructure investment arm of M&G Investments), where he sat on the boards of various portfolio companies. Prior to Infracapital, he was SVP Infrastructure and Regulation at e.on, based in Germany. He began his career as a consultant working in the utilities and space sectors, and has held various senior operational and strategic roles in infrastructure businesses. Kenton is a Chartered Engineer and currently sits on the boards of London City Airport, Caruna in Finland and Net4Gas in the Czech Republic amongst others.

Christopher Deacon
(69) A, R, N

Christopher became a Non-Executive Director of Thames Water Utilities Limited in December 2006. He is an independent infrastructure and project finance consultant, adviser to OFGEM, and a Non-Executive Director of various companies in the infrastructure and PPP market place.

His career in banking and structured/infrastructure finance has spanned over 20 years, acting as adviser and banker in major infrastructure and project financings around the world. He has acted as a consultant on large infrastructure projects both in the public and private sectors, with assignments including Eurotunnel, Channel Tunnel Rail Link, Tube PPP, and other transport infrastructure projects.

Christopher is a director of the trading company of London Business School and a past School Governor. He is Treasurer/Trustee of the Franco British Council UK Section.

Nick Horler
(58) C

Nick was appointed a Non-Executive Director of Thames Water Utilities Limited in April 2014. He has been a member of the Board of the Go-Ahead Group since 2011 and was previously a member of the Board of Royal Mail until February 2017. He has been Chair of Alderney Renewable Energy and Chair of Meter Provida Ltd since 2014 and, became the Chair of Adler & Allan in March 2015. He was Chair of the Advisory Board of KPMG's Energy and Natural Resources practice from 2011 to 2014.

Nick spent his executive career in the energy industry, where he worked for Phillips Petroleum for 12 years in a variety of roles in the UK and USA. He also spent 11 years with E.ON including eight years on the Board of e.on UK, first as Managing Director of PowerGen Energy Trading Limited and then as Managing Director of E.ON Retail. He was CEO of Scottish Power from 2008 to 2010.

Guy Lambert
(40)

Guy became a Non-Executive Director of Thames Water Utilities Limited in October 2014. He has been with the Abu Dhabi Investment Authority in the Infrastructure Division since February 2008 and currently heads up the utilities business globally within the Infrastructure Division. He is responsible for sourcing and executing new investments in the utilities sector and overseeing the existing utilities portfolio.

His previous roles include Corporate Finance and Advisory Manager at Macquarie Capital London and Corporate Finance and Advisory Analyst at Dresdner Kleinwort Wasserstein. Guy has an MSc in Economics from Erasmus University in Rotterdam, Netherlands.

Dipesh Shah OBE, FRSA
(64) A, C

Dipesh became a Non-Executive Director of Thames Water Utilities Limited in October 2007. He is Chairman of Genesis Housing Association and a Non-Executive Director on the Boards of Cannacord Genuity Group Inc, the Crown Estate, Cavendish Fluor Partnership and the EU Marguerite Fund where he is Chairman of the Investment Committee. He is Trustee of the British Youth Opera, Governor of Merchant Taylors' School and Chairman of ANHD International Advisory Services Ltd.

He was the Chief Executive of the UK Atomic Energy Authority and of various large businesses in the BP Group. He was a Non-Executive Director of Babcock International Group plc, Lloyd's of London and JKX Oil & Gas Plc. He was Chairman of Viridian Group plc, HgCapital Renewable Power Partners LLP and the European Photovoltaic Industry Association and was a member of the Government's Renewable Energy Advisory Committee from 1994 to 2002.

Key to Committees

A = Audit, Risk and Regulatory Committee
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C = Customer Service Committee
* = Chair of Committee

Our executive team

Our executive team is responsible for the day-to-day running of our business. As at 13 June 2017, it consists of the CEO, the CFO, the Director of Strategy and Regulation, and seven functional directors.

Steve Robertson
Chief Executive Officer

Steve became our CEO in September 2016, having previously held the position of Chief Executive Officer at Truphone, where he developed groundbreaking technology allowing it to become a disruptive player in the global market.

Prior to joining Truphone, Steve served as CEO of BT Openreach from its inception in 2005 until 2010.

He has gained extensive experience in the telecoms industry with a wide variety of roles in the BT Group and at COLT Telecommunications, including having responsibility for the overall performance and operation of the whole of BT's UK mainland telecommunications network, as Managing Director of Wholesale Operations.

Brandon Rennet
Chief Financial Officer

Brandon joined us in March 2017 as CFO, having previously worked for energy company SSE since February 2007, where he held a number of senior finance roles before being appointed Managing Director of Finance in July 2013.

Brandon's main achievements at SSE included leading the execution of more than £7 billion of funding, primarily in the public debt capital markets, and driving its finance transformation programme.

His earlier career included finance roles in Edinburgh, London, Philadelphia and Toronto for companies including PwC, HSBC, and British Energy.

Nick Fincham
Director of Strategy and Regulation

Nick was appointed to our Board in April 2016. Since April 2011 Nick has been a member of our Executive Committee as Director of Strategy and Regulation. In this role, he successfully oversaw our business planning for the PR14 price control review, ensuring that it was focused on the needs of the customer.

Before joining Thames Water, Nick spent six years as Director of Economic Regulation and Competition Policy at the Civil Aviation Authority.

Prior to that, he held senior positions at a number of economic regulators including OFFER, Ofgas, Ofgem and Postcomm.

Richard Aylard CVO
External Affairs and Sustainability Director

Richard joined Thames Water in 2002 as Corporate Responsibility Director. He leads our engagement with external stakeholders, including Government, the Environment Agency and the Consumer Council for Water and is the principal spokesperson with the media and other audiences.

As Sustainability Director, Richard has responsibility for environmental and social issues.

Janet Burr
Human Resources Director

Janet was appointed Human Resources Director in November 2010, having previously served as Interim Human Resources Director from June 2010. Janet has responsibility for all employee issues.

The HR function contributes to the overall business strategy, particularly through the Company's People Strategy, which underpins the vision, mission and values required to achieve the business goals of profitable growth and operational delivery.

Bob Collington OBE
Interim Chief Information Officer

Bob was appointed Interim Chief Information Officer in April 2017, having previously held the role of Managing Director, Water. Bob has held a number of senior roles throughout Thames Water and spent five years overseas in the USA at Elizabethtown Water Company and American Water where he served on the Board of the Long Island Water company.

Bob also serves as a Board Member for UK Water Industry Research, the independent company that facilitates research for the water industry in the UK.

In June 2013 Bob was awarded an OBE in the Queen's Birthday Honours list reflecting his huge contribution to Thames Water, the industry and in particular the management of the drought and the successful service delivery during the Olympic Games.

Lawrence Gosden
Managing Director, Wastewater

Lawrence is the Managing Director of our Wastewater business. He joined us in October 2007 and has previously held senior positions at Southern Water and South East Water.

Lawrence was responsible for the sustainable management of Thames Water's infrastructure together with a £5 billion capital investment programme between 2010 and 2015, including the Lee Tunnel, Thames Tideway sewage treatment works improvements and the four joint ventures responsible for the majority of its remaining programme.

Kelly Macfarlane
Managing Director, Customer Service and Retail

Kelly joined Thames Water in December 2016 and took up the role of Managing Director, Customer Service and Retail in March 2017, having previously worked at Openreach, the infrastructure division of BT Group since 2008.

Kelly has significant experience managing customer service operations and infrastructure in regulated environments and a demonstrable track record of achieving strong operational results and service transformation having held a variety of key regulatory, commercial and operational roles. Her earlier career included various roles leading service delivery operations at Deloitte, Tiscali and npower.

Sarah McMath
Managing Director, Water

Sarah joined Thames Water in 1994 in the Water Research and Development team and took up the role of Managing Director, Water in April 2017. She completed her doctorate in 1998, moving to lead the Water Quality team, before taking on the management of the Wastewater Western Provinces team in 2000. Since then Sarah has led Wastewater technical teams, Maintenance and operational teams and Asset Management functions

Moving to the Strategy and Regulation team in 2012, Sarah led the preparation and submission of our business plans for PR14 and took on the additional responsibility of Programme Director for Competition 2017 in November 2015.

Steve Spencer
Chief Delivery Officer

Steve joined Thames Water in 2012 and took up the role of Chief Delivery Officer in April 2017, having previously held a number of senior management positions in Thames Water. Steve is responsible for the successful delivery of our customer focused goals and strategic plans across the business.

Steve has significant experience managing in the water industry and has a proven track record of improving performance and delivering strong operational results. His career has been dedicated to the water sector with senior roles in Operations, Customer Service and Capital Delivery, both in the UK and overseas. His earlier career included various roles at Southern Water and MWH Australia.

Annual report and financial statements 2016/17

Compliance statement

The UK Corporate Governance Code 2014 (the "Code") applies to accounting periods beginning on or after 1 October 2014. In addition to the Code, we are required to adhere to Ofwat's Board Leadership, Transparency and Governance Principles (the "Ofwat Principles") which are built into our own governance framework.

During the financial year ended 31 March 2017, we applied all of the main principles of the Code with the exception of the following provisions:

Independence of the Chairman

Provision A.3.1 of the Code requires that the Chairman be independent on appointment. The Chairman is considered by the Board to be independent but for the purpose of the Code was not considered independent on his appointment as he was appointed by shareholders of Kemble Water Holdings Ltd. He is also Chair of the AGS Group, which is jointly managed by Macquarie Infrastructure and Real Assets and Ferrovial, with each party controlling 50%. Kemble Water International Holdings Limited, up until 31 May 2017, was the major shareholder of Kemble Water Holdings Limited.

The Boards of both Thames Water Utilities Limited and Kemble Water Holdings Limited consider that the Chairman provides impartial and effective leadership of the Board and are satisfied that no conflict of interest arises from his appointment as Chairman.

Senior Independent Director

Provision A.4.1 requires that the Board should appoint one of the independent non-executive directors to be the senior independent director to provide a sounding board for the chairman and to serve as an intermediary for the other directors when necessary.

Throughout the financial year and up until the date of his resignation, on 6 February 2017, Michael Pavia was the Senior Independent Director for the Board. As at the date of this report, 13 June 2017, the Board has yet to appoint a Senior Independent Director to replace Michael. The Board are in the process of identifying a replacement and the appointment will be approved by the Board as soon as possible.

Independent Non-Executive Directors

Provision B.1.2 of the Code requires that at least half the Board, excluding the Chairman, should comprise non-executive directors determined to be independent. In accordance with Ofwat's Principles, though not the Code provision, the Independent Non-Executive Directors, including the Chairman, represent the largest single group on the Board.

The Board considers that the balance of half of the Non-Executive Directors being independent provides sufficient balance to ensure that the Board operates in a fair and transparent manner.

Nominations Committee

Provision B.2.1 of the Code requires that the Company establish a nominations committee comprising a majority of independent non-executive directors. Our Nominations Committee includes four Non-Executive Directors, of whom two are considered to be independent and the Company Chairman. The Committee is chaired by the Company Chairman, who is considered by the Board to be independent but was not considered independent on appointment.

The Board considers that the Chairman provides appropriate and impartial leadership of the Committee and is satisfied that the Committee operates in an effective and transparent manner.

Board Evaluation

Provision B.6.1 requires that the Company, on an annual basis, undertake a formal evaluation of its own performance and that of its committees and individual directors.

Given the numerous changes that took place at Board level during the year, it was felt that an internal Board evaluation would not provide a clear and comprehensive review of the Board's performance. Therefore, the Board will undertake an internal evaluation during 2017/18 and an external evaluation will be held during 2018/19.

Remuneration Committee

Provision D.2.1 requires that we establish a remuneration committee including at least three independent non-executive directors. In addition, the company chairman may also be a member of, but not chair, the committee if he or she was considered independent on appointment as chairman. The composition of the Remuneration Committee comprises four Non-Executive Directors, of whom two are considered to be independent and the Company Chairman. The Committee is chaired by the Company Chairman, who is considered by the Board to be independent but was not considered independent on appointment.

The Board considers that the Chairman provides appropriate and impartial leadership of the Committee and is satisfied that the Committee operates in an effective and transparent manner.

Board meetings and agendas

The Thames Water Utilities Limited Board (the "Board") held eight meetings during the year, five scheduled and three additional meetings. In addition, there were three informal workshops to facilitate in-depth discussions on matters such as performance updates from the Alliances, dividend and gearing, derivatives, credit rating and bad debt management.

The Board holds separate meetings on a regular basis, without the Executive Directors being present, to discuss any issues or concerns. In addition, the Chairman meets only with the Independent Non-Executive Directors at least once a year. There are also a number of informal opportunities for the Directors to meet and discuss specific areas of the business with individual members of the Executive Team and other employees across the organisation.

Directors' attendance at Board meetings for the financial year 1 April 2016 to 31 March 2017 is summarised in the table below:

Membership of the Board during 2016/17	Scheduled meetings attended/eligible scheduled meetings	Additional meetings attended/eligible additional meetings
Sir Peter Mason	5/5	3/3
Steve Robertson (Appointed 01/09/16)	3/3	1/1
Brandon Rennet (Appointed 13/03/17)	-	1/1
Nick Fincham	5/5	2/3
Lorraine Baldry	5/5	3/3
Kenton Bradbury (Appointed 31/05/17)	-	-
Christopher Deacon	5/5	1/3
Nick Horler *	4/5	3/3
Dame Deirdre Hutton	5/5	2/3
Guy Lambert	5/5	2/3
Nick Land (Appointed 06/02/17)	-	1/1
Michael Pavia (Resigned 06/02/17)	5/5	2/2
Ian Pearson	5/5	3/3
Ed Richards*	4/5	2/3
Dipesh Shah*	4/5	2/3
Stuart Siddall (Resigned 31/12/16)	4/4	2/2
Mark Braithwaite (Resigned 31/05/17)*	4/5	3/3
Martin Baggs (Resigned 31/08/16)	2/2	2/2

*Nick Horler, Ed Richards, Dipesh Shah and Mark Braithwaite were unable to attend a scheduled meeting of the Board due to prior commitments.

Board activities during the year

This table sets out the Board's core agenda at every meeting and specific items of focus during the year.

Core agenda

- Review of the monthly management report which includes business updates on financial, regulatory and operational performance indicators
- Updates from the Head of Health, Safety, Security & Wellbeing on our health and safety performance
- Updates from the Competition 2017 Programme Director on market readiness ahead of market opening on 1 April 2017
- Reports from the Board Committees Chairmen on matters discussed at previous committee meetings

Focus areas

April 2016

- Reviewed and approved the 2016/17 budget
- Reviewed and considered talent development, succession planning and employee engagement
- Reviewed and discussed the external 2016 Board effectiveness review that took place in December 2015
- Received a report on retail non-household price control
- Approved a licence change to the wholesale revenue forecasting incentive mechanism
- Approved the formation of the Technology and Transformation Alliance
- Received a report on retail systems
- Renewed the annual insurance progamme

June 2016

- Received a presentation by Marcus Rink, Chief Inspector of the Drinking Water Inspectorate
- Reviewed and approved the Annual Report & financial statements and Annual Performance report
- Received a report on the renewal of liquidity facilities
- Reviewed and approved the Bonus and Long Term Incentive Plan payments
- Approved the Modern Slavery Act statement
- Received an update on retail non-household price control

September 2016

- Received a presentation by Moody's about our credit rating
- Received an update on business planning
- Received an update on household retail competition
- Approved the annual debt prospectus update

November 2016

- Received and discussed a report on leakage
- Reviewed and approved the interim financial statements
- Approved the refinancing of the PCR bond
- Considered and discussed the Statement of Reporting Risks & Draft Assurance plans
- Received an update on the 2017/18 wholesale and retail charges
- Approved a licence change to Water 2020
- Received an update from the Nominations Committee Chair on the recent CFO and Independent Non-Executive Director appointments

January 2017

- Received a presentation on the trunk mains bursts
- Received an update on business planning
- Reviewed and approved a dividend distribution to our shareholders

Leadership

The Board is chaired by Sir Peter Mason and at the date of this report there were three Executive Directors (CEO, CFO and Director of Strategy and Regulation), five Non-Executive Directors and five Independent Non-Executive Directors, (together the "Directors").

Role of the Board

The Board has a clearly defined framework of roles, responsibilities and delegated authorities in place to support its primary responsibility to promote the long term success of the Company for the benefit of its customers, employees, shareholders and other stakeholders. The Board seeks to achieve this by providing appropriate resources to meet strategic objectives and reviewing Executive management's performance. The Board considers that it sets the standards and values expected across the organisation and by its stakeholders.

Schedule of Delegated Authority

We have adopted a framework of delegated authorisations in its Schedule of Delegated Authority ("SoDA"). The SoDA defines the levels of authorisation required for specified transactions and also sets out approval limits for operating and capital expenditure. The SoDA authorises the CEO and CFO to approve certain transactions up to specified limits, beyond which the approval of the Board is needed.

The SoDA also contains matters specifically reserved to the Kemble Water Holdings Limited Board (the "Kemble Board") for approval. These include approval of annual budgets, financial plans, financial statements, material transactions, such as major acquisitions, divestments, funding and investment proposals and certain strategic decisions. During the year the Kemble Board accepted all recommendations from the Board on reserved matters.

Division of responsibilities

The roles of the Chairman and Executive management, led by the CEO, are separate and clearly defined. This division of responsibility has been approved by the Board.

Role of the Chairman

The Chairman is responsible for leading the Board, ensuring its effectiveness, setting the agenda and ensuring effective dialogue with the Company's shareholders. In addition, he is responsible for ensuring that the Board receives accurate, timely and clear information and that constructive relations exist between Executive and Non-Executive Directors. The Chairman maintains a dialogue with the Board outside of the scheduled Board meetings in order to keep them apprised of any matters of interest, and to ensure that any training requirements are duly arranged.

Sir Peter Mason remains Chairman of Thames Water Utilities Limited and Kemble Water Holdings Limited and both Boards consider that his appointment does not present a conflict of interest in light of the purpose of Kemble Water Holdings Limited, which acts as a holding company for the regulated entity, Thames Water Utilities Limited.

The selection of a successor to the Chairman will be the responsibility of the Independent Chairman Nominations Committee, which will constitiute solely for that purpose, and will comprise both Non-Executive Directors and a majority of Independent Non-Executive Directors.

Role of the CEO and executive team

The CEO is responsible for the leadership and operational management of the Company within the agreed strategy and business plan. He is supported by the CFO, the Director of Strategy and Regulation and seven functional directors (together, the "Executive Team"). None of the functional directors are members of the Board. (Biographies for the Executive Team can be found on pages 60 to 62).

Induction programme

Nick Land's induction programme included a meeting with the Chairman and CEO, as well as the Executive Directors and other senior management team to ensure he gained a thorough overview and understanding of the key business areas. In addition, key site visits were arranged during his first few months to allow him to experience, first hand, the operational side of the business.

Each new Director is provided with a wealth of information, including:

- Group structure and history
- Key people and succession plans
- Overview of our business including an explanation of the regulatory and governance frameworks
- Current strategic plan, business plan and budgets for the year
- Financial overview including group funding and dividend policy
- Overview of how our business operates covering retail, wastewater and water, and includes visits to key sites
- Commercial overview
- Major risks and internal risk management strategy
- A briefing about our customer engagement to understand our customer's views and a meeting with our Customer Challenge Group and other key stakeholders
- Visit to the Customer Solution Centre to better understand the practical issues affecting the business
- Status of the pension schemes

Board effectiveness

Independence and conflicts of interest

The Board reviews the independence of the Independent Non-Executive Directors on appointment and continues to do so, on an on-going basis. The Board considers that the Independent Non-Executive Directors are independent in character, judgement and behaviour and is satisfied that there are no relationships or circumstances which are likely to affect, or could appear to affect, the director's independence. The Independent Non-Executive Directors are appointed for three year terms. Details of Directors' contracts can be found in the Remuneration Report on page 78.

There are five Non-Executive Directors that are nominated and appointed by the shareholders of Kemble Water Holdings Limited and are therefore not classified as Independent. All Non-Executive Directors are subject to annual re-election.

Michael Pavia was the Senior Independent Director, until his resignation on 6 February 2017 and was available to all stakeholders to answer any queries that cannot be addressed by the Chairman or other Executive Directors. He was also available to chair the Board and Committee meetings if the Chairman or Committee Chairman be unable to attend. The Board are currently in the process of appointing a new Senior Independent Director.

As a matter of good governance all Directors are required to disclose their other significant commitments to the Board. They are also required to advise the Company Secretary of any actual or potential conflicts of interests as soon as they arise, so they can be considered by the Board at the next available opportunity. Any Director with a potential conflict of interest in relation to a specific matter under consideration by the Board or one of its Committees is required to recuse him/herself from the relevant meeting while this item is discussed and may not vote on the matter It is the Board's view that this procedure operated effectively during 2016/17.

Neither the CEO nor the CFO acts for any FTSE company in the capacity of a Non-Executive Director or Chairman.

Diversity

We operate a formal equal opportunities, diversity and inclusion policy to which all employees are required to adhere and we are continuing to focus on delivering improvements in this area. This year the number of women in the Executive Team has increased from one to three, while the number of women on the Board remains at two. Further details of the policy can be found on page 32.

Development

A personalised induction programme is arranged for new directors, tailored to their specific requirements, which is designed to develop their knowledge and understanding of our operations and culture. It includes meetings with the Executive Directors, other members of the Executive Team and the Company Secretary. The programme provides an overview of our financial and operational performance, the regulatory framework, commercial and customer service perspectives.

Training

Continuous training is provided for Directors during the year by way of site visits, presentations and circulated updates. During 2016/17, the Board received performance updates from each of the Alliances, presentations from senior managers on dividends and gearing, bad debt management and derivatives as well as an informative meeting by Moody's about our credit rating. Training is also available to meet individual needs as appropriate.

Company Secretary

The Company Secretary, David Hughes, ensures that the Board receives all relevant information in a timely manner, organises induction and training programmes for new directors and facilitates the Board evaluation in years when this is conducted internally. He is also responsible for ensuring that the correct Board and committee procedures are followed and advises the Board on corporate governance matters. He will also ensure that any concerns that are raised by the Directors are recorded clearly in the Board minutes and that Directors have access to independent professional advice, at the Company's expense. The appointment and removal of the Company Secretary is a matter requiring approval from the Board.

Board evaluation

An externally facilitated Board evaluation is conducted every three years, as required by the Code, with interim reviews conducted internally by the Company Secretary. A detailed evaluation of the Board was conducted by Egon Zehnder in December 2015 and the findings presented to the Board in April 2016.

Our shareholders

Dialogue with shareholders

We engage with our shareholders on all major shareholder issues and concerns and they have a direct interest in the strong and effective governance of our business. The current structure of the Board ensures that all of the shareholders are directly represented therefore enabling a regular and open dialogue with the other Non-Executive Directors.

The Chairman, the Senior Independent Director, the CEO, CFO and Director of Strategy and Regulation and the chairs of the Board's committees are available to meet shareholders on request. The Senior Independent Director has a specific responsibility to be available to shareholders who have concerns and for whom contact with the Chairman, CEO or CFO has either failed to resolve their concerns, or for whom such contact is inappropriate.

Ownership

Our ultimate holding company is Kemble Water Holdings Limited ("KWHL") and the effective equity interests in KWHL, as at 13 June 2017 are:

Shareholders	% holding
Borealis (Farmoor Holdings BV) Borealis Infrastructure provides investment advice and investment management services to the OMERS Adminstration Corporation (OAC) with respect to global infrastructure investment opportunities, in sectors including energy, transportation and government regulated services. OAC is the trustee and administrator of the OMERS primary pension plan (and trustee of the pension funds). OMERS primary pension plan is a large Canadian public employee pension plan regulated by the Financial Services Commission of Ontario in Canada.	17.543
Hermes (BT Pension Scheme) Hermes GPE is one of Europe's leading independent specialists in global private markets. It manages the asset on behalf of the BT Pension Scheme. Hermes GPE invests in and advises on infrastructure, private equity and credit products on behalf of its clients and is specialised in co-investments, primary fund and secondary investments.	13.060
Infinity Infinity Investments S.A is a subsidiary of the Abu Dhabi Investment Authority (ADIA). ADIA manages a global investment portfolio that is diversified across more than two dozen asset classes and sub-categories.	9.900
Wren House Wren House Infrastructure Management Limited, an English limited liability company, was set up in late 2013 as the global direct infrastructure investment vehicle of the Kuwait Investment Authority ("KIA"). The KIA is the sole shareholder of Wren House. Wren House has been assigned responsibility for building partnerships, sourcing and execution of transactions, as well as asset management. Wren House's strategy is targeting the creation of a long-term focused, sustainable infrastructure platform and Wren House seeks to do so through partnership investment models for sizeable transactions where large sums of capital can be deployed.	8.772
bcIMC bcIMC is one of Canada's largest institutional investors within the capital markets. It invests on behalf of public sector clients in British Columbia and its activities help finance the retirement benefits of more than 538,000 plan members, as well as the insurance and benefit funds that cover over 2.3 million workers in British Columbia.	8.706
Cicero Investment Corporation As a sovereign wealth fund, Cicero Investment Corporation is a vehicle to diversify China's foreign exchange holdings and seek maximum returns for its shareholder within acceptable risk tolerance.	8.688
AMP Capital AMP Capital is a large global investment manager headquartered in Sydney, Australia. It is part of the AMP Group, one of Australia's largest retail and corporate pension providers and its largest life insurance provider, with most assets originating from the aligned entity.	5.530
QIC QIC is a global diversified alternative investment firm offering infrastructure, real estate, private equity, liquid strategies and multi-asset investments. It is one of the largest institutional investment managers in Australia.	5.352
Aquila Aquila GP Inc.is a leading infrastructure management firm and a wholly owned subsidiary of Fiera Infrastructure Inc, a leading investor across all subsectors of the infrastructure asset class.	4.995
Stichting Pensioenfonds ABP Stichting Pensioenfonds ABP is a pension plan sponsor. The firm provides its services to employers and employees in the government and education sectors. It invests in the public equity markets.	4.344
Optrust OPTrust invests and manages one of Canada's largest pension funds and administers the OPSEU Pension Plan, a defined benefit plan with almost 90,000 members and retirees.	4.344
QSuper QSuper is a superannuation benefits fund. The firm provides its services to employees of Queensland Government departments, authorities, and enterprises. It invests in the public equity and fixed income markets of Australia and across the globe. QSuper is managed by QIC.	3.336
AIM (PIP2 (TW) LP) Alberta Investment Management Corporation ("AIM") is one of Canada's largest and most diversified institutional investment fund managers, with an investment portfolio of approximately $90 billion.	3.258
PGGM (Stichting Pensioenfonds Zorg en Welzijn) PGGM are a pension fund service provider and manage the pensions for different pension funds, the affiliated employers and their employees.	2.172

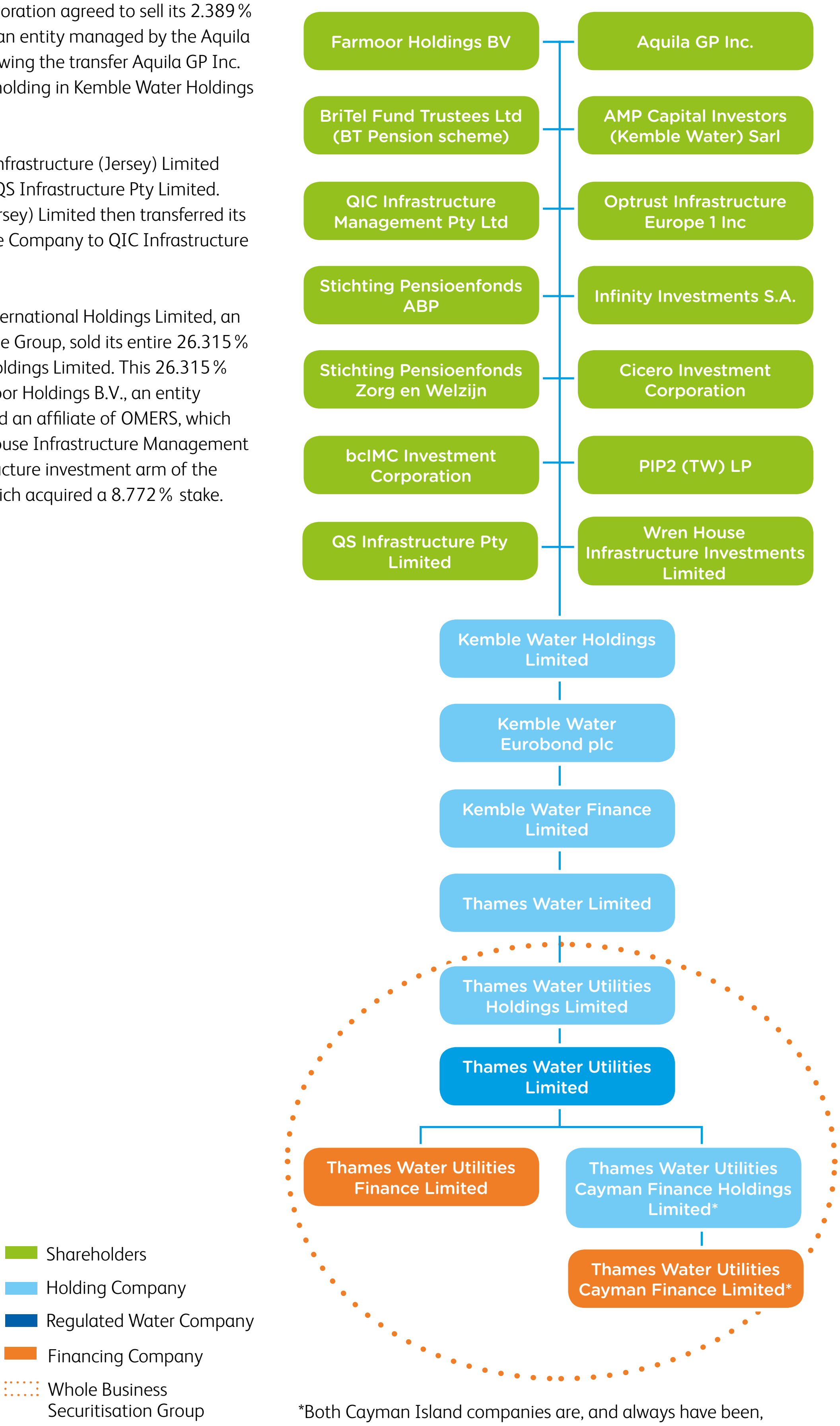
During the year and up to the date of this report on13 June 2017, the following changes to the equity interests in KWHL took place:

25 April 2017 – SAS Trustee Corporation agreed to sell its 2.389% stake to Aquila GP Inc., a Canadian entity managed by the Aquila Sonnet Limited Partnership. Following the transfer Aquila GP Inc. holds 4.995% of the total shareholding in Kemble Water Holdings Limited.

28 April 2017 – QIC Diversified Infrastructure (Jersey) Limited sold 3.336% of their interest to QS Infrastructure Pty Limited. QIC Diversified Infrastructure (Jersey) Limited then transferred its remaining 5.352% interest in the Company to QIC Infrastructure Management Pty Ltd.

31 May 2017 - Kemble Water International Holdings Limited, an entity managed by the Macquarie Group, sold its entire 26.315% shareholding in Kemble Water Holdings Limited. This 26.315% holding was split between, Farmoor Holdings B.V., an entity registered in The Netherlands and an affiliate of OMERS, which acquired 17.543%, and Wren House Infrastructure Management Limited the global direct infrastructure investment arm of the Kuwait Investment Authority, which acquired a 8.772% stake.

The structure chart below sets out the ownership of Thames Water and those subsidiaries that connect Kemble Water Holdings Limited to the regulated company, Thames Water Utilities Limited:



*Both Cayman Island companies are, and always have been, registered in the United Kingdom for tax purposes.

Accountability

Financial and business reporting

The Board is mindful of its responsibility to present a fair, balanced and understandable assessment of our position and performance, business model and strategy through the production of an annual report and financial statements and the Board is satisfied that it has met this obligation. This assessment is primarily provided in the Directors' Report on pages 100 to 103. The Statement of directors' responsibilities in respect of the Company's financial statements is set out on page 103.

Board Committees

Throughout the financial year 2016/17 Thames Water had four standing committees, each of which is described in more detail in individual reports on pages 72 to 97.

The workload of the committees includes the scheduled meetings during the year in addition to any ad hoc meetings, workshops and written updates, frequently requiring considerable amounts of time. All Directors are routinely invited to attend board committee meetings in addition to the nominated committee members.

Each of the committees has terms of reference which have been approved by the Board. These were reviewed during 2016/17 as part of the corporate governance programme and with reference to the ongoing review of the Shareholder Agreement by the Company's shareholders. The chair of each of committee provides updates to the Board on the work of their respective committees at each Board meeting. Minutes of the committee meetings are available to all Directors.

Health, Safety and Environment matters are a standing item for discussion at monthly Executive Committee meetings. Detailed reports are provided to the Board of Directors at every scheduled Board meeting.

Remuneration Committee Report
Chairman's report

Sir Peter Mason KBE
Chairman

Our approach to remuneration

I am pleased to present our 2016/17 Remuneration Committee Report. While the year has seen some significant changes to our Executive Directors, our policy and approach to Directors' remuneration has not changed. The Remuneration Committee (the "Committee") remains committed to transparency and best practice reporting and this report continues to reflect the structure of reporting required by the Listing Rules, Disclosure and Transparency Rules ("DTR") and the UK Corporate Governance Code, the UK Government's Department for Business, Energy, Innovation & Skills (BEIS) remuneration reporting regulations for listed companies and best practice guidance from Ofwat. This report sets out the information necessary to demonstrate the link between the Company's strategy, its performance and the remuneration outcomes for our Executive Directors.

Executive Director changes

We announced in the 2015/16 report that Martin Baggs (CEO) and Stuart Siddall (CFO) would be leaving the business during 2016/17. Payments on leaving were disclosed in the 2015/16 report and are detailed as appropriate below. Once again we would like to thank Martin and Stuart for their considerable contributions to Thames Water.

We also announced that Steve Robertson would succeed Martin Baggs as CEO, a role which he commenced in September 2016, while Nick Fincham was promoted to the Board as Strategy and Regulation Director in April 2016. In addition, Brandon Rennet joined Thames Water as Chief Finance Officer in March 2017, succeeding Stuart Siddall who stepped down as CFO in December 2016.

2016/17 performance and reward

As reported in the Strategic Report, it has been a difficult year for us in terms of both customer and financial performance. While it has been a challenging year for our water infrastructure, we've made good progress in complaint resolution and increased energy production while health and safety continues to deliver industry leading improvements.

This level of performance is reflected in the reward outcomes for our senior leaders. The bonus scheme applied to our Executive Directors is due to pay out at 14% of a maximum of 112.5% for the performance year 2016/17. This reflects the fact that performance outcomes for both customer and financial were below threshold at Group level.

As reported in my two previous annual reports, the LTIP payments released in 2016 and due in 2017 are the final payments from the 2010 scheme and as such reflect performance from the period 2012 to 2015. The payments calculated for the Executive Board Directors in 2015 amounted to 82.28% of salary from a maximum of 150% of salary. Nick Fincham who was in a different role during that performance period received a final outcome of 57.35% of salary from a maximum of 100% of salary. Neither Steve Robertson nor Brandon Rennet participated in the 2010 LTIP and therefore no payments have been made to them.

Approach for 2017/18 onwards

Following extensive discussions at the Remuneration Committee, the Company is reviewing all incentive structures in order to focus the leaders in the business on delivering long term sustainable improvements for customers and shareholders. While the final structures have not been agreed it is proposed that we will continue to emphasise the link between total remuneration and key customer, asset performance and financial measures.

Incentives will continue to be delivered in a mixture of short term annual management bonuses and long term incentive plans covering three year performance periods. In addition to incentive structures the Company is also reviewing the quantum payable to senior executives to ensure that these are appropriately benchmarked with comparable businesses and only pay out on delivery of improvements in performance.

Proposals have been presented to the Board and it is planned to present these in full, once agreed, on our website.

Non-Executive Director changes

Michael Pavia one of our longest serving Non-Executive Directors, announced his resignation from the Board from February 2017 after a tenure of ten years. Michael has been not only a highly effective Chair of the Audit, Risk and Regulatory Committee, but a highly valued member of the Remuneration Committee since 2010. The Committee members would like to wish Michael well in the future and thank him for the constant support combined with rigorous challenge which helped deliver some positive outcomes for the business, customers and shareholders. Nick Land joined the Board in February 2017, replacing Michael Pavia as Chair of the Audit, Risk and Regulatory Committee and as a member of the Remuneration and Nomination Committees.

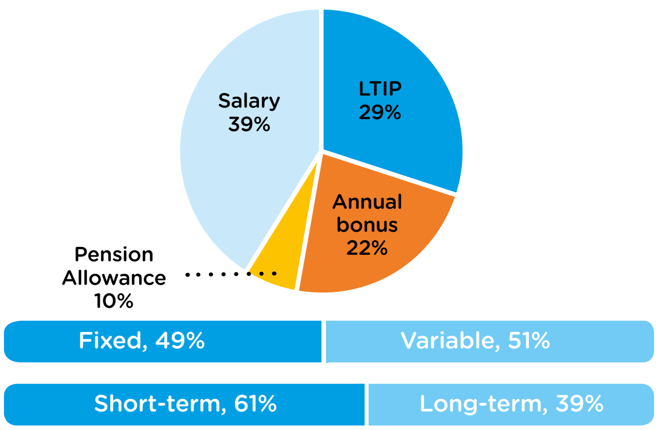
Sir Peter Mason KBE
Chair, Remuneration Committee

Our remuneration policy

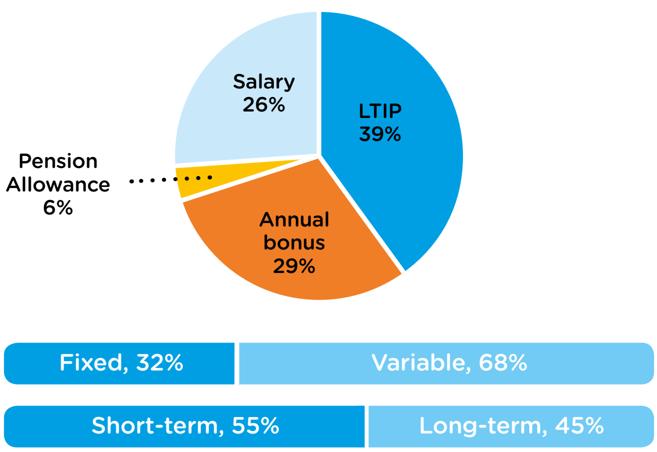
The Remuneration Committee formulates its position on remuneration policy against the following list of principles:

- the policy should promote the long-term success of the Company and ensure that it clearly links with Company strategy;
- remuneration should be aligned with the interests of the Company's stakeholders, in particular our customers and external shareholders;
- remuneration should be commensurate with packages provided by other companies of similar size and complexity, taking into account individual contribution and experience;
- the remuneration policy should establish firm links between an Executive Director's performance and the Company's performance; and
- remuneration should include a mix of fixed and variable pay comprising of basic salary plus performance related incentives.

Target Performance



Maximum Performance



Target and maximum bonus in the table above reflect the current scheme. Should there be any changes to target or maximum bonus/LTIP opportunity this will be confirmed along with scheme structure on our website following approval by the Board

Our comparator groups

There has been no change to the comparator groups agreed by the Committee in 2014/15 as part of a wider executive remuneration benchmarking review looking at both base salaries and total compensation. The comparators used are all water and sewerage companies, and other appropriately sized utilities.

This comparator group was identified as the most appropriate for the future as the selected companies either operate within similar industries, with adjustments being made for their size, or reflect the size and complexity of Thames Water.

Balancing short and long-term remuneration

Our strategy to develop an appropriate mix of short and long-term incentives and measures which drive the highest standards of performance across the Company is unchanged from previous years. As outlined above we are currently reviewing the structure and quantum of the managers' annual bonus and LTIP schemes. The proposals broadly mirror the principles of previous schemes which were specifically designed to provide a good balance of short and long-term incentives as outlined opposite.

The Remuneration Committee is carefully considering the blend of remuneration linked to our customer, health and safety, operational, regulatory and financial performance in order to produce well balanced short-term and long-term incentive plans. Fixed annual elements, such as salary, pension and benefits, are set to ensure current and future market competitiveness enabling us to attract and retain high performing executives.

The short-term incentives are used to drive performance primarily over the forthcoming year and as such proposals are being developed to focus our leaders over the next two years on the delivery of transformational programmes which will establish foundations for long term customer, asset health and shareholder value. To complement this, we are developing a new long-term incentives, measuring performance over a three year rolling basis, to encourage behaviours and performance to deliver the Company's longer term strategic goals and strong performance beyond the current regulatory period.

The Remuneration Committee will select performance conditions which are central to the Company's overall strategy and are key metrics used by the Board and Executive Team to oversee the operation of the business. Any performance targets will be proposed by management and approved by the Board through the Remuneration Committee. The Remuneration Committee believes that the performance targets for the annual bonus and LTIP are commercially sensitive and that it would be detrimental to the Company to disclose them before the end of the performance period. Our targets for 2016/17 are disclosed on page 81 of this report.

The Remuneration Committee will continue to review arrangements regularly to ensure that they remain effective and appropriate to the Company's circumstances and prospects, and to monitor the level of potential awards.

Remuneration policy details

The overall principles to the remuneration policy will remain unchanged in 2017/18 other than in relation to proposols for new bonus and LTIP schemes. New LTIP and bonus schemes are being developed which will comply with this policy by enhancing the mix of short and long-term incentives to the overall remuneration package for Executives and senior leaders. We summarise the key elements of our policy opposite.

Element of pay	Purpose and link to strategy	Operation of element	Maximum potential value and payment at threshold	Performance metrics used, weighting and time period applicable
Base salary	To attract, retain and recognise status and responsibility to deliver strategy	Base salary is paid in 12 monthly instalments during the year. Salaries are reviewed annually by the Remuneration Committee taking into account an individual's performance, the external market and internal and external economic factors. Any changes are effective from 1 July in the relevant financial year.	Annual salary increases will not normally exceed average increases for all employees. Larger increases may be applied where the Remuneration Committee considers this to be necessary e.g. changes to the scope and responsibility of a role where market conditions indicate a level of under competitiveness the Remuneration Committee judges there is a risk in respect of attracting and retaining executives. Where the Remuneration Committee exercises its discretion to recommend increases above the average for other employees, the resulting salary will not exceed the competitive market range.	Salary levels will be determined by individual performance, the external market and internal and external economic factors.
Benefits	To provide market competitive benefits consistent with role	Benefits are paid in 12 monthly instalments during the year or are benefits that are available as and when required on a one-off basis.	Benefits will include payments for car allowance, private medical insurance, life assurance, group income protection and a general entitlement to 25 days holiday. The CEO will also receive a housing allowance where appropriate.	None
Pension or pension allowance	To provide cost effective saving benefits for employees.	Payments are made in 12 monthly instalments during the year, directly to the individual or into their pension scheme.	Contribution of 25% of base salary for Executive Directors.	None
Annual bonus	To motivate and incentivise the Executive Directors to achieve the Company's key financial, customer, operational and strategic objectives through a combination of financial, customer and personal performance targets.	Annual bonuses are paid three months after the end of the financial year to which they relate. The Remuneration Committee reserves the right to reduce bonus payments if overall Company performance does not warrant payment. In addition clawback clauses are being applied for a period of two years after the payment is made.	The current scheme has an annual target of 56.25% of base salary and maximum of 112.5% of base salary. There is currently no minimum payment. Health and safety acts as an underpin whereby if performance falls below a certain level, the overall bonus pay-out would either be reduced in whole or in part. The Remuneration Committee could reduce incentive pay-outs on a discretionary basis if appropriate.	Performance measures are currently under discussion and will be published on the Thames Water website once agreed by the Board
Long-Term Incentive Plan (LTIP)	To reward performance over three year cycles, balancing the need for excellent performance in both the short and long-term.	As the Company is privately owned, the current LTIP is a cash scheme, not share based. Clawback clauses are being applied for a period of two years after the LTIP payments vest.	The current scheme has an annual target award of 75% of base salary and an annual maximum award of 150% of base salary. Award determined by performance set out in the plan and as set out by the Remuneration Committee. There is currently no minimum payment but asset health (the condition of our assets) acts as an underpin determining the proportion of the final award payable. The Remuneration Committee will retain the discretion to reduce incentive pay-outs if considered appropriate.	Performance measures are currently under discussion and will be published on the Thames Water website once agreed by the Board

Consideration of employment conditions elsewhere in the Company

The Remuneration Committee invites the HR Director to present proposals for the annual salary review for managers and employees in February along with any other changes to remuneration policy within the Company as and when they arise. The Remuneration Committee takes into account the salary increases and remuneration arrangements for the wider employee population when approving the salary increases for Executive Directors. Although employees are not consulted directly on the executive remuneration policy, employee engagement surveys are carried out on an annual basis and regular discussion takes place with union representatives on matters of pay and remuneration for employees covered by collective bargaining or consultation arrangements.

The HR Director consults with the Remuneration Committee to approve the performance targets for all bonuses and long-term incentive arrangements along with the remuneration packages offered to senior managers below Board level within the Company. The Remuneration Committee approves any payments made under these schemes to Executive Directors and also approves the levels of payments under the corporate elements of these schemes for all levels of management.

Following the successful launch of the Share in Your Success cash saving plan open to all employees in 2015, a second scheme was launched in 2016. The scheme broadly mirrors the 2015 scheme, giving all employees the option to save money, held in a savings account managed independently by Barclays bank, with the incentive of a cash bonus at the end of three years based. The cash bonus will be calculated based on each employee's level of savings, limited to a minimum of £20 and a maximum of £250 per month, and the Company's performance for customer service and EBIT. As such this scheme focuses participating employees on the same critical high level performance drivers as are in the manager's bonus scheme and long term investment. Further schemes are planned to be rolled out each year to encourage employee savings, support financial wellbeing and the focus on critical business performance.

Our approach to remuneration on recruitment

The Committee and Board approve the remuneration to be offered to Executive Directors on recruitment and takes the approach that offers will be in line with the market and that it will pay no more than is necessary to attract appropriate candidates to a role. Any new Executive Director's remuneration would include the same elements, and be subject to the same constraints, as those for existing Executive Directors (as set out on page 75 of this report).

It is not our policy to make any additional payments arising from forfeited payments from a previous employer, however, should the situation arise, it would need to be approved by the Committee. We can confirm that for the Executive Directors recruited in 2016/17 no additional payment was made for Steve Robertson (CEO), however, when Brandon Rennet was appointed on 13 March 2017 the Committee approved a payment of £600,000 mitigation for loss of bonus and LTIP payments already earned from his previous employment. This payment was made in April 2017, however since the recruitment to which the payment is linked was in the 2016/17 financial year it is reported here within this remuneration report.

Service contracts and policy on payment for loss of office

The following table sets out the key features of the service contracts for Executive and Non-Executive Directors:

Standard Provision	Policy	Details
Notice periods in Executive Director contracts	12 months' notice from Company 6 months' notice from Executive	Executive Directors may be required to work during the notice period or may be provided with pay in lieu of notice or placed on gardening leave at the discretion of the Company.
Compensation for loss of office in service contracts	Any payment as compensation for loss of office would be made at the complete discretion of the Board on recommendation from the Remuneration Committee.	In the event that the Company wishes to terminate an Executive Director's contract, other than in circumstances where the Company is entitled to summarily dismiss an Executive Director, it would need to give either, 12 months' notice or make a payment in lieu of salary. If the reason for dismissal is redundancy then the Executive Director would be entitled to a statutory redundancy payment.
Non-Executive Directors (NEDs)	No notice period. NEDs are appointed for an initial three year term. Shareholder appointed NEDs are appointed without a fixed end date.	No compensation would be payable in the event of early termination.
Treatment of unvested long-term incentive awards on termination under the plan rules	No payment unless employed on the date of vesting except for 'good leavers', death, ill-health, agreed retirement, redundancy, TUPE (Transfer of Undertakings Protection of Employment), change of control and other circumstances at the discretion of the Remuneration Committee.	Good leavers will be entitled to a payment pro-rated to the period of service during the year, in line with the specific plan rules on pro-ration. Payments will normally be made on the payment date and based on actual performance. The Remuneration Committee has discretion to recommend variations to the rules and level of vesting.
Treatment of annual bonus on termination under plan rules	No payment unless employed on the date of payment of bonus except for 'good leavers', death, ill-health, redundancy and other circumstances at the Remuneration Committee's discretion.	Leavers through ill health or death will be entitled to a bonus pro-rated to the period of service during the year. Leavers who have left through compulsory redundancy having completed the full bonus year remain eligible for a payment even if they are not employed on the payment date. Payments are made on normal payment date and are based on actual performance. The Remuneration Committee has discretion to vary the rules and level of payment. This is intended to be used only to provide flexibility in unusual circumstances.
Outside appointments	Executive Directors may accept external appointments with consent. Consideration is given to the appropriateness of the outside appointment and whether it may impact on their ability to perform the role appropriately.	The Chairman's approval must be sought before accepting an external appointment. Fees may be retained by the Executive Director for services relating to outside appointments.

Dates of Directors' service contracts/letters of appointment

The dates of the service contracts for the Executive Directors and their notice periods are set out below:

	Contract start date	Service period	Notice period
Steve Robertson, CEO	01/09/2016	n/a	6 months by employee 12 months by Company
Brandon Rennet, CFO	13/03/2017	n/a	6 months by employee 12 months by Company
Nick Fincham, Strategy & Regulation Director	01/04/2016	n/a	6 months by employee 12 months by Company
Martin Baggs CEO to 31 August 2016	05/03/2010	n/a	6 months by employee 12 months by Company
Stuart Siddall, CFO to 31 December 2016	20/09/2011	n/a	6 months by employee 12 months by Company

The dates of the service contracts for the Non-Executive Directors are set out below:

	Initial contract start date	Length of each period of appointment	Expiry date of current contract
Chairman			
Sir Peter Mason[1]	01/12/2006	3 Years	31/03/2018
Independent Non-Executive Directors			
Nick Land[2]	01/02/2017	3 Years	31/01/2020
Lorraine Baldry	01/09/2014	3 Years	31/08/2017
Dame Deirdre Hutton	22/07/2010	3 Years	21/07/2018
Michael Pavia[3]	01/12/2006	3 Years	21/07/2016
Ian Pearson	01/09/2014	3 Years	31/08/2017
Edward Richards	22/07/2010	3 Years	21/07/2018
Non-Executive Directors			
Mark Braithwaite	16/06/2015	N/A	N/A
Christopher Deacon	01/12/2006	N/A	N/A
Nicholas Horler	14/04/2014	N/A	N/A
Guy Lambert	15/10/2014	N/A	N/A
Dipesh Shah	15/10/2017	N/A	N/A

[1] Sir Peter Mason's contract expired on 1 April 2017 and was extended for 12 months

[2] Nick Land joined the Board in February 2017.

[3] Michael Pavia left Thames Water on 31 January 2017. Michael's contract was extended to ensure continuity until Nick Land's appointment.

The Chairman and Independent Non-Executive Directors have fixed appointment periods. The other Non-Executive Directors are appointed and terminated without notice by the shareholders of the Company in line with the Shareholder Agreement.

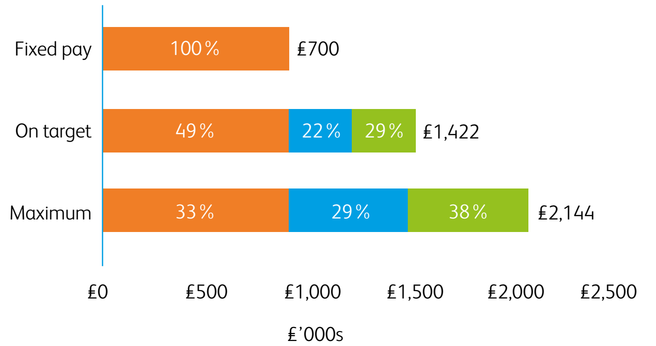
Total remuneration opportunity

The total remuneration for each of the Executive Directors that could result under different performance scenarios using the remuneration policy in 2016/17 is shown below. The following information has been reflected in the data:

- fixed pay - represents the base salary at the start of 2017/18 plus the value of pension contributions and benefits. The value of pension is a fixed percentage of the basic salary;
- on-target performance - results in 50% (56.25% of base salary) of the maximum annual bonus and 50% (75% of base salary) of the full LTIP award; and
- maximum performance - results in the maximum bonus payment (112.5% of base salary) and 100% vesting of LTIP award (150% of base salary).

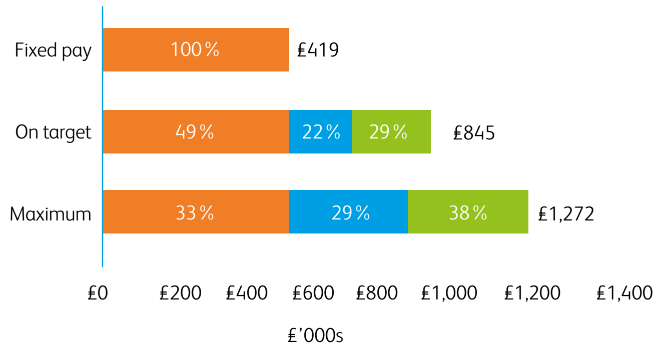
Steve Robertson – Chief Executive Officer

The chart below summarises structure of the CEO's annual remuneration package under three performance scenarios showing the value and pay mix for each.



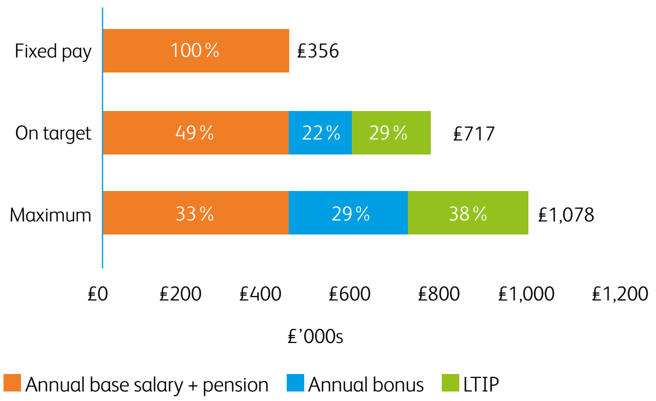
Brandon Rennet – Chief Finance Officer

The chart below summarises structure of the CFO's annual remuneration package under three performance scenarios showing the value and pay mix for each.



Nick Fincham – Strategy & Regulation Director

The chart below summarises structure of the Strategy and Regulation Director's annual remuneration package under three performance scenarios showing the value and pay mix for each.



Non-Executive Director ("NED") fee policy

Remuneration levels are set to enable us to attract NEDs who have a broad range of relevant experience and skills to oversee the performance of the Company and the implementation of our strategy. The Chairman and NED fees are proposed by the Remuneration Committee and approved by the Board. The annual fees will be paid in 12 equal monthly instalments throughout the year and are reviewed on a regular basis against those of NEDs in companies of a similar scale and complexity and requiring a similar time commitment. The fees were last reviewed in September 2015 when it was agreed that they were outside of market benchmarks, and increased with effect from 1 July 2015. There have been no further reviews of NED fees since 2015. NEDs are not eligible to receive further benefits, do not participate in any performance related arrangements and do not participate in pension plans.

Statement of consideration of shareholder views

Each year, the Remuneration Committee and Board review and approve the basic salaries, bonus scheme design, bonus payments and long-term incentive plan payments that are recommended for the Executive Directors. The Board is made up of representatives of each of the shareholders therefore their views are directly taken in to account when determining these matters.

Annual report on remuneration for 2016/17

This section has been prepared in accordance with the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. The information has been audited as indicated.

	Salary/fees		Taxable benefits		Annual bonus		LTIP		Pension related benefit		Total Group	
	£'000		£'000		£'000		£'000		£'000		£'000	
	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
Executive Directors												
S Robertson	321	n/a	7	n/a	54	n/a	-	n/a	80	n/a	460	n/a
B Rennet	17	n/a	601	n/a	-	n/a	-	n/a	-	n/a	618	n/a
N Fincham	272	n/a	13	n/a	46	n/a	103	n/a	68	n/a	502	n/a
M Baggs	203	481	24	53	-	361	-	-	51	120	278	1,015
S Siddall	251	331	12	15	-	248	-	-	63	83	326	677
Chairman												
Sir P Mason	325	325	-	-	-	-	-	-	-	-	325	325
Independent Non-Executive Directors												
L Baldry	60	57	-	-	-	-	-	-	-	-	60	57
Dame D Hutton	70	64	-	-	-	-	-	-	-	-	70	64
M Pavia	73	73	-	-	-	-	-	-	-	-	73	73
I Pearson	60	57	-	-	-	-	-	-	-	-	60	57
E Richards	60	53	-	-	-	-	-	-	-	-	60	53
N Land	11	0	-	-	-	-	-	-	-	-	11	n/a
Non-Executive Directors												
M Braithwaite	60	48	-	-	-	-	-	-	-	-	60	48
C Deacon	60	57	-	-	-	-	-	-	-	-	60	57
N Horler	60	56	-	-	-	-	-	-	-	-	60	56
G Lambert	50	50	-	-	-	-	-	-	-	-	50	50
D J Shah	60	57	-	-	-	-	-	-	-	-	60	57
Total	2,013	1,709	657	68	100	609	103	0	262	203	3,135	2,589

1. Steve Robertson joined Thames Water and was appointed to the Board on 1 September 2016. Remuneration reflects pro-rated annual salary £550,000, annual car allowance £12,500 and annual pension allowance of 25% of salary as detailed below.

2. Brandon Rennet joined Thames Water and was appointed to the Board on 13 March 2017. Remuneration reflects pro-rated annual salary of £325,000, annual car allowance of £12,500 and annual pension allowance of 25% of salary as detailed below. In addition the taxable benefits figure includes a payment of £600,000 mitigation for loss of bonus and LTIP payments already earned from his previous employment which was paid on joining as detailed in this report.

3. Nick Fincham was promoted to the Board on 1 April 2016. Remuneration reflects annual salary of £275,000 (which has been adjusted to account for unpaid leave taken), annual car allowance of £12,500 and annual pension allowance of 25% of salary as detailed opposite.

4. Martin Baggs' remuneration includes salary and benefits to 31 August 2016. Details of Martin Baggs' remuneration on departure are set out in the Payments for Loss of Office section in this report.

5. Stuart Siddall's remuneration includes salary and benefits to 31 December 2016. Details of Stuart Siddall's remuneration on departure are set out in the Payments for Loss of Office section in this report.

6. Michael Pavia resigned as a Non-Executive Director on 31 January 2017.

Of total Executive Directors' remuneration of £2,183,408 (2016: £1,691,694), £1,528,386 (2016: £1,184,186) is for the Executive Directors for their services to Thames Water Utilities Limited and has been disclosed within note 4 to the financial statements. In addition, the Executive Directors received total remuneration of £655,022 (2016: £507,508) for their services to other companies within the Kemble Water Holdings Limited Group. No operational distinction is made between services provided by the Directors to one or the other.

Additional requirements in respect of the single total remuneration figure table Base salary (audited)

Base salaries are a fixed sum payable monthly in arrears. For the Executive Directors base salaries are reviewed annually, taking into account their individual performance, the external market and internal and external economic factors, with any changes taking effect from 1 July each year. Base salaries are a fixed sum payable monthly in arrears.

Status	Name	Annual base salary 01/07/2016 (or at date of appointment, if later)	Annual base salary 01/07/2015	Percentage increase
Current Directors	Steve Robertson	£550,000	n/a	n/a
	Brandon Rennet	£325,000	n/a	n/a
	Nick Fincham	£275,000	n/a	n/a
Former Directors	Martin Baggs	£486,675	£486,675	0%
	Stuart Siddall	£335,265	£335,265	0%

Annual bonus (audited)

Performance against the bonus targets and the resulting bonuses payable to the Executive Directors in respect of 2016/17 are shown below.

Performance measures

					CEO Weighting Outcome (% of award)	CEO Max Actual £'000	CFO Max Actual £'000
Operating profit	Threshold: [678]	Target: [688]	Max [708]	Actual: [649]	25% 0%	90,234 0	n/a
Cash performance	Threshold: [183.2]	Target: [193.2]	Max [223.2]	Actual: [88.6]	25% 0%	90,234 0	n/a
Customer service (Absolute CSAT)	Threshold: [4.60]	Target: [4.64]	Max [4.68]	Actual: [4.53]	25% 0%	90,234 0	n/a
Personal Performance – transformation programme				Actual: [33%]	15% 4.95%	54,141 17,866	n/a
Personal performance – Personal objectives	Delivery of personal objectives varies by individual director.				10% 10%	36,094 36,094	n/a

The payments under this scheme will be made in July 2017 for Steve Robertson and Nick Fincham.

LTIP (audited)

No LTIP vested in 2016/17. The 2010 LTIP, which covered AMP5, was designed to pay out each year in 2013, 2014 and 2015, subject to the achievement of performance conditions. Of the final vest in 2015, this was released in three equal phases in July 2015, July 2016 with the final element due to be paid in July 2017.

Total pension entitlements (audited)

The Executive Directors are eligible to participate in the Company's defined contribution pension scheme, with the Company making contributions up to a maximum of 25% of base salary. No element of bonus or LTIP is pensionable. Executive Directors may choose to receive a cash allowance in lieu of these pension contributions. For 2016/17, Martin Baggs, Stuart Siddall, Steve Robertson, Brandon Rennet and Nick Fincham received only a cash allowance. None of the Executive Directors participates in a defined benefit pension scheme.

Status	Name	Cash Allowance in Lieu of Pension 2016/17	Cash Allowance in Lieu of Pension 2015/16
Current Directors	Steve Robertson, CEO	£80,208	n/a
	Brandon Rennet, CFO	£218	n/a
	Nick Fincham. Strategy & Regulation Director	£67,985	n/a
Former Directors	Martin Baggs, CEO	£50,695	£120,220
	Stuart Siddall, CFO	£62,862	£82,818
	Total	£261,968	£203,038

1. Brandon Rennet commenced employment on 13 March 2017 however, pension contributions commence from the last day of the month, therefore this represents one days pension contribution.

Scheme interests awarded in the year

Proposols for a new LTIP scheme are being developed and will be published following approval by the Board. As such, no scheme interests have been awarded to Executive Directors under the LTIP.

Aggregate Directors' emoluments (audited)

	2016/17	2015/16
Salaries	£1,062,522	£812,155
Taxable benefits/ allowances	£655,475	£68,000
Bonuses	£100,212	£609,424
Pension payments	£261,968	£203,038
NED fees	£949,822	£906,000
Total	£3,029,999	£2,598,577

Note: LTIPs are not deemed to be emoluments therefore they are not included within this table. Information relating to LTIPs can be found within the Single Figure for Remuneration table and LTIP section of this report.

Payments for loss of office (audited)

Martin Baggs (previous CEO) and Stuart Siddall (previous CFO) left Thames Water during the 2016/17 financial year. The details of the treatment of each individual's pay were fully disclosed in last year's remuneration report. It was agreed that each Director would receive payment in lieu of all contractual entitlements including base salary, pensions allowance and benefits plus payments for any incentives already due or lost incentive opportunity for the period up to 31 March 2017. This treatment was agreed in order to give the Company greater flexibility to identify and recruit the best candidates into the CEO and CFO roles. All payments made to the departing directors have been made in line with the Company's Remuneration Policy.

Martin Baggs

The payment to Martin Baggs as a result of his departure from the company was payment in lieu of notice (PILON) of £395,848 for the seven months from departure (31 August 2016) to 31 March 2017 (consisting of salary, benefits, pension provision and outstanding annual leave) and £638,762 in respect of lost bonus and LTIP as reported last year.

In addition to the above Martin Baggs has received the final portion of the 2010 LTIP in line with other participants, with a value of £349,690. This relates to a performance period that ended in 2014/15 and this value has already been disclosed in the remuneration report for that year.

Stuart Siddall

The payment to Stuart Siddall as a result of his departure from the company was payment in lieu of notice of £108,431 for the three months from departure (31 December 2016) to 31 March 2017 (consisting of salary, benefits, pension provision and outstanding annual leave) and £440,066 in respect of lost bonus and LTIP as reported last year.

In addition to the above Stuart Siddall has received the final portion of the 2010 LTIP in line with other participants, with a value of £246,840. This relates to a performance period that ended in 2014/15 and this value has already been disclosed in the remuneration report for that year.

Payments to past Directors (audited)

No payments were made to past Directors other than those payments made to Directors who resigned during the year and were no longer employed by the Company as at 31 March 2017.

Percentage change in CEO remuneration compared to all employees

The following shows the percentage change in CEO remuneration by comparison to all employees in the Company. This has been presented to show remuneration on a like-for-like basis to the prior year.

The calculation of the change in bonus pay-out for managers for 2016/17 against last year has been calculated by comparing the level of pay-out on the financial element of the bonus which comprises 50% of the total bonus potential.

% change 2016/17 against 2015/16			
	Annual base salary	Annual benefits[1]	Annual bonus
CEO (Martin Baggs)	0%	0%	n/a
All Employees (Manager Grade)[2]	2%	0%	-38.3%
All Employees (Non-Manager Grade)	2.2%	n/a	n/a

1 Benefits include a car allowance and private medical insurance. For the CEO this also includes a housing allowance. No bonus was paid under the 2016/17 scheme to Martin Baggs. Steve Robertson did not receive a bonus in 2015/16 to enable a direct comparison. A like for like comparison based on performance outputs for the CEO would have produced a year on year reduction in bonus of 80.4%.

2 Managers are reported separately from all employees as their pay is determined separately, employees by collective bargaining and managers through personal contracts. In addition bonus does not form part of non-manager's remuneration package. Managers below the Executive Team saw an average reduction in bonus of 38.3%. The Executive Team saw their bonus reduce by 73.8%.

Relative importance of spend on pay

The following table sets out the percentage change in operating profit, external shareholder distributions and overall spend on pay for the year ended 31 March 2017.

	2016/17	2015/16	Year-on-year change	
	£m	£m	£m	%
Operating profit	6.384	742.2	-103.8	-14.0
External shareholder distributions[1]	100.0	0.0	100.0	n/a
Total payroll costs including pensions	265.9	241.0	24.9	10.3

1. Shareholder distributions are those made to external shareholders outside of the Kemble group in respect of the relevant financial year. The Directors believe that this is the most relevant measure to use as a comparison.

Statement of implementation of remuneration policy in the following financial year

The remuneration policy will be implemented during 2017/18 as follows:

	Base salary 01/07/2017 (£'000)	Base salary 01/07/2016 (£'000)	Percentage increase (%)
Steve Robertson, CEO	550	n/a	n/a
Brandon Rennet, CFO	325	n/a	n/a
Nick Fincham, Strategy & Regulation Director	282	275.0	2.5

There have been three new appointments to the Board, Nick Fincham on 1 April 2016, Steve Robertson on 1 September 2016 and Brandon Rennet on 13 March 2017. Nick Fincham has been Thames Water's Strategy and Regulation Director since April 2011 but previously this was not a Board role. All have been appointed in accordance with the remuneration policy. Steve Robertson has been appointed on a broadly equivalent package to his predecessor, Martin Baggs, as outlined in the table below.

	Annual pension entitlement	Annual bonus maximum[1]	LTIP maximum[2]	Annual car allowance
Steve Robertson, CEO	25%	112.5%	150%	£12,500
Brandon Rennet, CFO	25%	112.5%	150%	£12,500
Nick Fincham, Strategy & Regulation Director	25%	112.5%	150%	£12,500

[1]This reflects the current bonus maximum. Any changes to scheme maximum opportunity will be communicated following approval by the Board
[2] This reflects the current LTIP maximum. Any changes to scheme maximum opportunity will be communicated following approval by the Board

Annual bonus targets 2017/18

The structure, quantum and performance targets for the annual bonus for 2017/18 for Executive Directors are currently under review. While we do not publish targets until after the performance year, full disclosure of the new scheme's structure, quantum and weightings will be published on our website once agreed by the Board.

Performance measures for long-term incentives to be awarded in 2017/18

The structure, quantum and performance targets for the 2017 LTIP scheme for Executive Directors are currently under review. As with the Company bonus scheme, specific performance targets are deemed to be commercially sensitive and will not be disclosed before the end of the financial year but outcomes against these targets will be disclosed on vesting of the award in 2020. Full disclosure of the new scheme's structure, quantum and weightings will be published on our website once agreed by the Board.

NED annual fees (audited)

The Chairman and NEDs receive a fixed fee for their duties which reflects their responsibilities and time commitments. They are not entitled to any annual bonus, long-term incentives, pension benefits or benefits in kind. There are no changes to the fee rates for 2017/18, which are set out below for reference.

	Total annual fees 01/07/2017	Total annual fees 01/07/2016	Percentage increase (%)
Chairman	£325,000	£325,000	0
Independent NED / NED (non-committee member)	£50,000	£50,000	0
Independent NED / NED (committee member)	£60,000	£60,000	0
Chair of the Customer Service Committee[1]	£70,000	£70,000[1]	0
Chair of the Audit, Risk and Regulatory Committee[2]	£75,000	£75,000[2]	0

[1] This is the normal Non-Executive Director fee plus an additional £10,000 in respect of services as a committee member, plus an additional £10,000 in respect of services as Chair of the Customer Service Committee.
[2] This is the normal Non-Executive Director fee plus an additional £10,000 in respect of services as a committee member, plus an additional £15,000 in respect of services as Chair of the Audit and Regulation Committee

Consideration by the Directors of Matters Relating to Remuneration Committee members and attendance

The Remuneration Committee is chaired by Sir Peter Mason and consists of two further independent Non-Executive Directors and two Non-Executive Directors. They are appointed to the Committee on an ongoing basis. The following table sets out the attendance of the members of the Committee during the year.

Committee Member	Number of Meetings during Term	Number of Meetings Attended
Sir Peter Mason (Chair)	5	5
Michael Pavia (resigned 06/02/17)	4	4
Christopher Deacon	5	5
Ian Pearson	5	5
Mark Braithwaite	5	4
Nick Land (appointed 06/02/17)	1	1

Committee's key activities and responsibilities

The Committee's activities cover a range of subjects including succession planning, people strategy and Executive Director remuneration. They are also responsible for recommending the structure of other aspects of remuneration for all employees, including setting a budget for employee pay reviews, reviewing the appropriateness and effectiveness of employee benefits including pensions and the structure of annual and long-term incentive arrangements for managers.

For this reporting period, the following remuneration activities in respect of Senior Executives were carried out by the Remuneration Committee:

Meeting	Activities
April 2016	• Review of bonus targets for 2016/17 • Update on pension scheme challenges for 2016/17 • Review of draft Remuneration Report
May 2016	• Review of performance against targets for the 2015/16 bonus and 2015 LTIP targets • Review of proposed structure, performance measures and appropriate weighting for the 2015 LTIP scheme • Review of executive pay • Final review of draft of Remuneration Report
September 2016	• Review of people strategy • Further review of 2016 pension scheme and valuation • Update on employee pay negotiations
November 2016	• Further review of Executive Director pay • Further update on 2016 pension scheme valuation and challenges • Final update on employee pay negotiations
February 2017	• Review of Gender Pay and Statutory Reporting in 2017 • Further update and proposals on 2016 pension scheme valuation • Review of performance against targets for the 2016/17 bonus targets • Review of performance against targets for the 2015 LTIP targets • Review of proposed structure, performance measures and appropriate weighting for the 2017/18 bonus and 2017 LTIP schemes • Review and approval of Pay Review budget

Advisors to the Remuneration Committee

PricewaterhouseCoopers LLP are retained by the Committee as independent advisers. During the year no services were provided to the Remuneration Committee and as such no fees were paid in the year.

This year's remuneration reporting has been prepared in accordance to the remuneration reporting regulations which came into effect on 1 October 2014, and is compliant with UK listing rules, as required by Ofwat as part of our operating license.

The Remuneration Committee report was approved by the Board on 13 June 2017, and signed on its behalf by:

Sir Peter Mason KBE
Chairman

Nominations Committee Report
Chairman's report

Sir Peter Mason KBE
Chairman

This year has been a very busy year for the Nominations Committee with considerable time spent on the search for a new Chief Financial Officer ("CFO"), to replace Stuart Siddall and a new Independent Non-Executive Director ("INED"), to replace Michael Pavia. In addition at the beginning of the year we completed our search for our new Chief Executive Officer, Steve Robertson.

In the search for a new CFO the Company engaged the services of Spencer Stuart to work alongside the Committee. As previously reported Egon Zehnder were engaged to assist with the recruitment of a new Independent Non-Executive Director to replace Michael Pavia.

Following a successful search we recruited Brandon Rennet as CFO and Nick Land as the new INED and their biographies can be found on pages 55 and 56.

Following the sale of the Macquarie managed stake to Borealis Infrastructure, the infrastructure investment manager of OMERS, Mark Braithwaite resigned as a Director on 31 May 2017 and we welcomed Kenton Bradbury in his place.

As previously reported, given the number of Board changes that took place during the year and to ensure continuity, it was agreed with the Board in June 2016 that I would extend my current contract for a further 12 months until March 2018. The search for my replacement will be undertaken by a specifically constituted committee, the Independent Chairman Nominations Committee, which will look to identify and recommend to the board a suitable successor.

Composition and meeting attendance

Membership of the Committee during 2016/17 was:	Independent	Meetings attended/ eligible meetings
Sir Peter Mason (Chair)	Yes	5/5
Mark Braithwaite (Resigned 31/05/17)	No	4/5
Christopher Deacon	No	5/5
Nick Land (appointed 06/02/17)	Yes	1/1
Michael Pavia (resigned 06/02/17)	Yes	4/4
Ian Pearson	Yes	5/5

Main duties

The main duties of the Committee are:

- to review, from time to time, the structure, size and composition of the Thames Water Utilities Limited Board and its committees and to make recommendations to the Board with regard to any adjustments that are deemed necessary;
- to keep under review the leadership needs of the Company and to satisfy itself that plans are in place for orderly succession for appointments to the Board so as to maintain an appropriate balance of skills and experience on the Board;
- to review the proposed recommendation of any individuals for the appointment to the post of Executive Director or Non-Executive Director; and
- to review the recommendations of the CEO in relation to the appointment of all senior executives and senior management of the Group (other than in relation to the CEO, which shall be a matter for the Committee to review).

The Committee's terms of reference are available on our website.

Appointment of Brandon Rennet

June 2016 – search decision

Following Stuart Siddall's announcement that he would retire in December 2016, the Committee commenced a search of potential candidates and appointed Spencer Stuart to carry out that search.

August 2016 – review of long list

The Chairman, CEO and Janet Burr, HR Director reviewed a long list of candidates researched by Spencer Stuart who had confirmed their interest in the role. The Committee identified selected candidates for interview.

September 2016 – interview process

The shortlisted candidates were interviewed by the CEO, Chairman and Janet Burr, HR Director. The final two candidates were interviewed by a panel from the Committee.

November 2016 – selection decision

Following feedback from the interviews, Brandon Rennet was identified as the preferred candidate and the Committee recommended his appointment to the Board.

November 2016 – announcement

Brandon's appointment was announced.

Audit, Risk and Regulatory Committee Report

Chairman's report

Nick Land
Chairman

I am pleased to present our Audit, Risk and Regulatory Committee (the "Committee" or "ARRC") report which describes our activities and areas of focus during the year.

I joined the Committee on 6 February 2017, replacing Michael Pavia as Chairman. I would like to thank Michael, on the Committee's behalf, for the considerable amount of work that he undertook during his tenure.

As we move into the year ahead, the Committee will continue to consider all aspects of audit, risk and regulatory matters on behalf of the Company, but with an increased focus on the emerging General Data Protection Regulations, that will come into force in 2018 and our plans for PR19.

Membership

Nick Land became Chairman of the ARRC on 6 February 2017 succeeding Michael Pavia who resigned from the Board on the same date. Nick has extensive financial and accounting experience and the Board regards Nick as the member of the Committee possessing recent and relevant financial experience.

Our external auditors, KPMG LLP ("KPMG"), CEO, CFO, Director of Strategy and Regulation, Head of Audit and Assurance, the Group Financial Controller and Company Secretary are invited to attend all meetings in order to ensure that all the information required by the Committee for it to operate effectively is available. Other members of the Thames Water senior management team attend by invitation when appropriate. In conjunction with each meeting, the external auditors hold a private session with the Committee without Thames Water management being present.

Further biographical details of the members are set out on pages 55 to 59.

Committee composition and meeting attendance

Membership of the Committee during 2016/17 was:	Independent	Meetings attended/ eligible meetings
Nick Land (Chair) (appointed 06/02/17)	Yes	1/1
Lorraine Baldry	Yes	7/7
Mark Braithwaite * (resigned 31/05/17)	No	4/7
Christopher Deacon	No	7/7
Ian Pearson	Yes	7/7
Dipesh Shah	No	6/7
Ed Richards	Yes	5/7
Michael Pavia (resigned 06/02/17)	Yes	6/6

*Although Mark Braithwaite was unable to attend a number of meetings during the year, he was provided with an update on the items discussed by the Chairman and attended separate meetings with KPMG.

Responsibilities

The Committee has primary responsibility for exercising oversight over the accuracy and completeness of the financial statements and for reviewing any matters of significance affecting the regulation of the Company. In addition, it is responsible for monitoring compliance with the risk management framework applied by the Board for financial operational matters. In this role, the Committee oversees the internal audit function and approves its annual plan.

The Committee will advise the Board on matters falling within the scope of its responsibilities. Such advice may be in the form of minutes of its meetings, supporting papers and written and oral reports at Board meetings.

The main responsibilities of the Committee are:

Financial reporting

- to exercise oversight over the accuracy and completeness of the Annual Report and Financial Statements ("AR&FS") and the Annual Performance Report ("APR"), including advising the board on whether the AR&FS and APR present a fair, balanced and understandable view of the Company;

- to ensure the AR&FS and APR give a true and fair view of the Company's results and are in compliance with financial reporting requirements, regulatory accounting guidelines and corporate governance; and

- to ensure that accounting policies, practices and disclosures are appropriate and assess whether the key estimates and judgements made by management are reasonable.

External auditor

- to review the effectiveness of the external auditor;

- to make recommendations to the Board on the appointment of the auditor to agree the fees paid to the auditor and to be responsible for the tender of the audit from time to time; and

- to review the scope and results of external audits.

Internal audit and controls

- to promptly review reports of the Company from the internal auditors; and

- to monitor and review the effectiveness of the Company's internal audit function in the context of the Company's overall risk management systems.

Whistleblowing and fraud

- to review the Company's arrangements for whistleblowing, reporting fraud and other unethical or inappropriate behaviour; and

- to ensure that arrangements allow proportionate and independent investigation of such matters and appropriate follow up action.

Regulatory, compliance and assurance

- to review the governance, policy and strategy of decisions with regulatory implications;

- to review guidance on current, emerging and future regulatory matters and advise the Board on regulatory strategy;

- to review the Company's progress in delivering against the regulatory outputs as established through the regulatory price review process;

- to review the assurance arrangements for the reporting of regulatory data as required by Ofwat under its Company Monitoring Framework; and

- to oversee the preparation of formal regulatory publications and submissions including those relating to price determinations, regulatory commitments, Ofwat action plans, and consultations.

Key activities

The ARRC was engaged with senior management in relation to a number of matters during the year, receiving presentations and participating in workshops.

The table sets out the Committee's core agenda at every meeting and certain key matters of focus that were considered during the year.

Core agenda

- Top company corporate risks
- Data Protection updates
- Strategy & Regulation reports and updates
- Audit and Assurance reports

Meeting	Key matters considered
June 2016	Reviewed and recommended to the Board the Financial Results 2015/16 and Annual Performance Report 2015/16 Received an update on the Company's approach to market disclosure Received a presentation from KPMG regarding findings from the external audit Treasury – refinancing plan Deep dive on cyber security risks Received a report on retail non-household price control Received an update on Water 2020
September 2016	Reviewed the KPMG external audit plan for 2016/17 Deep dive on Wholesale Waste risks Deep dive on Wholesale water risks Treasury – Annual Debt Prospectus C17 interim assurance letter*
November 2016	Interim Financial Results including going concern review KPMG report – review of interim financial statements Statement of Risks, Strengths and Weaknesses and draft assurance plans Received an update on the internal audit plan for 2016/17 Deep dive on Strategy & Regulation risks Deep dive on Finance & Business Services risks
January 2017	Market readiness update Business planning update Received an update on new IFRS Received the KPMG controls report C17 final assurance letter* Deep dive on Health, Safety & Wellbeing risks Reviewed and approved the internal audit plan for 2017/18 Reviewed and approved the revised Internal audit charter Reviewed and approved the Statement of Assurance
March 2017	Year-end financial reporting update Received an update from KPMG on the controls' audit Deep dive on Commercial risks Deep dive on HR risks Received an update on strategic business planning Received an update on market readiness Reviewed and approved the Committee's Terms of Reference

*The Committee held two workshops during the year to approve the Interim and Final Assurance letters in relation to the programme of activities to enable market opening of the non-household Retail market in April 2017. In addition the Committee held a workshop on derivatives and whole business securitisation.

Significant financial statement reporting issues

The Committee considered the integrity of the 2016/17 Annual Report and Financial Statements of the Company. In undertaking this review, the ARRC discussed the critical accounting policies and judgements applied with management and the external auditors, including meetings with KPMG without members of management being present. It discussed a report from KPMG identifying the significant accounting and judgemental issues that arose in the course of the audit. The ARRC also considered the management letter for issues and judgements raised and is monitoring action taken by management as a result of a number of audit recommendations.

After discussion with both management and the external auditor, the ARRC reviewed work on the following key estimates and judgements within the Company's financial statements. Based on the Committee's review of papers presented, it is satisfied on the appropriateness of the basis for key judgemental areas. In reaching this conclusion the members of the Committee also considered the responses received to their questions and the reporting provided by KPMG in these judgemental areas.

The matters below relate to the key estimates and significant judgements reviewed by the ARRC in respect of the financial statements for the year under review.

Significant judgements	Action taken
Bad Debt provision The level of bad debt provision recognised by the Company, including the judgemental impact of the level of historic and current cash collections, the effect of cancelling billings on expected debt recovery (for example where the property occupier has moved without informing the Company or where the Company was unable to invoice for a period of time when the property was unoccupied) and the levels of debtors due to be collected on the Company's behalf (Water-only Company and non-household debtors)	The Committee reviewed management's key assumptions underlying the bad debt provision via reviews of papers presented by management on the topic throughout the year, including a review of the debtors' ageing and the basis for cash collection and write-off rates in the year. The Committee also reviewed a number of reports from KPMG in relation to the work they had undertaken. Based on this review, the Committee was satisfied that potential bad debt was adequately provided for in the financial statements. The Committee acknowledged the change in risk profile for non-household debt, following the Company's announcement to transfer its non-household retail customers to Castle Water.
Management's judgment of the completeness and valuation of the provisions in relation to potential legal and regulatory claims and other matters	The Committee reviewed the levels of provisions held by the Company throughout the year, questioning and challenging the basis for such provisions. The Committee was provided with details of the main assumptions around the recognition and valuation criteria applied over provisions. The Committee also received a report from KPMG on their audit work in respect of provisions. Based on the reviews and report the Committee concurred with the level of provisions made.
Capex Vs Opex Given the significant investments that the Company makes in maintaining and improving its network infrastructure the allocation of such expenditure between capital and operating costs is a critical area	The Committee has reviewed the classification of costs within the financial statements, gained an understanding of the key investment projects and year-on-year movements. The Committee also reviewed reports on the audit work KPMG has undertaken in this area. Based on these reviews and discussions with both management and KPMG, the Committee has deemed the classification of expenditure as appropriate.

Review of annual financial statements

Prior to the 2016/17 Annual Report and Financial Statements being presented to the Board for formal approval, the ARRC, at the request of the Board, considered whether the Annual Report and Financial Statements is fair, balanced and understandable and whether it provides the necessary information for all stakeholders to assess the Company's position and performance, business model and strategy. The ARRC considered the consistency of accounting policies across the Company; the methods used to account for significant or unusual transactions; whether the Company had followed appropriate accounting standards; and whether the Company had made appropriate estimates and judgements, taking into account the views of KPMG LLP. The ARRC further considered whether appropriate disclosure had been made in the financial statements, the Strategic Report, Directors' Report and the Corporate Governance Report.

Based on consideration of the above items and the other work performed by the ARRC, the Committee advised the Board that, taken as a whole, the Annual Report and Financial Statements is fair, balanced and understandable and provides the information necessary for stakeholders to assess the Company's position and performance, business model and strategy.

External audit

The Committee is responsible for overseeing relations with the external auditors, including the approval of fees, and makes recommendations to the Board on their appointment and re-appointment.

In 2016/17 the Committee oversaw the relationship with KPMG including (but not limited to) whether fees for audit or non-audit services were appropriate. The Committee reviewed KPMG's terms of engagement, the scope and execution of their audit work. The Committee assessed the independence and objectivity of the external auditors, taking into account relevant UK professional and regulatory requirements and the relationship with the auditors as a whole, including the provision of any non-audit services in accordance with the Policy for the Provision of Non-Audit Services.

Auditor independence and objectivity

The independence of the external auditors is essential to the provision of an objective opinion on the true and fair view presented by the financial statements. Auditor independence and objectivity is safeguarded by reviewing the nature and value of non-audit services performed by the external auditors, ensuring that employees of the external auditors who have worked on the audit in the past two years are not appointed to senior financial positions within the Company and the rotation of the lead engagement partner at least every five years and key audit partner every seven years. The current lead engagement partner has held the position for two years, and has been a key audit partner for two years.

To support independence KPMG use a separate audit team to audit Thames Water Commercial Services Limited ("TWCSL"), a subsidiary company, which, up until 31 March 2017, was required to have an arm's length relationship with Thames Water Utilities Limited.

Following the transfer of TWCSL's customers to Castle Water during 2016/17, this company no longer requires the use of a separate audit team.

The ARRC met with KPMG on several occasions during the year without management present providing the external auditors with the opportunity to raise any matters in confidence. In addition, the Chair of the ARRC met privately with KPMG.

Following this year's annual review, the ARRC is satisfied with the effectiveness, independence and objectivity of KPMG LLP.

Non-audit services

To safeguard the objectivity and independence of KPMG, approval from the Committee Chairman is required for any services provided by the external auditor for which the fee is likely to be in excess of £100,000. As part of this process the Committee ensures that the external auditors are not permitted to perform any work that they may subsequently need to audit, or which could create a conflict of interest or constitute a breach of the external auditor's independence and objectivity. Non-audit services are normally limited to assignments which are closely related to the performance of the audit or where detailed knowledge of the Company is necessary for its completion.

Details of the fees paid to the external auditor during the year ended 31 March 2017 for audit and non-audit services are set out below and in note 3 to the statutory financial statements.

Total fees for audit and non-audit services incurred during the year amounted to £1 million (2016: £2.1million).

	2017 £'000	2016 £'000
Fees payable for the audit of the Company's financial statements	397	374
Fees payable to the Company's auditor for other services:		
Audit related assurance services	170	155
Other assurance services*	403	755
Other tax advisory services	14	16
Corporate finances services		570
Other services	80	224
Total aggregate remuneration	**1,064**	**2,094**

*Other assurance services include £0.3million (2016: £0.5million) related to external assurance work performed in the review of the Company's non-financial reporting submissions, specifically the reporting of the Company's 'Performance Commitments'. A separate team from KPMG, with the appropriate skills and qualifications to deliver this work, is in place. Their work is considered complementary to the external audit work undertaken by KPMG.

The Committee considered the level of non-audit fees and safeguards put in place relating to non-audit work, including written representations from KPMG which confirmed their independence, and was satisfied that the non-audit fees incurred have not resulted in a loss of independence or objectivity of the external auditor.

Audit appointment

The Company adopts the same approach to audit tendering as a FTSE 100 company ensuring the Company's compliance with the 2014 UK Corporate Goverance Code and the reforms of the audit market by the UK Competition and Markets Authority. In alignment with the EU regulatory framework for statutory audit the Company plans to operate a ten-year tender process for its auditors, however the ARRC may recommend that the Company puts the audit out to tender at any time, based on the results of the assessments of auditor independence and audit quality outlined above. KPMG were appointed after a competitive tender for the 31 March 2009 financial year end audit. There are no contractual obligations restricting our choice of external auditors and no auditor liability agreement has been entered into by the Company. For the financial year ended 31 March 2018 the ARRC has recommended to the Board that KPMG be re-appointed.

Internal audit

The Committee monitored and reviewed the effectiveness of the Company's internal audit function in the context of the Company's overall risk management systems. In particular, in 2016/17 the Committee considered and approved the remit and activities of the internal audit function ensuring that it had adequate resources and appropriate access to information to enable it to perform its function effectively, in accordance with the relevant professional standards and was free from management or other restrictions.

The Committee reviewed and assessed the annual internal audit plan which contains a mix of risk based and cyclical reviews. The plan is delivered through appropriately skilled and qualified internal resources supported with external resources where more specialised skill sets are required, typically within Information Systems and Treasury.

Inputs to the plan include principal risks, corporate priorities and objectives, external research and benchmarking of emerging risks and trends and discussions with members of the Executive Team and Senior Leadership Group.

The plan is approved by the Committee in January each year with focus given to not only the areas which are being covered but also those that are not, to ensure that the plan aligns with the Committee's view of risks.

During the year the Committee considered reports on the Company from the internal auditors, including management's responsiveness to the findings and recommendations of the internal audit team. The Committee Chairman discussed high priority issues directly with the relevant members of management to ensure he had a thorough understanding of the matters raised and the process for resolution and held private meetings with the internal auditors.

Internal control, risk and compliance

The Board has overall responsibility for the Company's risk management framework and systems of internal control. These systems are designed to manage, rather than eliminate the risk of failure to meet business objectives and can only provide reasonable, not absolute, assurance against material misstatement or loss. The key features of the systems of internal control and risk management are:

- a control environment with clearly defined organisational structures operating within a framework of policies and procedures;
- comprehensive business planning, risk assessment and financial reporting procedures, including the annual preparation of detailed operational budgets for the year ahead and projections for subsequent years;
- regular monitoring of risks and control systems throughout the year, supported by the use of risk registers;
- an annual self-certification process requiring senior management to report on the effectiveness of internal controls in operation within their business area, identify opportunities for improvement and to propose and implement remedial action where required;
- an internal audit function providing independent scrutiny of internal control systems and risk management procedures;
- a governance model whereby our Board delegates responsibility for certain matters to a number of committees in line with best practice; and
- review of reports produced by internal and external audit.

The ARRC routinely reviews the effectiveness of the systems of internal control and risk management, principally by means of reports in respect of the above activities and makes reports to the Board thereon.

The Company's risk management process is designed both to identify emerging risks and to minimise the adverse impact of emerging and existing risks through mitigating actions.

Each business area is responsible for managing its risks and maintaining a risk register. Significant risks are escalated and reviewed by the Executive Team and Senior Leadership Group through the Risk, Opportunities and Controls Committee. The Risk, Opportunities and Controls Committee is chaired by Nick Fincham, Director of Strategy and Regulation, on a rotational basis so that the approach to risk management is regularly refreshed.

The ARRC kept the adequacy and effectiveness of the Company's internal controls and risk management systems under review in 2016/17. The ARRC approved for recommendation to the Board the statements to be included in the 2016/17 statutory and regulatory reports concerning internal controls and risk management. The Committee reviewed the risk management strategy approved by the

Board and was satisfied that the Board received regular reports on internal controls from management.

The ARRC ensured that there were clear reporting lines for all issues associated with risk management and reviewed the adequacy of structures, processes and responsibilities for identifying and managing key risks facing the organisation. The Committee was satisfied that appropriate work was undertaken developing the maturity of risk management.

The ARRC reviewed the principal risks and uncertainties appearing on pages 42 to 50.

Regulatory matters

In line with its responsibility to assist the Board in reviewing current and future regulatory matters, the Committee considered a number of key regulatory developments over the course of the year, and oversaw the preparation of a number of formal regulatory publications and submissions.

Key regulatory matter	How the issue was addressed by the Committee
Non-Household Retail Market Readiness	Throughout the year, the Committee oversaw the Company's readiness for the opening of the retail non-household market on 1 April 2017. This included reviews of key milestones in the process, the associated assurance requirements, the status of internal arrangements and the exit of the non-household retail market by transferring non-household retail activities to Castle Water. Outside the formal calendar of meetings, additional workshops were arranged for members of the Committee in support of the Board Assurance Letter process. The Committee reported to the Board and recommended approval of the interim letter of assurance (October 2016) and final letter of assurance (February 2017).
Household Retail Competition	The Committee monitored developments in the area of household retail competition, with a specific focus on Ofwat's review of the costs of household retail competition. The Committee reviewed Ofwat's emerging findings, as published in June 2016, our subsequent response, in August 2016, and Ofwat's final report, published in September 2016.
Water 2020	Throughout the year the Committee reviewed developments in the area of Ofwat's design decisions for PR19 as part of its Water 2020 programme of work. In particular, the Committee considered Ofwat's position that certain design decisions for PR19 would require licence amendments to be made. The Committee monitored developments in this area, reviewed the proposed licence changes contained in Ofwat's consultation of 9 November 2016, and recommended to the Board that it approve the proposed changes at its meeting of 23 November 2016.
Strategic Business Planning	Over the course of the year, the Committee oversaw developments in the area of strategic business planning. This included the development of the Corporate Strategy and longer-term planning, which will be used to inform the PR19 regulatory price review.
Licence Simplification	In addition to the Water 2020-related licence amendments referenced above, during the year, the Committee oversaw other developments in the area of the company's Instrument of Appointment ("licence"). In particular, the Committee considered Ofwat's licence simplification project, aimed at both simplifying and updating the content of company licences. The Committee also recommended the Board's approval of licence amendments relating to the Wholesale Revenue Forecasting Incentive Mechanism (WRFIM), which the company confirmed to Ofwat on 9 November 2016.
2016 Retail Non-Household Price Control	The Committee oversaw the preparations for the 2016 retail non-household price control. This included reviewing Ofwat's statement of method, and the status of internal preparations including assurance and governance arrangements, ahead of the PR16 submission on 20 July 2016. The Committee monitored the status of the Draft and Final Determinations ahead of retail exit, and the transfer of the retail non-household business to Castle Water.
2017/18 Wholesale and Retail Charges	The Committee oversaw the development of the Company's 2017/18 charges. This included consideration of the regulatory environment (including developments in the scope of Ofwat's duties), the timeline for establishment of the charges, and the associated assurance and governance approach. The Committee was also presented with information on indicative bill impacts for a range of typical unmetered, assessed and metered household and non-household customers.
London Asset Health Response to Ofwat	Ofwat wrote to us on 20 December 2016 and 9 February 2017 requesting information relating both directly and indirectly to our water infrastructure assets, with a particular focus on our London water mains (including trunk mains). The Committee reviewed responses to Ofwat's enquiries and provided comments prior to its approval by the Board and has committed to oversee the delivery of the commitments made.

We run numerous workshops with our customers to better understand their needs.

Customer Service Committee Chairman's report

Dame Deirdre Hutton DBE
Chairman

Following the appointment of Steve Robertson, our new Chief Executive Officer, the Customer Service Committee has seen a renewed focus on providing excellent service to our customers.

We continue to make good progress but we also recognise that we still have work to do to achieve consistent excellent customer service. We remain confident that the work currently being undertaken by the Committee will benefit the delivery of the commitments we have made to our customers.

Kelly Macfarlane, our new Managing Director, Customer Service and Retail has undertaken a detailed and in-depth view of the current challenges for customer service. A programme of work and supporting roadmap has been agreed to enable the delivery of our customer service ambitions. This is already driving tangible improvements in the quality of communications and support for customers who have been affected by major disruption to their water and waste water services. A social media team now provides a 24/7 service and a dedicated team of customer representatives are in place to provide on-site face to face support and customer care.

Going forward, the Committee will continue to challenge and support the business to deliver against the roadmap and commitments to ensure that the customer is at the heart of everything we do.

Composition and meeting attendance

Membership of the Committee during 2016/17 was:	Independent	Meetings attended/ eligible meetings
Dame Deirdre Hutton (Chair)	Yes	4/4
Lorraine Baldry	Yes	4/4
Nick Horler	No	3/4
Dipesh Shah	No	3/4
Ed Richards	Yes	2/4

Our CEO, CFO, Director of Strategy and Regulation, Managing Director, Customer Service and Retail and Company Secretary are invited to attend all meetings in order to ensure that all the information required by the Committee for it to operate effectively is available. Other members of the Thames senior management team attend by invitation when appropriate.

Role of the Committee

The core activities of the Committee are to review, advise and challenge across a number of areas including operational performance, strategy and customer consultation and engagement. The main objectives of the Committee include the following areas:

- performance – the review of current Company position and performance against industry comparators and external best practice companies;
- strategy – reviewing the development of the customer service strategy reflecting the opportunities and challenges faced by the Company over the next five years: and
- customer consultation and engagement – to review and advise on the proposed communications approach and channels with consumers and customers.

Activities

During the year, the Committee reviewed the regular key performance measures and assessed certain areas focusing on revenue, wholesale water, wholesale wastewater and the Technology and Transformation Alliance.

During the year, deep dives into the following subjects were conducted:

- Thames Water brand refresh;
- Customer immersion for customer-facing employees – Here for Customers;
- Customer insight and analysis informing Thames Water's approach to PR19 planning;
- Winter readiness – plans in our water and wastewater units; and
- Annual Billing process

Other items reviewed by the Committee during the year included the operational model work completed in our wastewater division to improve the customer experience of blockage events, customer engagement strategy for PR19 and plans to improve customer management systems stability and resilience. In addition Dame Deirdre visited our new customer solutions centre in Slough that brings together our expert customer service teams from Thames Water and Lanes that are working in tandem to support the customer service improvements in our wastewater business.

Directors' Report

Directors' Report

The Directors present their annual report and the audited financial statements for the year ended 31 March 2017. These are the Company's statutory accounts as required to be delivered to the Registrar of Companies. This Directors' Report includes certain disclosures required under the Companies Act 2006.
The Directors consider that the annual report and the audited financial statements, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

The Directors have carried out a robust assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity, and details of these risks and their management or mitigation can be found on pages 42 to 50.

The Directors have voluntarily complied with the Disclosure and Transparency Rules ("DTR"), to the extent that these can be reasonably applied to the Company. The Company is required, under its licence, to publish information about its results as if it were a company with a Listing on the London Stock Exchange. Consequently, the Company has prepared Corporate Governance, Remuneration Committee and Audit, Risk and Regulatory Committee reports included within this Annual Report.

Corporate Governance

The Company's compliance with the UK Corporate Governance Code is reported on page 64.

Directors

The current Directors of the Company, including their biographical details can be found on pages 55 to 62. Details of the Directors' remuneration, service contracts and any interest in the shares of the Company are included within the Remuneration Committee report on pages 72 to 85.

During the year, Martin Baggs stepped down as Chief Executive Officer on 31 August 2016, Stuart Siddall retired as Chief Financial Officer on 31 December 2016, Michael Pavia stepped down as Senior Independent Director on 6 February 2017 and Mark Braithwaite resigned as Non-Executive Director on 31 May 2017.
Nick Fincham was appointed to the Board as Director of Strategy and Regulation with effect from 1 April 2016, Steve Robertson joined the Board as Chief Executive Officer on 1 September 2016, Nick Land, Independent Non-Executive Director and Chair of the Audit, Risk and Regulatory Committee and Brandon Rennet, Chief Financial Officer joined the Board on 6 February and 13 March 2017, respectively. In addition, Kenton Bradbury joined the Board as a Non-Executive Director with effect from 31 May 2017.

Branches

The Company does not have any branches outside of the UK.

Share Capital

As at 13 June 2017, the Company's issued share capital was 29,050,000 ordinary shares of £1 each amounting to £29,050,000. There were no movements in the Company's share capital during the year.

Dividends

The Company's dividend policy is to pay a progressive dividend commensurate with the long-term returns and performance of the business, after considering the business' current and expected regulatory and financial performance, regulatory restrictions, management of economic risks and debt covenants. Directors, in assessing the dividend to be paid (to a maximum of statutory distributable reserves), are required to ensure that:

- sufficient liquidity is maintained to enable the business to meet its financial obligations for at least 15 months;
- the Company maintains a minimum of 2% headroom on its Regulated Asset Ratio covenant restrictions (see page 37); and
- post-dividend financial ratios remain within their agreed limits at both the balance sheet date and on a forward-looking basis.

The Company paid dividends totalling £157million during the financial year 2016/17 (2015/16: £82.4million).

Employee Involvement

We undertake significant levels of communication with our people, through regular business review conferences, team briefs and varied written communications. In 2016 we have significantly expanded the use of an internal social media platform called Yammer which enables employees to share successes and discuss issues. In 2017 the Executive also launched a series of company-wide discussions to seek employee input in to developing our Strategy, Vision and Values. Having already held face to face conferences with managers, the senior leaders of the business are meeting all employees in their teams, using "rich pictures" to illustrate the critical values we aspire to achieve to drive a discussion on how these might be achieved.

Thames Water recognises three trade unions, UNISON, GMB and Unite, working with them through an agreed Partnership approach. Company, trade union and where appropriate non-union representatives regularly meet at Company, business unit and function level to discuss issues affecting employees. In addition specific groups consider issues relating to Health, Safety and Wellbeing as well as undertake reviews of Company policies. Pay and conditions for non-managerial grades are negotiated by the Partnership trade unions. In 2016 the Company and trade unions ran a joint employee survey and workshops on pay and benefits to provide a clearer understanding of what all of our people value in their remuneration package and how we night develop this in the future.

All Managers and Senior Leaders in the Company are incentivised to deliver Company performance against the same key performance indicators, including financial, customer, asset health, health and safety indicators as well as the delivery of strategic and personal objectives. Following requests from employees for greater involvement in Company performance, we launched a cash saving scheme for all employees in 2015 focussing on two of the same critical performance indicators, specifically EBIT and Customer Satisfaction. Further schemes have been launched in 2016 and further schemes are planned each year.

The Company regularly shares key performance and other critical business information to employees through the various communications mentioned above, including business reviews and written communications. Specifically a monthly "Team Talk" session includes key performance, customer and business unit information which is communicated to every team. This session includes key messages from the CEO and CFO, typically in video format.

Equal Opportunities

At Thames Water, we recognise that our people are at the heart of our business. To help us succeed in our aim to provide best-in-class water and sewerage service, to be profitable and sustainable and to act in the long-term interests of our wider community, we need a range of skills and capabilities, representative of society, throughout our business.

We seek to attract, develop, reward, promote and retain a mix of colleagues who can offer different but complementary attitudes, ideologies, talents and knowledge. We understand the importance of appreciating and harnessing the unique skills, experiences and backgrounds that each individual brings to our family.

To support an equal opportunity, fair, diverse and inclusive Thames Water free from discrimination, bulling, harassment or victimisation, we are committed to building a working environment and culture that inspires our people to live our values.

All employees at all levels including managers and partners have a part to play to ensure people feel comfortable to bring their whole self to work.

The attitude and behaviour of all our staff working for an on behalf of Thames Water, including our Alliance partners, has a profound impact on our reputation and ability to ensure that everyone is provided with the same opportunities, treated with respect and valued, irrespective of their protected characteristic; age, disability, gender reassignment marriage and civil partnership, pregnancy and maternity, race, religion and belief, sex or sexual orientation. Everyone is entitled to be treated fairly, equally and provided with the same opportunities regardless of the nine protected characteristics defined by the Equality Act 2010 or factors such as trade union membership, political opinion, part-time or fixed-term status.

Employees with disability

As an equal opportunities company we aim for people with disabilities to have full and fair consideration for all vacancies. During the year, we have focussed on attracting people with disabilities to our join our organisation. We have received the governments 'Disability Confident' accreditation and promote opportunities at Disability Job Fairs.

Our 'Give Someone a Start' programme offers 3 weeks work experience to those people not in work including those with disabilities or health conditions with the aim to helping them into employment.

We endeavour to retain employees in the workforce if they become disabled during employment. We support individuals with their personal requirements and currently have a programme of work to ensure our key buildings have disability friendly facilities.

Going concern

The Directors believe, after due and careful enquiry, that the Company has sufficient resources to meet its present obligations as they fall due and, therefore, consider it appropriate to adopt the going concern basis in preparing the 2016/17 financial statements. In forming this assessment the Directors have considered the following information:

- The Company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 14 to 50. The financial position of the Company, its cash flows, liquidity position and borrowing facilities are described in the Strategic Report on pages 34 to 41;

- Day to day working capital requirements are funded by the business. During the year, £581.0m, gross of issuance costs, of new external debt was secured and £841.3m of debt repaid. There is no current requirement to raise additional finance to meet future project obligations. There are also cash balances and liquid resources of £56.5m and undrawn committed facilities of £1,408.0m;

- The committed facilities consist of £1,450m facilities with a group of banks made up of a £950m revolving credit facility (£908m of which is undrawn) that expires in 2021 that is not expected to be drawn down in full in the ordinary course of business, and £500m of 364-day liquidity facilities due for renewal in August 2017. The liquidity facilities can only be used if the Securitised Group is in standstill;

- The Company is in compliance with its financial covenant requirements as at 31 March 2017; and

- The Company's forecasts and projections, taking account of reasonably possible changes in trading performance, show that the Company should be able to operate within the level of its current facilities and covenant restrictions for at least 12 months from the date of this report.

Shareholder changes in the ultimate parent company

During the year ended 31 March 2017 Kemble Water International Holdings Limited, an entity managed by the Macquarie Group, agreed to sell its full 26.315% shareholding in Kemble Water Holdings Limited, the ultimate parent company of the Company.

The legal transfer of shares was made on 31 May 2017 from Kemble Water International Holdings Limited. Of the total shareholding in Kemble Water Holdings Limited, Farmoor Holdings B.V., an entity registered in the Netherlands and an affiliate of OMERS, received 17.543%, and Wren House Infrastructure Management Limited, the global direct infrastructure investment arm of the Kuwait Investment Authority, received 8.772%.

During the year ended 31 March 2017, SAS Trustee Corporation, agreed to sell its 2.389% shareholding in Kemble Water Holdings Limited to Aquila GP Inc., a Canadian entity managed by the Aquila Sonnet Limited Partnership. The legal transfer of shares was made on 25 April 2017. Following the transfer Aquila GP Inc. holds 4.995% of the total shareholding in Kemble Water Holdings Limited.

QIC Diversified Infrastructure Limited, agreed to sell 3.336% of the total shareholding in Kemble Water Holdings Limited to QS Infrastructure Pty Ltd, an entity registered in Australia and managed by QS UK Infrastructure Trust No. 1. The legal transfer of shares was made on 28 April 2017. At the same time, QIC Diversified Infrastructure Limited transferred the remainder of their holding, 5.352% to QIC Infrastructure Management Pty Limited
There will be no direct financial effect on the financial statements of the Company.

Transfer of non-household retail customers to Castle Water

From 1 April 2017, the Water Act 2014 allows all non-household customers to choose their supplier of water and wastewater retail services. On 18 July 2016, we announced our decision to exit the non-household retail market, and transfer our non-household customers to Castle Water Limited from the date of market opening. The Company continues to recognise wholesale revenue from these customers. On 1 April 2017, all non-household retail customers of Thames Water were transferred to Castle Water Limited which will result in the recognition of a profit on sale of the business. The sale did not become unconditional until the date of market opening (post year-end) and therefore the profit on sale, which we expect to be between £85.0 million and £87.0 million, will be recognised during the next financial year.

New bonds issued

A total of £550.0 million in new class B sterling bonds were issued by Thames Water Utilities Cayman Finance Limited on 3 May 2017, with a £300.0 million tranche maturing in 2023 and £250.0 million maturing in 2027. The proceeds are expected to be used to fund the redemption of the existing £550.0 million class B bonds which mature in 2025 but have their first call date in July 2017.

Material financial instruments

Financial risk management and information on financial instruments is covered on pages 34 to 41 of the Strategic Report.

Research and development

The Company's research and development programme consists of a portfolio of projects designed to address technical needs across the range of water cycle activities, delivering innovative technical solutions aligned with business needs to address challenges for AMP6 and beyond and also provide specialist technical support to the business. Expenditure on research and development totalled £4.0million for the year (2016: £3.1million).

Charitable fundraising

During the year, the Company raised £350,147 for WaterAid, with a further £93,000 of income pledged, which is being used to improve access to clean water for two towns in Malawi.
In addition, the Company raised a further £ 42,450 for other local and national charities through internal fundraising activities. The company match funded employee fundraising efforts with £34,483. The Company supports the local community through volunteering events and contributions to community investment funds.

Political donations

No political donations were made by the Company (2016: £nil).

Greenhouse gas emissions

We have made strong progress throughout 2016/17 in reducing our emissions, both by reducing our energy consumption and by increasing our renewable self-generation. Where we're not able to produce our own energy, we started sourcing renewable electricity through a contract with Haven Power. As a result we have achieved our 16/17 emissions targets.

In the last year we have reduced our emissions by 245.9 kTCO2e to 507.4 kTCO2e. We calculate our greenhouse gas emissions using the UK Water Industry Research Carbon Accounting Workbook ("CAW"). The CAW is the industry standard which is updated annually to reflect changes to emission factors and carbon reporting guidance from the Department of Environment, Food and Rural Affairs (Defra). Operational Greenhouse Gas Emissions ("GHG") within the regulated business are calculated annually reflecting the six major greenhouse gases and the Defra Environmental Reporting Guidelines. The emissions reported are associated with the operational emissions of the regulated business and include:

- Scope 1 (Direct emissions);
- Scope 2 (Indirect energy use emissions);
- Scope 3 (Emissions from outsourced services and business travel); and
- Carbon intensity ratios per mega-litre day (MLd) of service delivered.

Emissions from the greenhouse gases are standardised to global warming potential represented as carbon dioxide equivalents ("CO2e").

Intellectual property

The Company protects intellectual property of material concern to the business as appropriate, including the filing of patents where necessary.

Directors' indemnities

The Company has made qualifying third party indemnity provisions for the benefit of its Directors and for the benefit of other persons who are directors of associated companies and these remain in force at the date of this report.

Insurance

The Company maintains a comprehensive insurance programme, renewed annually. This includes cover for a range of insurance classes including Public Liability, Property, Employers Liability, Construction, Motor, and Directors & Officer liability cover.
The insurance coverage has been reviewed and approved by an Independent insurance adviser retained to ensure that the Company's insurances are consistent with good industry practice, have regard to the risk being covered and address the interests of the Company.

Statement of Directors' responsibilities in respect of the annual report and financial statements

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

Company law requires the Directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union ("EU") and applicable law.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the 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 estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; 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 adequate accounting records that 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 enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.
Under applicable law and regulations, the Directors are also responsible for preparing a Strategic report, Directors' report, Directors' remuneration report and corporate governance statement that complies with that law and those regulations.
The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

We confirm to the best of our knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company taken as a whole;
- the Strategic report (contained on pages 14 to 50) includes a fair review of the development and performance of the business and the position of the Company, taken as a whole, together with a description of the principal risks and uncertainties that are faced; and
- the Directors consider the annual report, taken as a whole, is fair, balanced and understandable and provides the information necessary for investors to assess the Company's position and performance, business model and strategy.

Disclosure of information to the auditor

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware and each director has taken all the steps that they ought to have taken as a director to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

Auditor

Pursuant to section 487 of the Companies Act 2006, the auditor will be deemed to be reappointed and KPMG LLP will therefore continue in office.

The Directors' Report was approved by the Board of Directors on 13 June 2017 and signed on its behalf by:

David Hughes, Company Secretary
Thames Water Utilities Limited, Clearwater Court,
Vastern Road, Reading, Berkshire RG1 8DB

Our statutory financial statements

Our statutory financial statements

Independent auditor's report

to the members of Thames Water Utilities Limited only

Opinions and conclusions arising from our audit

1. Our opinion on the financial statements is unmodified

We have audited the financial statements of Thames Water Utilities Limited for the year ended 31 March 2017 set out on pages 111 to 155. In our opinion the financial statements:

— give a true and fair view of the state of the Company's affairs as at 31 March 2017 and of its profit for the year then ended;

— have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union; and

— have been prepared in accordance with the requirements of the Companies Act 2006.

Overview		
Materiality: financial statements as a whole	£22.0m (2016: £22.0m) 0.13% (2016: 0.13%) of Total assets	
Risks of material misstatement		**vs 2016**
Recurring risks	Provision for trade receivables	◄►
	Classification of costs between operating and capital expenditure	◄►
	Completeness and valuation of other provisions	◄►

2. Our assessment of risks of material misstatement

In arriving at our audit opinion above on the financial statements, the risks of material misstatement that had the greatest effect on our audit, in decreasing order of audit significance, were as follows:

	The risk	Our response
Provision for trade receivables (£176.4m; 2016: £189.7m) *Refer to page 91 (Audit, Risk and Regulatory Committee Report), page 119 (accounting policy) and page 137 (financial disclosures).*	**Subjective estimate** A significant level of judgement is needed to calculate the doubtful debt provision based on the expected level of future cash collection and the anticipated level of cancelled and reissued bills. Key assumptions are made based on past history of non-collection of bills across the wide ranging portfolio of properties to which water and waste services are supplied. **Data capture** In addition, there is a risk that the data captured by the billing system and input into the calculation of the doubtful debt provision is incomplete and/or inaccurate.	Our procedures included: **- Control design:** With assistance from our own IT specialists, testing the completeness and accuracy of the data extracted from the Company's billing system used to calculate the provision, including data in respect of the debt ageing profile, historical cash collections, write-offs, cancellation and loss on rebill rates; **- Benchmarking assumptions:** Assessing the key inputs used, including the forecast cash collection rates, cancellations and rebill recoverability against historical trends; and **- Assessing transparency:** Assessing the adequacy of the disclosures made in relation to the Company's provisioning policy applied and the level of provisions recorded.
Classification of costs between operating and capital expenditure Operating expenditure (£1,515.4m; 2016: £1,419.4m) Capital expenditure (£1,115.3m; 2016: £1,198.7m) *Refer to page 91 (Audit, Risk and Regulatory Committee Report), page 116 (accounting policy) and pages 129 and 135 (financial disclosures).*	The Company's substantial investment programme, totalling over £1bn per annum, involves the enhancement and maintenance of both infrastructure and non-infrastructure assets. **Accounting treatment** Certain projects may contain a mixture of asset enhancement and maintenance, particularly where assets are being replaced or upgraded. Judgement is therefore required to ensure an appropriate allocation of costs between capital and operating expenditure. This allocation between operating and capital expenditure is inherently judgmental and there is a risk that the allocation is incorrect with expenditure misstated between the income statement and balance sheet. In addition, initial and subsequent expenditure, including employee and other internal expenditure, on capital assets is capitalised only if it can be demonstrated that it is directly attributable to the asset, provides probable economic benefit to the Company and can be measured reliably. There is a risk that costs capitalised do not meet these criteria.	Our procedures included: **- Accounting analysis:** In light of any new types of expenditure in the current year, challenging whether the Company's capitalisation policy remains compliant with applicable accounting standards, and in particular the criteria for capitalisation; **- Control design:** Inspecting Investment Committee meeting minutes for evidence of the authorisation and assessment of capital projects; **- Expectation vs. outcome:** Assessing the proportion of overhead costs which are capitalised by business area using historical comparisons and expected changes based upon corroborated enquiry; **- Tests of detail:** Assessing the appropriateness of the cost classification for a sample of projects, including by inspecting supporting documentation such as vendor statements of work completed for an understanding of the nature and type of costs incurred and assessing this against the criteria for capitalisation or expensing; and **- Assessing transparency:** Assessing the adequacy of the disclosures made in relation to the Company's policy of capitalisation or expensing of costs and the judgements involved.

2. Our assessment of risks of material misstatement (cont.)

	The risk	Our response
Completeness and valuation of other provisions (£35.9m; 2016: £40.7m) *Refer to page 91 (Audit, Risk and Regulatory Committee Report), page 118 (accounting policy) and pages 147 - 148 (financial disclosures).*	**Subjective estimate** The Company is required to comply with regulations set by Ofwat and other external and government agencies in the UK. For example, the Company is required to comply with all relevant Environmental Laws. Non-compliance may lead to potential fines and/or rectifying actions for the Company to address. Final agreement can often last for extended periods due to ongoing negotiations or, where relevant, the legal proceedings involved. The assessment required is inherently judgmental, and there is a risk that final settlements are materially different to the amounts provided. **Omitted exposures** There is also a risk that the assessment of provisions does not include all claims and therefore the provisions recorded are understated.	Our procedures included: - **Enquiry of lawyers:** Reviewing any correspondence with external regulators or agencies in connection with material disputes, and enquiring of the Company and the Company's external legal advisers regarding the nature of any claims, and the assumptions made with regard to the best estimate of the likely outcome; - **Benchmarking assumptions:** Assessing the key assumptions with regard to publicly available information concerning other settled disputes within the Water industry for similar claims; - **Historical comparisons:** Evaluating the historical accuracy of the Company's estimated provisions where claims are settled in the current year; and - **Assessing transparency:** Assessing the adequacy of the disclosures made concerning provisions recorded.

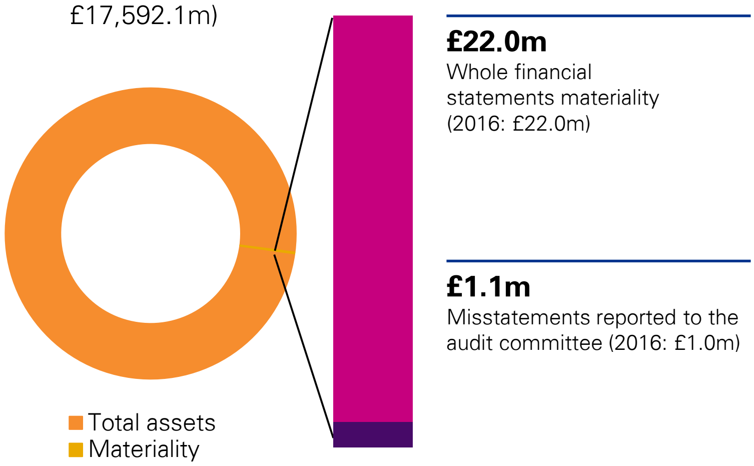
3. Our application of materiality and an overview of the scope of our audit

Materiality for the financial statements as a whole was set at £22.0m (2016: £22.0m), determined with reference to a benchmark of Company's total assets, of which it represents 0.13% (2016: 0.13%).

We reported to the Audit, Risk and Regulatory Committee any corrected or uncorrected identified misstatements exceeding £1.1m (2016: £1.0m), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Total assets
£17,360.8m (2016: £17,592.1m)

Materiality
£22.0m (2016: £22.0m)



KPMG

4. Our opinion on other matters prescribed by the Companies Act 2006 and under the terms of our engagement is unmodified

In addition to our audit of the financial statements, the directors have engaged us to audit the information in the Directors' Remuneration Report that is described as having been audited, which the directors have decided to prepare as if the company were required to comply with the requirements of Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008 No. 410) made under the Companies Act 2006.

In our opinion:

- the part of the Directors' Remuneration Report which we were engaged to audit has been properly prepared in accordance with Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 made under the Companies Act 2006, as if those requirements were to apply to the company;
- the information given in the Strategic Report and the Directors' Report for the financial year is consistent with the financial statements; and
- the information given in the Corporate Governance Statement set out on page 93 with respect to internal control and risk management systems in relation to financial reporting processes and about share capital structures ("the specified Corporate Governance Information") is consistent with the financial statements.

Based solely on the work required to be undertaken in the course of the audit of the financial statements and from reading the Strategic Report, the Directors' Report and the Corporate Governance Statement:

- we have not identified material misstatements in the Strategic Report, the Directors' Report and the Corporate Governance information;
- in our opinion, the Strategic Report and the Director's Report have been prepared in accordance with the Companies Act 2006; and
- in our opinion, the Corporate Governance Statement has been prepared in according with rules 7.2.2, 7.2.3, 7.2.5, 7.2.6 and 7.2.7 of the Disclosure Rules and Transparency Rules of the Financial Conduct Authority.

5. We have nothing to report on the disclosures of principal risks

Based on the knowledge we acquired during our audit, we have nothing material to add or draw attention to in relation to:

- the Directors' statement of viability on pages 40 and 41, concerning the principal risks, their management, and, based on that, the Directors' assessment and expectations of the Company's continuing in operation over the three years to 31 March 2020; or
- the disclosures in the accounting policies section of the financial statements concerning the use of the going concern basis of accounting.

6. We have nothing to report in respect of the matters on which we are required to report by exception

Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the Annual Report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading. In particular, we are required to report to you if:

- we have identified material inconsistencies between the knowledge we acquired during our audit and the Directors' statement that they consider that the Annual Report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy; or
- the Audit, Risk and Regulatory Committee Report does not appropriately address matters communicated by us to the Audit, Risk and Regulatory Committee.

Under the Companies Act 2006 and under the terms of our engagement we are required to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Directors' Remuneration Report which we were engaged to audit 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.

In addition to our audit of the financial statements, the directors have engaged us to review their Corporate Governance Statement as if the company were required to comply with the Listing Rules and the Disclosure Rules and Transparency Rules of the Financial Conduct Authority in relation to those matters. Under the terms of our engagement we are required to review:

- the directors' statements, set out on pages 100 and 40 - 41, in relation to going concern and longer-term viability; and
- the part of the Corporate Governance Statement on page 64 relating to the company's compliance with the eleven provisions of the 2014 UK Corporate Governance Code specified for our review.

We have nothing to report in respect of the above responsibilities.

Scope and responsibilities

As explained more fully in the Directors' Responsibilities Statement set out on page 103, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate. This report is made solely to the Company's members as a body and is subject to important explanations and disclaimers regarding our responsibilities, published on our website at www.kpmg.com/uk/auditscopeukco2014b, which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

Robert Brent (Senior Statutory Auditor)

for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London
E14 5GL

13 June 2017

Income statement

For the year ended 31 March

	Note	2017 Underlying £m	2017 BTL £m	2017 Total £m	2016 Underlying £m	2016 BTL £m	2016 Total £m
Revenue	2	**2,027.1**	**33.0**	**2,060.1**	2,039.5	-	2,039.5
Operating expenses	3	**(1,515.4)**	**-**	**(1,515.4)**	(1,419.4)	-	(1,419.4)
Profit on the sale of property, plant and equipment		**4.1**	**-**	**4.1**	48.5	-	48.5
Other operating income	5	**89.6**	**-**	**89.6**	73.6	-	73.6
Operating profit		**605.4**	**33.0**	**638.4**	742.2	-	742.2
Finance income	6	**94.5**	**-**	**94.5**	86.1	-	86.1
Finance expense	6	**(456.3)**	**-**	**(456.3)**	(343.3)	-	(343.3)
Net (losses)/gains on financial instruments	7	**(205.5)**	**-**	**(205.5)**	26.2	-	26.2
Profit on ordinary activities before taxation		**38.1**	**33.0**	**71.1**	511.2	-	511.2
Taxation on profit on ordinary activities	8	**70.3**	**(2.2)**	**68.1**	55.2	-	55.2
Profit for the year		**108.4**	**30.8**	**139.2**	566.4	-	566.4

Statement of other comprehensive income

For the year ended 31 March

	Note	2017 Underlying £m	2017 BTL £m	2017 Total £m	2016 Underlying £m	2016 BTL £m	2016 Total £m
Profit for the year		**108.4**	**30.8**	**139.2**	566.4	-	566.4
Other comprehensive income							
Will not be reclassified to the income statement:							
Net actuarial (losses)/gains on pension schemes	23	**(151.2)**	**-**	**(151.2)**	113.4	-	113.4
Deferred tax credit/(charge) on net actuarial loss/gain	20	**21.6**	**-**	**21.6**	(30.8)	-	(30.8)
May be reclassified to the income statement:							
Losses on cash flow hedges		**(50.7)**	**-**	**(50.7)**	(65.0)	-	(65.0)
Cash flow hedges transferred to income statement	7	**2.1**	**-**	**2.1**	-	-	-
Deferred tax credit on cash flow hedge loss	20	**6.1**	**-**	**6.1**	8.7	-	8.7
Other comprehensive (loss)/income for the year		**(172.1)**	**-**	**(172.1)**	26.3	-	26.3
Total comprehensive (loss)/income for the year		**(63.7)**	**30.8**	**(32.9)**	592.7	-	592.7

The Company's activities above are derived from continuing activities.

Bazalgette Tunnel Limited ("BTL") is an independent company un-related to Thames Water Utilities Limited, and was appointed in 2015 to construct the Thames Tideway Tunnel. This is the first year that we have recognised revenue on the arrangement with BTL and so we have disclosed our underlying performance separately.

The arrangement with BTL means the Company has included construction costs of the Thames Tideway Tunnel within its bills to wastewater customers during the year ended 31 March 2017. As cash is collected, these amounts are subsequently paid to BTL. Accounting standards require the Company to present the amounts billed as revenue in our financial statements, and with no associated costs, this also gives rise to reporting profit which is taxable. This non-appointed revenue is excluded from our key performance indicators which is consistent with our banking covenants. The revenue and resulting profit on this arrangement has been disclosed separately to the Company's underlying performance in the statements above. As a result of this arrangement with no cash retained, a prepayment is created and recorded by the Company as BTL will transfer the tunnel to us once construction is complete under a finance lease arrangement.

The accounting policies and notes on pages 115 to 155 are an integral part of these financial statements.

Statement of financial position

As at 31 March

	Note	**2017**			2016		
		Underlying £m	**BTL £m**	**Total £m**	Underlying £m	BTL £m	Total £m
Non-current assets							
Intangible assets	10	**140.5**	**-**	**140.5**	65.9	-	65.9
Property, plant and equipment	11	**14,094.5**	**-**	**14,094.5**	13,473.0	-	13,473.0
Investment in subsidiaries	12	**0.1**	**-**	**0.1**	0.1	-	0.1
Derivative financial assets	19	**83.6**	**-**	**83.6**	336.4	-	336.4
Intercompany loans receivable	13	**2,274.7**	**-**	**2,274.7**	2,315.0	-	2,315.0
Trade and other receivables	15	**2.8**	**30.4**	**33.2**	2.5	1.3	3.8
		16,596.2	**30.4**	**16,626.6**	16,192.9	1.3	16,194.2
Current assets							
Inventories and current intangible assets	14	**21.7**	**-**	**21.7**	20.7	-	20.7
Assets held for sale		**1.0**	**-**	**1.0**	1.0	-	1.0
Intercompany loans receivable	13	**16.8**	**-**	**16.8**	4.4	-	4.4
Trade and other receivables	15	**634.2**	**3.0**	**637.2**	559.8	-	559.8
Short term investments	19	**1.0**	**-**	**1.0**	289.5	-	289.5
Cash and cash equivalents	16	**52.7**	**3.8**	**56.5**	522.5	-	522.5
		727.4	**6.8**	**734.2**	1,397.9	-	1,397.9
Current liabilities							
Trade and other payables	17	**(924.4)**	**(6.6)**	**(931.0)**	(869.4)	(1.5)	(870.9)
Borrowings	18	**(383.4)**	**-**	**(383.4)**	(1,036.9)	-	(1,036.9)
Derivative financial liabilities	19	**(23.8)**	**-**	**(23.8)**	-	-	-
		(1,331.6)	**(6.6)**	**(1,338.2)**	(1,906.3)	(1.5)	(1,907.8)
Net current (liabilities)/assets		**(604.2)**	**0.2**	**(604.0)**	(508.4)	(1.5)	(509.9)
Non-current liabilities							
Trade and other payables	17	**(404.9)**	**-**	**(404.9)**	(362.3)	-	(362.3)
Borrowings	18	**(10,423.5)**	**-**	**(10,423.5)**	(9,928.0)	-	(9,928.0)
Derivative financial liabilities	19	**(900.7)**	**-**	**(900.7)**	(940.9)	-	(940.9)
Deferred tax	20	**(877.4)**	**-**	**(877.4)**	(981.8)	-	(981.8)
Provisions for liabilities and charges	21	**(112.5)**	**-**	**(112.5)**	(97.6)	-	(97.6)
Retirement benefit obligations	23	**(379.8)**	**-**	**(379.8)**	(260.0)	-	(260.0)
		(13,098.8)	**-**	**(13,098.8)**	(12,570.6)	-	(12,570.6)
Net assets		**2,893.2**	**30.6**	**2,923.8**	3,113.9	(0.2)	3,113.7
Equity							
Called up share capital	22	**29.0**	**-**	**29.0**	29.0	-	29.0
Share premium	22	**100.0**	**-**	**100.0**	100.0	-	100.0
Cash flow hedge reserve	22	**(222.4)**	**-**	**(222.4)**	(179.9)	-	(179.9)
Revaluation reserve	22	**1,053.1**	**-**	**1,053.1**	1,071.9	-	1,071.9
Retained earnings	22	**1,933.5**	**30.6**	**1,964.1**	2,092.9	(0.2)	2,092.7
Total equity		**2,893.2**	**30.6**	**2,923.8**	3,113.9	(0.2)	3,113.7

Bazalgette Tunnel Limited ("BTL") is an independent company un-related to Thames Water Utilities Limited, and was appointed in 2015 to construct the Thames Tideway Tunnel. This is the first year that we have recognised revenue on the arrangement with BTL and so we have disclosed our underlying performance separately.

Bazalgette Tunnel Limited ("BTL") is responsible for the construction of the Thames Tideway Tunnel. For the year ended 31 March 2017 the Company has included construction costs of the Thames Tideway Tunnel within its bills to wastewater customers. These amounts are subsequently paid to BTL. The revenue and profit on this arrangement, which is excluded from our key performance indicators, has been disclosed separately to the Company's underlying performance in the income statements. The statement of financial position above separately recognises the associated assets and liabilities as a result of this arrangement.

The accounting policies and notes on pages 115 to 155 are an integral part of these financial statements.

The financial statements for Thames Water Utilities Limited, registered in England & Wales company number 02366661, were approved by the Board of Directors on 13 June 2017 and signed on its behalf by:

Brandon Rennet
Chief Financial Officer

Statement of changes in equity

For the year ended

	Share capital £m	Share premium £m	Cash flow hedge reserve £m	Revaluation reserve £m	Retained earnings £m	**Total equity £m**
At 1 April 2015	29.0	100.0	(123.6)	1,076.5	1,521.5	**2,603.4**
Profit for the year	-	-	-	-	566.4	**566.4**
Loss on cash flow hedge	-	-	(65.0)	-	-	**(65.0)**
Deferred tax credit on cash flow hedge	-	-	8.7	-	-	**8.7**
Actuarial gain on pension scheme	-	-	-	-	113.4	**113.4**
Deferred tax charge on actuarial gain	-	-	-	-	(30.8)	**(30.8)**
Total comprehensive income	-	-	(56.3)	-	649.0	**592.7**
Transfer of depreciation	-	-	-	(38.4)	38.4	**-**
Deferred tax on depreciation transfer	-	-	-	7.7	(7.7)	**-**
Reduction in deferred tax rate	-	-	-	26.1	(26.1)	**-**
Dividends paid	-	-	-	-	(82.4)	**(82.4)**
At 31 March 2016	29.0	100.0	(179.9)	1,071.9	2,092.7	**3,113.7**
Profit for the year	-	-	-	-	139.2	**139.2**
Loss on cash flow hedge	-	-	(50.7)	-	-	**(50.7)**
Cash flow hedges transferred to income statement	-	-	2.1	-	-	**2.1**
Deferred tax credit on cash flow hedge loss	-	-	6.1	-	-	**6.1**
Actuarial loss on pension scheme	-	-	-	-	(151.2)	**(151.2)**
Deferred tax on actuarial loss	-	-	-	-	21.6	**21.6**
Total comprehensive income	-	-	(42.5)	-	9.6	**(32.9)**
Transfer of depreciation	-	-	-	(38.4)	38.4	**-**
Deferred tax on depreciation transfer	-	-	-	6.9	(6.9)	**-**
Reduction in deferred tax rate	-	-	-	12.7	(12.7)	**-**
Dividends paid	-	-	-	-	(157.0)	**(157.0)**
At 31 March 2017	29.0	100.0	(222.4)	1,053.1	1,964.1	**2,923.8**

The accounting policies and notes on pages 115 to 155 are an integral part of these financial statements.

Statement of cash flows

For the year ended 31 March

	Note	2017 Underlying £m	2017 BTL £m	2017 Total £m	2016 Underlying £m	2016 BTL £m	2016 Total £m
Net cash generated by operating activities	28	**1,046.0**	**3.8**	**1,049.8**	1,157.9	-	1,157.9
Investing activities:							
Decrease/(increase) in current asset investments		**288.5**	**-**	**288.5**	(12.4)	-	(12.4)
Interest received		**81.9**	**-**	**81.9**	107.7	-	107.7
Proceeds from repayment of loans to group companies		**40.3**	**-**	**40.3**	-	-	-
Purchase of property, plant and equipment		**(1,144.5)**	**-**	**(1,144.5)**	(1,262.4)	-	(1,262.4)
Purchase of intangible assets		**(102.7)**	**-**	**(102.7)**	(27.3)	-	(27.3)
Proceeds from sale of property, plant and equipment		**5.9**	**-**	**5.9**	14.7	-	14.7
Increase in deferred income - retail non-household sale		**97.3**	**-**	**97.3**	-	-	-
Net cash used in investing activities		**(733.3)**	**-**	**(733.3)**	(1,179.7)	-	(1,179.7)
Financing activities:							
New loans raised		**568.1**	**-**	**568.1**	641.4	-	641.4
Repayment of borrowings		**(841.3)**	**-**	**(841.3)**	(267.4)	-	(267.4)
Interest paid		**(352.3)**	**-**	**(352.3)**	(268.2)	-	(268.2)
Dividends paid		**(157.0)**	**-**	**(157.0)**	(82.4)	-	(82.4)
Net cash generated (used in)/from financing activities		**(782.5)**	**-**	**(782.5)**	23.4	-	23.4
Net (decrease)/increase in cash and cash equivalents		**(469.8)**	**3.8**	**(466.0)**	1.6	-	1.6
Net cash and cash equivalents at beginning of year		**522.5**	**-**	**522.5**	520.9	-	520.9
Net cash and cash equivalents at end of year		**52.7**	**3.8**	**56.5**	522.5	-	522.5

No additions to property, plant and equipment during the year, or the immediately preceding year, were financed through new finance leases.

The Company holds short term investments as current financial assets (see note 19) which include money market deposits held with external parties. In the prior year the net cash flows on these investments were presented within financing activities. The Directors have considered the nature of these short term investments and have presented the net cash movement within investing activities with the prior year comparative re-presented in this same category. There is no impact on the total net movement in cash and cash equivalents for TWUL resulting from this change in presentation.

Bazalgette Tunnel Limited ("BTL") is an independent company un-related to Thames Water Utilities Limited, and was appointed in 2015 to construct the Thames Tideway Tunnel. This is the first year that we have recognised revenue on the arrangement with BTL and so we have disclosed our underlying performance separately.

Bazalgette Tunnel Limited ("BTL") is responsible for the construction of the Thames Tideway Tunnel. For the year ended 31 March 2017 the Company has included construction costs of the Thames Tideway Tunnel within its bills to wastewater customers. These amounts are subsequently paid to BTL. The revenue and profit on this arrangement, which is excluded from our key performance indicators, has been disclosed separately to the Company's underlying performance in the statements above. The cash balance included above reflects amounts collected and not paid over at the balance sheet date.

The accounting policies and notes on pages 115 to 155 form an integral part of these financial statements.

Accounting policies

The following accounting policies have been adopted in the preparation of these financial statements. They have been applied consistently in dealing with items which are considered material.

General information

Thames Water Utilities Limited ("the Company") is a company incorporated in England & Wales and domiciled in the United Kingdom under the Companies Act 2006. The address of the registered office is Clearwater Court, Vastern Road, Reading, RG1 8DB. The Company is also an intermediate holding company within the Kemble Water Holdings Limited Group of companies ("the Group").

The Company's principal activity is that of an appointed water and wastewater services provider, including acting as a retailer for household and non-household customers, operating in London, the Thames Valley and surrounding area in accordance with its licence of appointment. Following our decision in July 2016 to exit from the competitive non-household retail market, from the date of market opening (1 April 2017), the Company no longer acts as a retailer to non-household customers.

Statement of compliance with International Financial Reporting Standards

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union ("EU").

Basis of Preparation

The financial statements for the year ended 31 March 2017, set out on pages 111 to 114, have been prepared on the going concern basis, under the historical cost convention, as modified by the revaluation of certain financial assets and liabilities at fair value, and the Disclosure and Transparency Rules ("DTR") issued by the Financial Conduct Authority. This is discussed in the Directors' Report on page 100.

The Company has exercised exemption under section 400 of the Companies Act 2006 from the requirement to prepare group financial statements as the Company and its subsidiaries are included within the consolidated financial statements of its ultimate parent company, Kemble Water Holdings Limited, an entity registered in England and Wales. The address of the registered office of Kemble Water Holdings Limited is Clearwater Court, Vastern Road, Reading, Berkshire, RG1 8DB.

These financial statements present information about the Company as an individual undertaking and not about its group.

Revenue recognition

Revenue represents the fair value of the consideration received or receivable in the ordinary course of business, excluding value added tax and trade discounts, for goods and services provided which are recognised in accordance with IAS18 *Revenue*. Revenue is recognised at the time of delivery of the service. Should the Company consider that the criteria for full revenue recognition are not met at the time of a transaction, recognition of the associated revenue would be deferred until such time as the criteria have subsequently been met. Bad debt on bills raised in the year, which are considered uncollectable based on historic experience, is recognised as a deduction to revenue to ensure revenue is recorded at fair value.

Revenue includes an estimate of the amount of mains water and wastewater charges unbilled at the period end, which are recorded within accrued income. The usage is estimated using a defined methodology based upon historical data and assumptions. When a new property is connected to the infrastructure network an estimate is made of the sales value of water supplied and wastewater charges incurred between the date of connection and the period end. Where actual results differ from estimates used, revenue is adjusted in the period for which the revision to the estimate is determined.

For unmetered customers, the amount to be billed is dependent upon the rateable value of the property, as assessed by an independent rating officer. The amount billed is recorded within deferred income and is apportioned to revenue over the period to which the bill relates.

The Company only raises bills in the name of the "occupier" when it has evidence that an unmeasured property is occupied but cannot confirm the name of the occupier. When the Company identifies the occupants the bill is cancelled and re-billed in the customer's name. If the Company has not identified an occupant within six months the bill is cancelled and the property is classified as empty.

Revenue includes amounts billed to wastewater customers in respect of construction costs for the Thames Tideway Tunnel. Under specific arrangements with Bazalgette Tunnel Limited, TWUL (in its capacity as principal) is responsible for the billing and collection of cash. TWUL passes the associated cash on to Bazalgette Tunnel Limited within 50 working days after the month end in which the cash is collected. The cost of any bad debt is borne by Bazalgette Tunnel Limited. Accounting standards require the Company to present the amounts billed as revenue in our financial statements, and with no associated costs this also gives rise to reporting profit which is taxable. The cash collected is not retained by the Company and accordingly the revenue and resulting profit on this arrangement has been disclosed separately in the Company's financial statements, and is excluded from our key performance indicators. As a result of this arrangement with no cash retained, a prepayment is created and recorded by the company as BTL will transfer the tunnel to TWUL once construction is complete under a finance lease arrangement.

Interest income is accrued on a time basis by reference to the principal outstanding and the Effective Interest Rate ("EIR") applicable. The EIR is the rate that exactly discounts the estimated future cash payments or receipts over the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or liability. Interest income is presented within finance income in the income statement.

Property, plant and equipment

Property, Plant and Equipment ("PP&E") is comprised of network assets (including water mains, sewers, pumped raw water storage reservoirs and sludge pipelines) and non-network assets. PP&E is stated at cost (or at deemed cost in the case of network assets, being the fair value at the date of transition to IFRS) less accumulated depreciation and provision for impairment.

The Company capitalises the directly attributable costs of procuring and constructing PP&E in accordance with IAS16 *Property, Plant and Equipment*. These costs include labour and other internal costs incremental to the business due to the scale and nature of the capital implementation programme of the Company. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and its cost can be measured reliably.

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of the associated asset. All other borrowing costs are included as finance expenses within the income statement.

Where items of PP&E are transferred to the Company from customers or developers, generally in the form of adopted water mains, self-lay sewers or adopted pumping stations, the fair value of the asset transferred is recognised in the statement of financial position. Fair value is determined based on estimated replacement cost. Where the transfer is in exchange for connection to the network and there is no further obligation for ongoing services, the corresponding credit is recognised immediately within revenue. Where the transfer is considered to be linked to the provision of ongoing services, the corresponding credit is recorded in deferred income and is released to other operating income over the expected useful economic lives of the associated assets as shown below.

The gain or loss arising on the disposal or retirement of an item of PP&E is determined as the difference between the sale proceeds and the carrying amount of the asset at the date the transaction arises, and is recognised separately in the income statement.

PP&E is depreciated to its estimated residual value over its estimated useful life, with the exception of freehold land which is not depreciated. Assets in the course of construction are not depreciated as these assets are not considered to commence their economic lives until they are commissioned, whereupon they are transferred into an appropriate category of PP&E.

The estimated useful economic lives are as follows and refer to non-current assets disclosed in note 11:

	Years
Network assets:	
Reservoirs	250
Strategic sewer components	200
Wastewater network assets	150
Water network assets	80-100
Raw water tunnels and aqueducts	80
Non-network assets:	
Land and buildings:	
Buildings	15-60
Operational structures	30-100
Plant and equipment:	
Other operational assets	7-40
Fixtures & fittings	5-7
Vehicles	4-5
Computers	3-5
Fixed and mobile plant	4-60

Grants and contributions

Contributions received in respect of certain infrastructure charges (where on connection of a new property to the network the Company receives cash from the developer towards the investment required to enhance network capacity, to meet new demand and maintain service levels) are treated as deferred income and released to other operating income over a 30 year period.

Contributions which are given in compensation for expenses incurred with no future related costs, including the cost of excavating, connecting and reinstating a new water supply to an existing mains connection, are recognised within other operating income in the period that they become receivable as no continuing obligation remains once the connection has been made.

Non-current intangible assets

Separately acquired intangible assets are stated at cost, less accumulated amortisation and any provision for impairment.

Research expenditure is expensed to the income statement as incurred. Development expenditure is capitalised when appropriate criteria are met under *IAS 38 Intangible Assets*. Amortisation of the asset begins when development is complete and the asset is available for use. It is amortised over the period of expected future benefit on a project by project basis.

Amortisation is charged to the income statement on a straight-line basis over the estimated useful economic life of the intangible asset. These intangible assets are amortised from the date they become available for use. The estimated useful economic life is as follows:

	Years
Development expenditure	3-25
Software	5-10

Investment in subsidiaries

Investments in subsidiary undertakings are stated at cost, less any provision for impairment.

Assets held for sale

Non-current assets are reclassified as held for sale if all of the following criteria are satisfied:

- the carrying amount will be recovered principally through sale rather than through continuing use;
- the asset is available for immediate sale in its present condition; and
- a sale is considered to be highly probable.

On initial reclassification as held for sale, non-current assets are measured at the lower of the previous carrying amount and fair value less costs to sell, with any adjustments being recognised within the income statement. Once classified as held for sale no further depreciation or amortisation is recognised.

Inventories and current intangible assets

Inventories are stated at the lower of cost and net realisable value ("NRV"). Costs comprise direct materials and, where applicable, direct labour costs and those overheads that have been incurred in bringing the inventories to their present location and condition. Inventory is assessed for obsolescence on an item-by-item basis and when determined to be obsolete is written off immediately to the income statement.

Purchased carbon emission allowances (relating to the emission of carbon dioxide in the UK) are recorded as current intangible assets, stated at cost, less accumulated amortisation and any provision for impairment. A provision is simultaneously recorded in respect of the obligation to deliver emission allowances in the period in which the emissions are made and the associated charge is recognised as an operating expense within the income statement.

Leased assets

Leases where the Company obtains assets which transfer substantially all the risks and rewards of ownership to the Company are treated as finance leases. The lower of the fair value of the leased asset and the present value of the minimum lease payments is capitalised as an asset, with a corresponding liability representing the obligation to the lessor. Lease payments are treated as consisting of a capital element and a finance charge; the capital element reducing the obligation to the lessor and the finance charge being written off to the income statement at a constant rate over the period of the lease, in proportion to the capital amount outstanding. Depreciation is charged at the shorter of the estimated useful economic life and the lease period.

All other leases are classified as operating leases. Payments made under operating leases are recognised in the income statement on a straight line basis over the term of the lease. Lease incentives and premiums received are recognised in the income statement as an integral part of the total lease expense and are released to the income statement on a straight line basis over the term of the lease. Leases of land are ordinarily treated as operating leases, unless ownership is transferred to the Company at the end of the lease.

On completion of construction of the Thames Tideway Tunnel, substantially all the risks and rewards of ownership will lay with the Company. The Company will therefore account for the transaction arrangement with BTL post construction as a finance lease. The tunnel will be recognised as an asset within PP&E and depreciated over the life of the lease. On inception of the lease, the tunnel will be recognised at fair value, being the prepayment plus the present value of the minimum lease payments, with a corresponding liability being recognised as a finance lease payable. Interest will be recognised in the income statement over the period of the lease.

Provisions for liabilities and charges

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated.

The Company is subject to a number of legal claims which include commercial and contractual disputes, which are handled and defended in the ordinary course of business. The Company routinely assesses the likelihood of any adverse judgements or outcomes to these matters as well as ranges of probable and reasonably estimated losses. Reasonable estimates involve judgements made by management after considering available information including notifications, settlements, estimates performed by independent parties and legal counsel, available facts, identification of other potentially responsible entities and their ability to contribute, and prior experience.

Provisions for insured liabilities are recognised or released by assessing their adequacy using current estimates of future cash flows under insurance contracts.

Provisions are discounted to present value using a pre-tax discount rate that reflects the risks specific to the liability, where the effect is material.

The Company is subject to Outcome Delivery Incentives (“ODIs”) where failure to achieve targets can lead to financial penalties and outperformance can result in financial rewards. These penalties and rewards are in the form of revenue adjustments or Regulated Capital Value (“RCV”) adjustments. The Company does not recognise a provision for penalties or rewards in the period in which they are incurred or achieved as the financial impact of these is taken in the following Asset Management Plan (“AMP”) period.

Risks, opportunities and innovation (“ROI”) funds

The Company has entered into certain alliance arrangements with a number of third parties. The alliance agreements include incentive mechanisms which result in the alliance partners sharing in any over or underspend on contracted works. Remuneration for services provided under the contract are also linked to TWUL’s performance commitments. During the year ended 31 March 2017 there were three alliances responsible for delivering works over AMP6.

A notional ROI fund for each alliance is created and built up over the AMP. The ROI fund is ultimately paid to alliance partners at contractual percentages. This occurs once certain conditions are satisfied, as specified in the alliance contracts between the Company and the alliance partners.

A provision for ROI amounts is recognised when the Company has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount can be reliably estimated. Conversely, a receivable for ROI will be recognised when: the Company has a right to receive cash at a future date; the amount can be reliably estimated; and receipt is virtually certain.

ROI amounts arising from an over or underspend against the contracted cost for a capital project, where the spend is directly attributable to the asset created, are deemed to be an integral cost in bringing an asset into the condition and location for use as intended by management. They are therefore capitalised as part of the cost of the asset and depreciated over the asset’s useful life.

ROI amounts arising from operating expenditure over or underspend against the contracted cost, where spend cannot be directly attributed to a capital asset, are recognised directly in profit or loss as the spend is incurred.

ROI amounts linked to an ODI/SIM penalty or reward are recognised in the income statement at the point the penalty has been incurred or reward has been achieved.

Discontinued operations

Components of the Company will be classified as a discontinued operation if that component has either been disposed of, or is classified as held for sale. A component comprises operations that can be clearly distinguished, operationally and for financial reporting purposes from the rest of the Company. A component will only be classified as discontinued given that either: it represents a separate major line of business, or geographical area; or is part of a single co-ordinated plan to dispose of a separate major line of business.

Transfer of non-household retail customers to Castle Water

Following our decision in July 2016 to exit from the competitive non-household retail market from the date of market opening (1 April 2017), the Company entered an agreement to transfer its non-household customers to Castle Water from the date of market opening. The Company continues to recognise wholesale revenue from these customers. The non-household retail component does not represent a material portion of the activities of the Company and accordingly it is not presented as a discontinued operation.

Retirement and other employment benefits

Defined benefit schemes

The Company operates two, independently administered, defined benefit pension schemes, both of which are closed to new employees. Actuarial valuations are carried out as determined by the Trustees, using the projected unit credit method for both schemes at intervals of not more than three years. The rates of contributions payable and the pension cost are determined on the advice of the actuaries, having regard to the results of these valuations.

The difference between the value of defined benefit pension scheme assets and liabilities is recorded within the statement of financial position as a retirement benefit or obligation. Defined benefit pension scheme assets are measured at fair value using the bid price for assets with quoted prices. Defined benefit pension scheme liabilities are measured at the reporting date by an independent actuary using the projected unit credit method and discounted at the current rate of return on high quality bonds of equivalent term and currency to the liability.

Service costs, representing the cost of employee service in the period, and scheme administration expenses are included within operating expenses in the income statement. The net finance cost is calculated by applying the discount rate used for the scheme liabilities to the net deficit.

Changes in the retirement benefit obligation may arise from:

- differences between the return on scheme assets and interest included in the income statement;
- actuarial gains and losses from experience adjustments; or
- changes in demographic or financial assumptions.

Such changes are classified as re-measurements and are charged or credited to equity and recorded within the statement of comprehensive income in the period in which they arise.

Defined contribution schemes

The Company operates a Defined Contribution Stakeholder Pension Scheme (“DCSPS”) managed through Standard Life Assurance Limited. From 1 April 2011 the DCSPS is the only scheme to which new employees of the Company are eligible. The assets of the DCSPS are held separately from those of the Company and obligations for contributions to the scheme are recognised as an expense in the income statement in the periods during which they fall due.

Long-term incentive plans (“LTIP”) and bonus

Cash based LTIP awards are accrued in the financial statements for the duration of the award. The accrual is based on the values assessed for the applicable schemes, taking into account the duration of the individual scheme, and by comparing the Company’s performance against the assumptions used to award payments. These are recognised as the present value of the benefit obligation.

Bonus payments are accrued in the period based on assessments of performance against targets set at the beginning of the financial year. Bonuses are paid in the following financial year, once performance has been measured against targets set.

During the year, the Company opened ‘Share in Your Success 2016’. This follows the successful launch of ‘Share in Your Success 2015’ which enrolled employees in the financial year ended 31 March 2016. Both schemes are open to all employees. Employees are able to contribute between £20 and £250 per month from their salary into a savings account over a three year period. At the end of the three years, the employee is then entitled to all of the cash they have sacrificed during that period, plus interest that has accrued on that balance, and a ‘bonus’ element paid by the Company of up to 35% of the amount invested. If an employee is to leave the Company within the three year period, then they are entitled to the amount they have invested up until the point of departure, including the interest due in that period.

Non-derivative financial instruments

A financial instrument is any contract that gives rise to a financial asset in one entity and a financial liability or equity instrument in another entity. Non-derivative financial instruments comprise trade and other receivables, cash and cash equivalents, loans and borrowings and trade and other payables.

Trade and other receivables

Trade and other receivables are measured at fair value on initial recognition. Subsequent to initial recognition they are measured at amortised cost using the effective interest method. If there is objective evidence that the asset is impaired it is written down to its recoverable amount and the irrecoverable amount is recognised as an expense within operating costs. 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, and is assessed by management on a case-by-case basis.

Included within trade receivables is an assessment of the recoverability of debts which will ultimately be cancelled, and may or may not be rebilled, and of debts which have not yet been billed but are part of the metered sales accrual. This assessment is made by reference to the Company’s historical collection experience, including comparisons of the relative age of the individual balance and consideration of the actual write-off history. The provisioning rates applied in the calculation are reviewed on an annual basis to reflect the latest historical collection performance data and management’s expectation of future performance and industry trends. A provision is also made against debts due from Water Only Companies (“WOCs”) who bill their customers for sewerage services provided by the Company. As detailed information about the debt, including the ageing, is unavailable, the level of provision is calculated with reference to the level of historical, current and forecast write-offs.

Included within prepayments are amounts paid and payable to Bazalgette Tunnel Limited which represent a prepayment for the use of the Thames Tideway Tunnel once the project is complete.

Trade and other payables

Trade and other payables are recognised initially at fair value. Subsequent to initial recognition they are measured at amortised cost using the effective interest method.

Trade and other payables include amounts owed to Bazalgette Tunnel Limited. Amounts owed to Bazalgette tunnel represent revenue collected and passed across to Bazalgette Tunnel Limited for the construction of the Thames Tideway Tunnel, which have not yet been paid at the reporting date.

Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and in hand and demand deposits and other short-term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value. Such investments are normally those with less than three months maturity from the date of acquisition and include cash and bank balances and investments in liquid funds.

Bank overdrafts that are repayable on demand form an integral part of the Company's cash management and are also included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

Included within cash are amounts collected in relation to Bazalgette Tunnel Limited revenue which have not yet been paid across to Bazalgette Tunnel Limited at the reporting date.

Interest bearing borrowings

Interest bearing borrowings are financial liabilities recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition these are stated at amortised cost using the effective interest method. The amortisation is included within finance costs in the income statement and is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the effective interest rate. An exchange or modification of interest bearing borrowing with substantially different terms is accounted for as an extinguishment of the original financial liability and the recognition of new financial liability. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the financial liability and are amortised over the remaining term of the modified financial liability.

Interest bearing loans issued to other group companies

Interest bearing loans issued to other group companies are initially recognised at fair value plus transaction costs that are directly attributable to the acquisition of the financial asset. They are subsequently measured at amortised cost using the effective interest rate method, less any provision for impairment. The amortisation is included within finance income in the income statement and is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the effective interest rate. An exchange or modification of interest bearing loans issued to other group companies with substantially different terms is accounted for as derecognition of the original financial asset and the recognition of new financial asset. If an exchange of loan or modification of terms is accounted for as derecognition, any costs or fees incurred are recognised as part of the gain or loss on derecognition. If the exchange or modification is not accounted for as derecognition, any costs or fees incurred adjust the carrying amount of the financial asset and are amortised over the remaining term of the modified financial asset.

Derivative financial instruments and hedging

Derivatives are used to manage exposure to movements in interest rates, foreign exchange rates and inflation. A financial instrument is classified as derivative if:

- its value changes in response to the change in a specified interest rate, foreign exchange rate or index of prices or rates;
- it requires no initial net investment or an initial net investment that is smaller than the underlying principal; and
- it is settled at a future date.

Derivative financial instruments not designated as hedging instruments

Derivative financial instruments are initially recognised at fair value with transaction costs being taken to the income statement. The gain or loss on re-measurement to fair value is recognised immediately in profit or loss.

Derivative financial instruments designated as hedging instruments

The Company uses derivative financial instruments, such as forward currency contracts and interest rate swaps to hedge its foreign currency risks and interest rate risks, respectively. At the inception of each hedge relationship the Company documents:

- the relationship between the hedging instrument and the hedged item;
- its risk management objectives and strategy for undertaking the hedge transaction; and
- the results of tests to determine whether the hedging instrument is expected to be highly effective in offsetting changes in cash flows or fair values (as applicable) of the hedged item.

The Company continues to test and document the effectiveness of the hedge on an ongoing basis. Hedge accounting discontinues when the hedging instrument expires, is sold, terminated or exercised, or no longer qualifies for hedge accounting.

Cash flow hedges

Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or a highly probable forecast transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in the cash flow hedge reserve. Any ineffective portion of the hedge is recognised immediately in the income statement.

When the forecast transaction subsequently results in the recognition of a non-financial asset or non-financial liability, the associated cumulative gain or loss is removed from the cash flow hedge reserve and reclassified to the income statement in the same period or periods during which the asset acquired or liability assumed affects profit or loss, i.e. when interest income or expense is recognised.

When a hedging instrument expires or is sold, terminated or exercised, or the Company revokes designation of the hedge relationship but the hedged forecast transaction is still expected to occur, the cumulative gain or loss at that point remains in the cash flow hedge reserve within equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to take place, the cumulative unrealised gain or loss recognised in equity is recognised in the income statement immediately.

Embedded derivatives

Where a contract includes terms that cause some of its cash flows to vary in a similar way to a derivative financial instrument, that part of the contract is considered to be an embedded derivative. Embedded derivatives are separated from the host contract and measured at fair value with gains and losses taken to the income statement if:

- the risks and characteristics of the embedded derivative are not closely related to those of the host contract; and
- the contract is not carried at fair value with gains and losses reported in the income statement.

In all other cases embedded derivatives are accounted for in line with the accounting policy for the contract as a whole.

Fair value measurement

The Company measures financial instruments, such as derivatives, at fair value at each financial reporting date. Fair value is the price that would be received in selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value reflects the non-performance risk.

De-recognition of financial instruments

A financial asset is derecognised when the rights to receive cash flows from the asset have expired.

A financial liability is derecognised when the obligation under the liability is discharged, cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as the derecognition of the original liability and the recognition of a new liability. The difference between the carrying amount of the financial liability extinguished or transferred and the consideration paid is recognised in the income statement.

Offsetting financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously.

Financial guarantees

The Company is part of a whole business securitisation group. Companies in the whole business securitisation group raise debt in external debt markets through the issuance of secured bonds and the issue of loans. Thames Water Utilities Holdings Limited, Thames Water Utilities Limited, Thames Water Utilities Finance Limited, Thames Water Utilities Cayman Finance Holdings Limited and Thames Water Utilities Cayman Finance Limited have guaranteed the principal and interest payments due under the terms of the bonds. Where the Company enters into financial guarantee contracts to guarantee the indebtedness of other companies within this group, the Company considers these to be insurance arrangements and accounts for them as such. In this respect, the Company treats the guarantee contract as a contingent liability until such a time as it becomes probable that the Company will be required to make a payment under the guarantee.

Foreign currency

Transactions in foreign currencies are translated to sterling (the Company's functional and presentational currency) at the foreign exchange rate ruling at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies at the financial reporting date are retranslated to the functional currency at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement except for differences arising on the retranslation of qualifying cash flow hedges, which are recognised directly in the cash flow hedge reserve.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are retranslated to the functional currency at foreign exchange rates ruling at the dates the fair value was determined.

Dividends

Dividends unpaid at the financial reporting date are only recognised as a liability at that date to the extent that they are appropriately authorised and are no longer at the discretion of the Company. This occurs when the shareholders' right to receive payment has been established.

Unpaid dividends that do not meet these criteria are disclosed in the notes to the financial statements.

Impairment excluding inventories and deferred tax assets

Financial assets (including receivables)

A financial asset not carried at fair value through profit or loss is assessed at each financial reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset and can be measured reliably.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment is reversed through the income statement.

Trade receivables that are assessed not to be impaired individually are assessed collectively for impairment by reference to the Company's historical collection experience for receivables of a similar age.

Non-financial assets

The carrying amounts of the Company's non-financial assets, other than inventories and deferred tax assets, are reviewed at each financial reporting date to determine whether there is any indication of impairment. If any such indication exists then the assets recoverable amount are estimated.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generate cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit").

An impairment loss is recognised if the carrying amount of an asset or its cash generating unit exceeds its estimated recoverable amount. Impairment losses are recognised in the income statement. Impairment losses recognised in prior periods are assessed at each financial reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Taxation

Tax on the profit or loss for the period comprises current and deferred tax. Tax is recognised in the income statement except to the extent that it relates to items recognised directly within equity, in which case it is recognised within the statement of other comprehensive income.

Current tax

Current tax is the expected tax payable or receivable on the taxable income or loss for the period, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustments to tax payable in respect of previous periods.

Taxable profit differs from the profit on ordinary activities before tax as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other periods and items that are never taxable or deductible. It also includes the effect of tax allowances.

Deferred tax

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax is measured on a non-discounted basis using tax rates enacted or substantively enacted at the balance sheet date and that are expected to apply in the period when the deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised only to the extent that it is probable that sufficient future taxable profits will be available against which deductible temporary differences can be utilised.

Deferred tax assets and deferred tax liabilities are offset when there is a legally enforceable right to set off tax assets against tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Uncertain tax positions

Tax rules can be subject to interpretation and a tax provision is recognised where it is considered more likely than not that an amount will be paid to the tax authorities. Management use their experience, and seek professional advice where appropriate, to prudently assess the likelihood of an outflow arising. The amount recognised is the single most likely outcome.

New accounting policies and financial reporting changes

There has been no material introduction, removal or amendment of accounting policies during the year other than the policy adopted to separately present the cash collection arrangement with BTL (see revenue recognition policy above).

No new financial reporting standards have been adopted by the Company that have a material impact on the financial statements in the current year. The following issued standards have not yet been adopted by the Company:

- IFRS 9: *Financial instruments*, which will be effective on 1 January 2018 (and thus to the Company 1 April 2018);
- IFRS 15 *Revenue from Contracts with Customers*, which will be effective on 1 January 2018 (and thus to the Company 1 April 2018); and
- IFRS 16 *Leases*, which will be effective on 1 January 2019 (and thus to the Company 1 April 2019), subject to EU endorsement.

In addition to these, there are a number of other amendments and annual improvement project recommendations that are not yet effective but which have been endorsed by the EU. These are not anticipated to have a material impact on the consolidated financial statements of the Company.

IFRS 9 impact assessment

Management are conducting the assessment of the impact of IFRS 9 Financial Instruments on the Company. A review of the three phases of IFRS 9 is being conducted; Classification and Measurement, Impairment Methodology, and Hedge Accounting.

Classification and Measurement:

The review has included an assessment of the contractual cash flow characteristics of financial instruments, in order to determine their classification and measurement under IFRS 9. There are currently no indications that reclassifications of financial instruments will have a material impact on the financial statements.

Impairment Methodology:

Management have assessed the current accounting policies (see "Impairment excluding inventories and deferred tax assets" pages 122 to 123) in relation to financial assets not held at fair value through profit or loss, and specifically for financial assets held at amortised cost. This is in accordance with the treatment required for financial assets under IFRS 9. As a result there is no change expected in the Company's impairment methodology of financial assets, and therefore no material impact on the financial statements.

Hedge Accounting:

IFRS 9 provides increased flexibility for hedge accounting. An assessment is planned for the forthcoming financial year which will involve identifying and evaluating the potential impact of any existing contracts which are currently not hedge accounted, but may be eligible for hedge accounting under IFRS 9. Therefore, to date, it is not possible to estimate the impact of any changes in hedge accounting on the financial statements.

IFRS 15 impact assessment

Management have commenced a review of the contractual arrangements that comprise our current income streams to determine how IFRS 15 will impact the recognition and disclosure from these arrangements. The work performed to date has identified that, for the majority of the Company's income, the application of IFRS 15 will not have a material impact on the current revenue recognition under IAS 18: Revenue.

Further work is still required in 2017 to complete the reviews of certain revenue streams including those which relate to capital contributions. Final conclusions are being delayed whilst Ofwat consults on new development charging rules which look to formalise the definition of what infrastructure charges are intended to cover. The new charging rules framework is expected to come into effect on 1 April 2018.

The necessary processes required to capture adjustments and additional disclosures required under IFRS 15 will be considered in 2017.

IFRS 16 impact assessment

Management are conducting an impact assessment of IFRS 16 Leases on the Company's position and performance. The assessment involves a review for completeness that aims to identify agreements which are a lease, or contain a lease, as prescribed by IFRS 16. This has been done through a variety of methods, including contract reviews, data-mining, as well as departmental and onsite interviews and questionnaires.

The work performed to date has indicated that there will be a material impact to the statement of financial position primarily due to property leases for our major offices. The Company is subject to a loan covenant under which lease liabilities are classified as unsecured debt, the level of which cannot exceed a specified ratio. A risk that this covenant may be breached in future has been identified. Transition options on whether to apply IFRS 16 using a modified or fully retrospective approach are still being considered.

Work in this area is continuing. It is expected that final conclusions and quantitative results of the impact assessment will be completed during the year ending 31 March 2018.

Significant accounting judgements and key sources of estimation uncertainty

In the process of applying the Company's accounting policies, the Company is required to make certain judgements, estimates and assumptions that it believes are reasonable based on available information. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results may ultimately differ from these estimates.

Significant accounting judgements

Significant accounting judgements and key sources of estimation uncertainty which are also considered significant risks as set out in the Audit, Risk and Regulatory Committee Report, and Independent Auditor's Report are as follows:

Property, plant and equipment

The Company capitalises expenditure relating to water and wastewater infrastructure where such expenditure enhances or increases the capacity of the network. Maintenance expenditure is taken to the income statement in the period in which it is incurred. Differentiating enhancement from maintenance expenditure is subjective, particularly where a single project may include a mix of both types of activities. Additionally management capitalises employee time and other expenses incurred by central functions on capital programmes and consequently judgement is applied concerning the capitalisation rate used. Property, plant and equipment additions for the year ended 31 March 2017 were £1,115.3 million (2016: £1,198.7 million).

Calculation of the depreciation charge requires estimates to be made regarding the useful economic lives of the assets. These estimates are based on engineering data and the Company's experience of similar assets. If management identifies that actual useful economic lives differ materially from the estimates used to calculate the depreciation charge, that charge will be adjusted prospectively. The total depreciation charge for the year ended 31 March 2017 was £492.0 million (2016: £457.9 million).

The Company is required to evaluate the carrying values of PP&E for impairment whenever the circumstances indicate that the carrying value of those assets may not be recoverable. An impairment review requires management to make subjective judgements regarding the recoverable value and value in use of the assets under review.

Provision for doubtful debt

Provisions are made against trade receivables based on an assessment of the recovery of debts including those which will ultimately be cancelled, and may or may not be rebilled, and of debts which have not yet been billed but are part of the metered sales accrual. This assessment is made by reference to the Company's historical collection experience, including comparisons of the relative age of the individual balance and consideration of the actual write-off history. The actual level of receivables collected may differ from the estimated level of recovery which could affect operating results positively or negatively. The bad debt provision at 31 March 2017 was £176.4 million (2016: £189.7 million) as shown within note 15.

Provisions for other liabilities and charges

Assessing the financial outcome of uncertain commercial and legal cases requires judgement to be made regarding the extent to which any claim against the Company is likely to be successful after considering available information including notifications, settlements, estimates performed by independent parties and legal counsel, available facts, identification of other potentially responsible entities and their ability to contribute, and prior experience.

The required provision may change in the future due to new developments and as additional information becomes available and in such instances the provision will be adjusted prospectively. Provisions for liabilities and charges totalled £112.5 million at 31 March 2017 (2016: £97.6 million). A further breakdown of provisions can be found within note 21.

Other areas of accounting judgement and estimation uncertainty

The key assumptions and other sources of estimation uncertainty that are not considered significant risks are as follows:

Unbilled revenue

Revenue reflects the fair value of the consideration received, or receivable, in the ordinary course of business, excluding value added tax and trade discounts, for goods and services provided. Revenue is recognised at the time of delivery of the service and consequently payments received in advance of revenue recognition are recorded as deferred income.

The Company raises bills in accordance with its entitlement to receive revenue in line with the limits established by the Periodic Review. For water and wastewater customers with water meters, the amount recognised depends on the volume supplied including an estimate of the sales value of units supplied between the date of the last meter reading and the financial reporting date. Amounts recognised within revenue but unbilled at the financial reporting date are included within accrued income. Meters are read on a cyclical basis and the Company recognises revenue for unbilled amounts based on estimated usage from the last billing to the financial reporting date. The estimated usage is based on historical data and assumptions. The unbilled revenue for the year ended 31 March 2017 was £244.6 million (2016: £245.0 million) as shown within note 15.

Where actual results differ from estimates used, revenue is adjusted in the period for which the revision to the estimate is determined.

Retirement benefit obligations

The Company operates defined benefit pension schemes for which full actuarial valuations are carried out as determined by the Trustees at intervals of not more than three years. Determining the amount of the Company's retirement benefit obligations and the net costs of providing such benefits requires assumptions to be made including, but not restricted to, long term interest rates, inflation and rate of increases to pensions in payment. These are assessed using the advice of an independent qualified actuary, market observations and assumptions from the latest actuarial valuation. Changes in these assumptions could significantly affect the amount of obligations recognised and the cost of providing such benefits. The total retirement benefit obligation at 31 March 2017 was £379.8 million (2016: £260.0 million) as shown within note 23.

Fair value of derivatives

The fair value of the derivatives is determined by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates at the measurement date. The valuations are tested for reasonableness by comparing these to bank quotes. The fair value calculations have been adjusted to incorporate the Company's own and counterparty's credit risk where appropriate. A table detailing the fair value of financial assets and liabilities can be found within note 19.

Notes to the financial statements

1. Segmental analysis

IFRS 8 *Operating Segments* requires segmental information to be presented on the same basis as that used for internal management reporting. Segmental information is reported internally on a monthly basis by the individual business units to the Executive Committee. The Executive Committee, responsible for the day-to-day running of the business, is headed by the Chief Executive Officer and is also comprised of the Chief Financial Officer, the Strategy and Regulation Director and the Company's functional Directors. Consequently for the purposes of IFRS 8 the Executive Committee is considered to be the Chief Operating Decision Maker ("CODM") of the Company.

Management considers that the Company's reportable segments are those used by the Executive Committee for the purposes of resource allocation and to assess the Company's performance. These segments are also aligned with the internal business structure and the regulatory environment in which the Company operates, and therefore may differ from Ofwat definitions, which are as follows:

Retail: comprising both the household and non-household business units and provides certain customer-facing activities including billing and revenue collection. This includes billing and revenue collection in relation to BTL that is shown separately in the financial statements.

Water: responsible for all aspects of raw water abstraction and treatment as well as the distribution of high quality drinking water to household and non-household customers; and

Wastewater: responsible for all aspects of wastewater collection, treatment and safe disposal. Wastewater will be responsible for the construction of interface works to the Thames Tideway Tunnel.

The CODM reviews the non-household retail and household retail business units as a whole for the purposes of financial performance, monitoring and assessment and this is consistent with internal management reporting. The retail non-household and household business units have similar economic characteristics and are managed as one single business under a common Managing Director ("MD"), CFO and management team. Consequently these have been aggregated into a single reportable segment for the purposes of this financial statements disclosure. No other segments have been presented on an aggregated basis.

From 1 April 2017 the Company no longer provides non-household retail services since non-household customers have been transferred to Castle Water.

Other activities conducted by the Company primarily relate to certain non-regulated activities and shared corporate services that have not been included within the above segments. Management does not consider these activities to represent a separate reportable segment and consequently for the below disclosures they have been aggregated into a single caption designated "Unallocated".

The Company has a large and diverse customer base and consequently there is no significant reliance on any single customer such that no one customer exceeds 10% of total revenues in any reportable segment.

The Company is subject to economic regulation by Ofwat and operates under a licence to provide water and wastewater services within a defined geographical region, being London, the Thames Valley and the surrounding area. Therefore management considers there to be only one single geographical location of business.

Segmental performance

Transactions between reportable segments are included within segmental results in accordance with the Company's accounting policies. These are eliminated on production of the Company's financial statements, as shown within the reconciliation presented. Information regarding the performance results of each reportable segment are provided in line with that evaluated by the CODM and is based on Earnings before Interest and Tax ("EBIT").

Financial income and expenses are not allocated to the reportable segments as this activity is managed centrally by the Company's treasury function, which manages the overall cash and net debt position of the Company. Similarly the corporation tax credit or charge is not allocated to the individual reportable segments as this is considered to be borne by the Company as a whole.

A segmental analysis of revenue and EBIT has been presented overleaf:

1. Segmental analysis (continued)

Revenue and EBIT

Year ended 31 March 2017	Retail £m	Water £m	Wastewater £m	Unallocated £m	**Total £m**
External revenue excluding BTL	2,026.4	20.8	20.4	14.8	**2,082.4**
Reallocation of other income	-	-	-	(9.4)	**(9.4)**
BTL	-	-	-	33.6	**33.6**
Inter-segment revenue	(1,820.6)	816.4	1,004.2	-	**-**
Statutory reclassification of bad debt expense	-	-	-	(46.5)	**(46.5)**
Net statutory revenue	205.8	837.2	1,024.6	(7.5)	**2,060.1**
Operating expenses	(191.8)	(382.9)	(401.4)	(59.2)	**(1,035.3)**
Depreciation of property plant and equipment	(1.9)	(178.2)	(210.2)	(19.1)	**(409.4)**
Amortisation of intangible assets	-	-	-	(25.0)	**(25.0)**
Reconciliation to statutory operating expenditure:					
Statutory depreciation adjustments	-	-	-	(82.6)	**(82.6)**
Statutory adjustment to write-off costs of assets in development	-	-	-	(3.1)	**(3.1)**
Statutory reclassification of bad debt expense	-	-	-	46.5	**46.5**
Statutory reclassification of other operating income	-	-	-	(14.9)	**(14.9)**
Statutory reclassification of pension costs	-	-	-	11.3	**11.3**
Other	-	-	-	(2.9)	**(2.9)**
Total statutory operating expenditure	(193.7)	(561.1)	(611.6)	(149.0)	**(1,515.4)**
Profit on sale of property, plant and equipment	(4.0)	-	-	8.1	**4.1**
Other operating income	-	-	-	89.6	**89.6**
Earnings before interest and tax	8.1	276.1	413.0	(58.8)	**638.4**
Net finance expense including net fair value loss on financial instruments	-	-	-	(567.3)	**(567.3)**
Profit/(loss) before tax for the year	8.1	276.1	413.0	(626.1)	**71.1**

Year ended 31 March 2016	Retail £m	Water £m	Wastewater £m	Unallocated £m	**Total £m**
External revenue	2,033.3	19.4	9.0	15.5	**2,077.2**
Inter-segment revenue	(1,826.6)	816.0	1,010.6	-	**-**
Statutory reclassification of bad debt expense	-	-	-	(37.7)	**(37.7)**
Net revenue	206.7	835.4	1,019.6	(22.2)	**2,039.5**
Operating expenses	(182.5)	(365.4)	(384.8)	(48.0)	**(980.7)**
Depreciation	(1.3)	(165.8)	(189.7)	(18.4)	**(375.2)**
Amortisation	-	-	-	(17.9)	**(17.9)**
Reconciliation to statutory operating expenditure:					
Statutory depreciation adjustments	-	-	(0.9)	(81.8)	**(82.7)**
Statutory amortisation adjustments	-	-	-	(0.6)	**(0.6)**
Statutory reclassification of bad debt expense	-	-	-	37.7	**37.7**
Statutory reclassification of other operating income	-	-	-	(12.8)	**(12.8)**
Statutory reclassification of pension costs	-	-	-	14.0	**14.0**
Other	-	-	-	(1.2)	**(1.2)**
Total statutory operating expenditure	(183.8)	(531.2)	(575.4)	(129.0)	**(1,419.4)**
Profit on sale of property, plant and equipment	-	-	-	48.5	**48.5**
Other operating income	-	-	-	73.6	**73.6**
Earnings before interest and tax	22.9	304.2	444.2	(29.1)	**742.2**
Net finance expense including net fair value loss on financial instruments	-	-	-	(231.0)	**(231.0)**
Profit/(loss) before tax for the year	22.9	304.2	444.2	(260.1)	**511.2**

1. Segmental analysis (continued)

Segmental net assets

Separate segmental analysis of total assets and total liabilities are not reviewed by the CODM. Instead the information provided to the CODM comprises a measure of capital expenditure and segmental net assets. Certain centrally held provisions (including deferred tax liabilities), capitalised borrowing costs, external financing obligations and retirement benefit obligations are not allocated to the individual segments as they are considered to be borne by the Company as a whole.

A segmental analysis of the net asset position of each segment and level of capital expenditure is presented below:

As at 31 March 2017	Retail £m	Water £m	Wastewater £m	Unallocated £m	**Total £m**
Total assets	551.5	6,293.9	7,398.1	1,544.6	**15,788.1**
Total liabilities	(235.9)	(360.0)	(490.4)	(12,323.8)	**(13,410.1)**
Net assets/(liabilities)	315.6	5,933.9	6,907.7	(10,779.2)	**2,378.0**
Reconciliation to statutory net assets:					
Fair value asset	-	-	-	1,384.0	**1,384.0**
Depreciation of fair value asset	-	-	-	(244.9)	**(244.9)**
Capitalised borrowing costs	-	-	-	277.1	**277.1**
Fair value of self-lay sewers	-	-	-	46.3	**46.3**
Fair value of derivatives	-	-	-	(840.9)	**(840.9)**
Statutory pension adjustment	-	-	-	(144.5)	**(144.5)**
Tax adjustments	-	-	-	72.1	**72.1**
Other	-	-	-	(3.4)	**(3.4)**
Statutory net assets	315.6	5,933.9	6,907.7	(10,233.4)	**2,923.8**
Capital expenditure on property, plant and equipment and intangibles	41.1	443.0	451.1	282.8	**1,218.0**

As at 31 March 2016:	Retail £m	Water £m	Wastewater £m	Unallocated £m	**Total £m**
Total assets	470.9	4,909.1	6,480.6	1,388.6	**13,249.2**
Total liabilities	(205.6)	(230.1)	(443.0)	(10,273.5)	**(11,152.2)**
Net assets/(liabilities)	265.3	4,679.0	6,037.6	(8,884.9)	**2,097.0**
Reconciliation to statutory net assets:					
Fair value asset	-	-	-	1,384.0	**1,384.0**
Depreciation of fair value asset	-	-	-	(162.4)	**(162.4)**
Capitalised borrowing costs	-	-	-	200.8	**200.8**
Fair value of self-lay sewers	-	-	-	9.9	**9.9**
Fair value of derivatives	-	-	-	(392.6)	**(392.6)**
Statutory pension adjustment	-	-	-	(16.7)	**(16.7)**
Other	-	-	-	(6.3)	**(6.3)**
Statutory net assets/(liabilities)	265.3	4,679.0	6,037.6	(7,868.2)	**3,113.7**
Capital expenditure on property, plant and equipment and intangibles	26.1	387.0	644.9	168.0	**1,226.0**

2. Revenue

	2017			2016		
	Underlying £m	**BTL £m**	**Total £m**	Underlying £m	BTL £m	Total £m
Gross revenue	**2,073.0**	**33.6**	**2,106.6**	2,077.2	-	2,077.2
Charge for bad and doubtful debts	**(45.9)**	**(0.6)**	**(46.5)**	(37.7)	-	(37.7)
Total	**2,027.1**	**33.0**	**2,060.1**	2,039.5	-	2,039.5

All revenue is derived from activities based in the UK.

Bazalgette Tunnel Limited ("BTL") is responsible for the construction of the Thames Tideway Tunnel. For the year ended 31 March 2017 the Company has included construction costs of the Thames Tideway Tunnel within its bills to wastewater customers. Cash collected on BTL's behalf is subsequently paid over to them. The revenue on this arrangement, which is excluded from our key performance indicators, has been disclosed separately to the Company's underlying performance in the table above.

3. Operating expenses

	2017 Total £m	2016 Total £m
Wages and salaries	**210.6**	198.1
Social security costs	**23.3**	18.0
Pension costs – defined benefit schemes	**24.1**	23.5
Pension costs – defined contribution schemes	**6.8**	5.2
Severance costs	**1.1**	1.6
Release of restructuring provision in relation to severance costs	**-**	(5.4)
Total employee costs	**265.9**	241.0
Power	**104.3**	110.0
Carbon reduction commitment	**6.6**	6.2
Raw materials and consumables	**53.4**	44.8
Charge for bad and doubtful debts	**3.9**	27.3
Rates	**94.5**	93.6
Depreciation of property, plant and equipment	**492.0**	457.9
Amortisation of intangible assets	**25.0**	18.5
Write-off of costs from assets in development	**3.1**	-
Operating lease rental – plant and machinery	**1.0**	1.8
Operating lease rental – other	**15.1**	9.1
Research and development expenditure	**4.0**	3.1
Other operating costs	**634.8**	541.0
Gross operating costs	**1,703.6**	1,554.3
Own work capitalised	**(188.2)**	(134.9)
Net operating expenses	**1,515.4**	1,419.4

Amounts payable to the Company's auditor are shown below in respect of the following services to the Company:

	2017 £'000	2016 £'000
Fees payable to the Company's auditor:		
Fees payable for the audit of the Company's financial statements	**397**	374
Fees payable to the Company's auditor for other services:		
Audit related assurance services	**170**	155
Other assurance services	**403**	755
Other tax advisory services	**14**	16
Corporate finance services	**-**	570
Other services	**80**	224
Total aggregate remuneration	**1,064**	2,094

3. Operating expenses (continued)

Fees payable for the audit of the Company's financial statements include £30,000 (2016: £40,000) for out of pocket expenses incurred for delivery of the audit.

Fees for corporate finance services include £nil (2016: £0.6 million) in respect of advice on the Thames Tideway Tunnel. These costs have been capitalised as part of the design phase of the project. The contract was awarded to KPMG LLP in a prior year following a competitive tendering process in line with the Company's procurement procedures.

Other assurance services include certain agreed upon procedures performed by KPMG LLP in connection with the Company's regulatory reporting requirements for Ofwat.

No fees, other than those disclosed, were payable to KPMG LLP in respect of this Company in the current or preceding financial year.

4. Employees and Directors

Employees

All Company employees are based in the United Kingdom. The average number of persons employed by the Company (including Executive Directors) during the year, analysed by category, was as follows:

	2017 Number	2016 Number
Retail	**851**	937
Water	**1,850**	1,887
Wastewater	**1,861**	1,746
Group services	**405**	487
Total persons employed	**4,967**	5,057

Directors

The Directors' emoluments were as follows:

	2017 £'000	2016 £'000
Salary and fees	**1,563**	1,314
Pension and pension allowances	**183**	142
Bonus	**70**	426
Long-term incentive plan	**73**	418
Payment on loss of office	**1,583**	-
Other benefits	**459**	47
Total aggregate emoluments	**3,931**	2,347

Included in the table above, is £1,528,000 (2016: £1,602,000) for the Executive Directors for their services to the Company. In addition, the Executive Directors received total remuneration of £655,000 (2016: £687,000) for their services to other companies within the Group.

In the current and preceding financial years no amounts were accruing to any Directors under the Group's defined benefit scheme in respect of services to the Company. The Company contributed cash of £183,000 (2016: £142,000) as a pension supplement for five Directors (2016: two Directors). In the current and preceding years the Company made no contributions into the Company's defined contribution pension scheme in relation to the Directors.

Amounts disclosed in respect of the long-term incentive plan ("LTIP") are those where all performance and service conditions have been met. Detailed disclosures of items of remuneration, including those accruing under LTIPs can be found within the Remuneration Committee Report on pages 72 to 85.

Highest paid Director

Total emoluments, including payments and accruals under long term incentive schemes of the highest paid Director in respect of work done for the Company during the year were £918,000 (2016: £955,000). In addition, emoluments of £393,000 (2016: £410,000) were paid to the highest paid Director for services to other companies within the Group.

5. Other operating income

	2017 £m	2016 £m
Power income	**10.1**	8.0
Requisitions and diversions charges	**21.7**	22.6
Service connections charges	**25.4**	21.6
Release from deferred income – infrastructure charges	**15.4**	14.1
Rental income	**7.6**	7.3
Other income	**9.4**	-
Total	**89.6**	73.6

Power income comprises income from the sale of internally generated electricity.

6. Finance income and expense

Finance income

	2017 £m	2016 £m
Interest income on bank deposits	**2.8**	2.6
Interest income on intercompany loans receivable	**26.6**	27.4
Interest income on swaps	**65.1**	56.1
Total finance income	**94.5**	86.1

Finance expense

	2017 £m	2016 £m
Interest in relation to bank and other loans:		
Interest expense	**31.0**	23.9
RPI accretion on loans	**33.2**	12.7
Interest in relation to intercompany borrowings:		
Interest expense	**356.8**	351.6
RPI accretion on loans	**69.8**	33.7
Interest expense on swaps	**35.7**	25.4
Net interest expense on defined benefit obligation	**6.1**	10.4
Gross finance expense	**532.6**	457.7
Capitalised borrowing costs	**(76.3)**	(114.4)
Total finance expense	**456.3**	343.3

7. Net (losses)/gains on financial instruments

	2017 £m	2016 £m
Exchange losses on other loans	**(19.7)**	(11.2)
(Loss)/gain arising on swaps where hedge accounting is not applied	**(183.7)**	37.4
Loss on cash flow hedge transferred from equity	**(2.1)**	-
Total	**(205.5)**	26.2

8. Taxation

	2017 Underlying £m	2017 BTL £m	2017 Total £m	2016 Underlying £m	2016 BTL £m	2016 Total £m
Current tax:						
Amounts payable in respect of group relief	**6.4**	**2.2**	**8.6**	8.9	-	8.9
Adjustment in respect of prior periods – group relief	**-**	**-**	**-**	15.1	-	15.1
Current tax subtotal	**6.4**	**2.2**	**8.6**	24.0	-	24.0
Deferred tax:						
Origination and reversal of timing differences	**(9.9)**	**-**	**(9.9)**	76.8	-	76.8
Adjustment in respect of prior periods	**(7.0)**	**-**	**(7.0)**	(35.1)	-	(35.1)
Adjustment in respect of corporation tax rate changes	**(59.8)**	**-**	**(59.8)**	(120.9)	-	(120.9)
Deferred tax subtotal	**(76.7)**	**-**	**(76.7)**	(79.2)	-	(79.2)
Tax (credit)/charge on profit on ordinary activities	**(70.3)**	**2.2**	**(68.1)**	(55.2)	-	(55.2)

The tax charge for the year ended 31 March 2017 is lower (2016: lower) than the standard rate of corporation tax in the UK. The differences are explained below:

	2017 Underlying £m	2017 BTL £m	2017 Total £m	2017 Effective tax rate %	2016 Underlying £m	2016 BTL £m	2016 Total £m	2016 Effective tax rate %
Profit on ordinary activities before taxation	**38.1**	**33.0**	**71.1**		511.2	-	511.2	
Tax at 20% (2016: 20%)	**7.6**	**6.6**	**14.2**	**20.0%**	102.2	-	102.2	20.0%
Effects of:								
Recurring items								
Depreciation on assets that do not qualify for tax relief	**4.0**	**-**	**4.0**		4.1	-	4.1	
Disallowable expenditure [1]	**2.0**	**-**	**2.0**		2.6	-	2.6	
Non-taxable income [2]	**(5.2)**	**-**	**(5.2)**		(4.3)	-	(4.3)	
Property disposals [3]	**(0.1)**	**-**	**(0.1)**		(3.7)	-	(3.7)	
Group relief paid for at lower than statutory rate [4]	**(12.9)**	**(4.4)**	**(17.3)**		(15.2)	-	(15.2)	
Tax as adjusted for recurring items	**(4.6)**	**2.2**	**(2.4)**	**(3.4%)**	85.7	-	85.7	16.8%
Non-recurring items								
Tax rate change on temporary timing differences [5]	**(58.7)**	**-**	**(58.7)**		(120.9)	-	(120.9)	
Adjustments to tax charge in respect of prior periods – group relief	**-**	**-**	**-**		15.1	-	15.1	
Adjustments to tax charge in respect of prior periods – deferred tax [6]	**(7.0)**	**-**	**(7.0)**		(35.1)	-	(35.1)	
Total tax (credit)/charge	**(70.3)**	**2.2**	**(68.1)**	**(95.8%)**	(55.2)	-	(55.2)	(10.8%)

[1] Disallowable expenditure primarily relates to fines included in operating expenses.

[2] Non-taxable income relates to income from new service connections. This income is reflected in the accounts as non-taxable income under IFRS principles; however, such income is ultimately taxed through capital allowances.

[3] Tax chargeable on gains arising on property disposals is lower than the accounting profits recognised for these disposals because of additional deductions available for tax purposes.

8. Taxation (continued)

[4] The Company has decided to utilise tax losses available in its parent Company for the year ended 31 March 2017. As a result, the Company has reduced its claims for tax relief on its capital expenditure in the year. This tax relief is deferred to later periods and as a result, a deferred tax credit of £23.4 million is included in the current year deferred tax charge. The Company will pay £8.6 million to its parent Company for the tax losses, which is shown in the income statement as a current year current tax charge. The Company is paying for the tax losses at a rate which is lower than the standard rate of corporation tax, which reflects the value of the tax losses to the Company. This results in a reduction of the current tax charge of £17.3 million. Utilising tax losses in this way should ultimately benefit customers through lower tax funding in future regulatory settlements.

[5] A reduction in the UK corporation tax rate from 21% to 20% (effective from 1 April 2015) was substantively enacted on 2 July 2013. Further reductions to 19% (effective from 1 April 2017) and to 18% (effective 1 April 2020) were substantively enacted on 26 October 2015, and an additional reduction to 17% (effective 1 April 2020) was substantively enacted on 6 September 2016. This will reduce the Company's future current tax charge accordingly. The net deferred tax liability at 31 March 2017 has been calculated based on these rates. This has resulted in an overall deferred tax credit in the income statement of £59.8 million, which comprises a deferred tax release/(charge) in respect of fixed assets, cash flow hedges, retirement benefit obligations and other temporary differences of £62.4 million, (£3.8 million), £1.8 million and (£0.6 million) respectively.

[6] Following the agreement of tax computations with HMRC up to and including 31 March 2014, the provision for uncertain tax positions has been reduced resulting in a prior year deferred tax credit of £6.0 million, which is included in the total prior year deferred tax credit of £7.0 million.

The Company is not currently in a tax paying position with HMRC (although it does pay for group relief), primarily due to capital allowances on capital expenditure, tax deductions for borrowing costs and group relief which has arisen on interest expenses in holding companies. The differences between profit on ordinary activities before taxation at the standard tax rate and the current tax charge for the year are set out below.

	2017			2016		
	Underlying £m	**BTL £m**	**Total £m**	Underlying £m	BTL £m	Total £m
Profit on ordinary activities before taxation	**38.1**	**33.0**	**71.1**	511.2	-	511.2
Tax at 20%	**7.6**	**6.6**	**14.2**	102.2	-	102.2
Effects of:						
Depreciation on assets that do not qualify for relief	**4.0**	**-**	**4.0**	4.1	-	4.1
Disallowable expenditure	**2.0**	**-**	**2.0**	2.6	-	2.6
Non-taxable income	**(5.2)**	**-**	**(5.2)**	(4.3)	-	(4.3)
Property disposals	**(0.1)**	**-**	**(0.1)**	(3.7)	-	(3.7)
Capital allowances for the year in excess of depreciation	**(8.8)**	**-**	**(8.8)**	13.5	-	13.5
Tax effect of transition to IFRS [7]	**-**	**-**	**-**	(60.7)	-	(60.7)
Capitalised borrowing costs allowable for tax	**(15.3)**	**-**	**(15.3)**	(22.9)	-	(22.9)
Losses/(gains) on financial derivatives [8]	**35.2**	**-**	**35.2**	(8.1)	-	(8.1)
Pension cost charge in excess of pension contributions	**(6.3)**	**-**	**(6.3)**	3.9	-	3.9
Other short term timing differences	**6.3**	**-**	**6.3**	(2.5)	-	(2.5)
Group relief not paid at standard rate	**(13.0)**	**(4.4)**	**(17.4)**	(15.2)	-	(15.2)
Adjustments in respect of prior periods – group relief	**-**	**-**	**-**	15.1	-	15.1
Current tax charge for the year	**6.4**	**2.2**	**8.6**	24.0	-	24.0

[7] A one off tax deduction of approximately £300 million arose in the year ended 31 March 2016 following the transition to IFRS, resulting in a current tax reduction of £60.7 million in that year.

[8] Accounting fair value profits and losses arising on our derivatives are non-taxable and non-deductible respectively, as instead they are taxed as the cash flows arise. Deferred tax is provided on these temporary differences.

Uncertain tax positions

Provisions for uncertain corporation tax positions are included in the deferred tax liability as any liability is likely to crystallise as deferred tax. At 31 March 2017 the total value of these provisions was £0.3 million (2016: £6.3 million). It is possible that amounts agreed will be different from the amount provided.

8. Taxation (continued)

Effective tax rate

The effective tax rate, as adjusted for recurring tax items, of (3.4%) is low primarily due the effect of group relief paid for at below the statutory rate. Expected changes in tax legislation which are likely to be effective from 1 April 2017 may provide greater flexibility for tax losses carried forward in the parent Company, which may mean the Company does not claim tax losses from its parent in the future.

The deferred tax credited/(charged) directly to other comprehensive income during the year is as follows:

	2017 £m	2016 £m
Deferred tax:		
Tax on actuarial loss/(gain)	**21.6**	(30.8)
Tax on cash flow hedges	**6.1**	8.7
Total	**27.7**	(22.1)

9. Dividends

During the year, the Company paid total dividends of £157.0 million (2016: £82.4 million) to its immediate parent, Thames Water Utilities Holdings Limited. These dividends were distributed within the group as follows:

	2017 £m	2016 £m
Distribution to ultimate shareholders:		
External dividend distributions	**22.8**	-
Interest on Kemble Water Eurobond Plc debt	**77.2**	-
	100.0	-
Distributions not distributed to ultimate shareholders:		
Interest on Kemble Water Finance Limited debt	**55.0**	55.0
Distribution to Thames Water Limited	**2.0**	2.5
Distribution to Thames Water Utilities Holdings Limited	**-**	24.9
	57.0	82.4
Total	**157.0**	82.4

The aggregate amount of dividends proposed but not paid nor recognised as liabilities at the period end is £nil (2016: £nil).

Dividends paid to Kemble Water Finance Limited were used to enable it to continue to service its external debt. Dividends paid to Thames Water Utilities Holdings Limited were used to fund interest obligations of the Company. Dividends paid to Thames Water Limited were used to fund activities of the Company.

Further information on dividend payments can be found in Managing our Finances on page 37.

10. Intangible assets

	Software £m	Assets in development £m	**Total £m**
Cost:			
At 1 April 2015	141.6	-	**141.6**
Additions	10.4	16.9	**27.3**
At 31 March 2016	152.0	16.9	**168.9**
Additions	-	102.7	**102.7**
Transfers	37.6	(37.6)	**-**
Write-off	-	(3.1)	**(3.1)**
At 31 March 2017	189.6	78.9	**268.5**
Amortisation:			
At 1 April 2015	(84.5)	-	**(84.5)**
Amortisation charge	(18.5)	-	**(18.5)**
At 31 March 2016	(103.0)	-	**(103.0)**
Amortisation charge	(25.0)	-	**(25.0)**
At 31 March 2017	(128.0)	-	**(128.0)**
Net book value:			
At 31 March 2017	61.6	78.9	**140.5**
At 31 March 2016	49.0	16.9	**65.9**

The write-off of costs in the year ended 31 March 2017 relates to software under development that is no longer required as a result of the transfer of non-household customers to Castle Water.

11. Property, plant and equipment

	Land & buildings £m	Plant & equipment £m	Network assets £m	Assets under construction £m	**Total £m**
Cost:					
At 1 April 2015	3,300.6	5,830.0	5,368.0	2,312.0	**16,810.6**
Additions	-	-	5.1	1,193.6	**1,198.7**
Transfers between categories	47.8	364.1	1,102.2	(1,514.1)	**-**
Disposals	(27.2)	(2.2)	(0.1)	-	**(29.5)**
At 31 March 2016	3,321.2	6,191.9	6,475.2	1,991.5	**17,979.8**
Additions	-	24.2	15.9	1,075.2	**1,115.3**
Transfers between categories	95.0	626.3	255.9	(977.2)	**-**
Disposals	(3.7)	(3.8)	-	-	**(7.5)**
At 31 March 2017	3,412.5	6,838.6	6,747.0	2,089.5	**19,087.6**
Depreciation:					
At 1 April 2015	(811.8)	(3,144.2)	(120.8)	-	**(4,076.8)**
Depreciation charge	(49.0)	(285.3)	(123.6)	-	**(457.9)**
Disposals	26.0	1.8	0.1	-	**27.9**
At 31 March 2016	(834.8)	(3,427.7)	(244.3)	-	**(4,506.8)**
Depreciation charge	(52.7)	(318.8)	(120.5)	-	**(492.0)**
Disposals	2.0	3.7	-	-	**5.7**
At 31 March 2017	(885.5)	(3,742.8)	(364.8)	-	**(4,993.1)**
Net book value:					
At 31 March 2017	2,527.0	3,095.8	6,382.2	2,089.5	**14,094.5**
At 31 March 2016	2,486.4	2,764.2	6,230.9	1,991.5	**13,473.0**

£76.3 million borrowing costs were capitalised during the year (2016: £114.4 million). The effective rate of borrowing costs for the year was 4.86% (2016: 4.22%).

12. Investment in subsidiaries

	2017 £m	2016 £m
Cost of shares in subsidiary undertakings	**0.1**	0.1

The Company has no interest in joint ventures or associates. The Company had the following investments in subsidiary undertakings as at 31 March 2017:

	Holding	Principal undertaking	Country of incorporation	Class of shares held	Proportion of voting rights & shares held
Thames Water Utilities Finance Limited	Direct	Finance Company	United Kingdom	£1 Ordinary	100%
Thames Water Utilities Cayman Finance Holdings Limited	Direct	Holding Company	Cayman Islands	$1 Ordinary	100%
Thames Water Utilities Cayman Finance Limited	Indirect	Finance Company	Cayman Islands	$1 Ordinary	100%

All subsidiary undertakings are wholly owned by the Company.

The address of the registered office of Thames Water Utilities Finance Limited is Clearwater Court, Vastern Road, Reading, Berkshire, RG1 8DB. The address of the registered office for both Thames Water Utilities Cayman Finance Holdings Limited and Thames Water Utilities Cayman Finance Limited is PO Box 309GT, Ugland House, South Church Street, George Town, Grand Cayman, Cayman Islands. Both are, and always have been, resident in the United Kingdom for tax purposes.

13. Intercompany loans receivable

	2017 £m	2016 £m
Amounts owed by group undertakings:		
Thames Water Utilities Holdings Limited	**1,974.7**	2,015.0
Thames Water Utilities Finance Limited	**200.0**	200.0
Thames Water Utilities Cayman Finance Limited	**100.0**	100.0
	2,274.7	2,315.0
Interest receivable on amounts owed by group undertakings:		
Thames Water Utilities Holdings Limited	**7.2**	-
Thames Water Utilities Finance Limited	**9.4**	4.2
Thames Water Utilities Cayman Finance Limited	**0.2**	0.2
	16.8	4.4
Total	**2,291.5**	2,319.4
Disclosed within non-current assets	**2,274.7**	2,315.0
Disclosed within current assets	**16.8**	4.4

The above intercompany loans are unsecured and the Directors do not anticipate any repayment of the principal within 12 months. These balances have not been included within the Company's net debt and covenant calculations.

Interest on all of the above loans is charged at a floating rate (2016: floating rate).

14. Inventories and current intangible assets

	2017 £m	2016 £m
Raw materials and consumables	**14.1**	11.3
Current intangible assets – emissions allowances	**7.6**	9.4
Total	**21.7**	20.7

Emission allowances represent purchased carbon emission allowances (relating to the emission of carbon dioxide in the UK). A provision (see note 21) is simultaneously recorded in respect of the obligation to deliver emission allowances in the period in which the emissions are made and the associated charge is recognised as an operating expense within the income statement.

15. Trade and other receivables

	2017 Underlying £m	2017 BTL £m	2017 Total £m	2016 Underlying £m	2016 BTL £m	2016 Total £m
Non-current:						
Prepayments and accrued income	**-**	**30.4**	**30.4**	-	1.3	1.3
Other receivables	**2.8**	**-**	**2.8**	2.5	-	2.5
	2.8	**30.4**	**33.2**	2.5	1.3	3.8
Current:						
Gross trade receivables	**421.9**	**3.2**	**425.1**	409.3	-	409.3
Less doubtful debt provision	**(175.8)**	**(0.6)**	**(176.4)**	(189.7)	-	(189.7)
Net trade receivables	**246.1**	**2.6**	**248.7**	219.6	-	219.6
Amounts owed by group undertakings	**2.0**	**-**	**2.0**	1.1	-	1.1
Insurance claims receivable	**39.0**	**-**	**39.0**	20.3	-	20.3
Prepayments and accrued income	**286.2**	**0.4**	**286.6**	276.2	-	276.2
Other receivables	**60.9**	**-**	**60.9**	42.6	-	42.6
	634.2	**3.0**	**637.2**	559.8	-	559.8
Total	**637.0**	**33.4**	**670.4**	562.3	1.3	563.6

The Directors consider that the carrying amount of trade and other receivables is approximately equal to their fair value.

Prepayments and accrued income at 31 March 2017 includes £244.6 million (31 March 2016: £245.0 million) of water and wastewater income not billed.

Doubtful debts provision

Movements in the doubtful debts provision were as follows:

	2017 £m	2016 £m
At 1 April	**(189.7)**	(178.9)
Charge for bad and doubtful debts – charged against revenue	**(46.5)**	(37.7)
Charge for bad and doubtful debts – included within operating expenses	**(3.9)**	(27.3)
Amounts written off	**63.7**	54.2
Total at 31 March	**(176.4)**	(189.7)

The ageing of receivables which are past due but not impaired cannot be performed. Ageing of gross receivables is as follows:

	2017 £m	2016 £m
Up to 365 days	**252.0**	230.2
1 – 2 years	**77.4**	79.5
2 – 3 years	**41.5**	37.3
More than 3 years	**54.2**	62.3
Total	**425.1**	409.3

All BTL receivables are due in up to 365 days.

A collective provision is recorded against assets which are past due but for which no individual provision is made. This is calculated based on historical experience of levels of recovery. Ageing of impaired receivables is as follows:

	2017 £m	2016 £m
Up to 365 days	**71.5**	79.4
1 – 2 years	**32.7**	37.0
2 – 3 years	**23.7**	20.9
More than 3 years	**48.5**	52.4
Total	**176.4**	189.7

The bad debt provision for BTL receivables of £0.6 million relates to receivables due within 365 days.

16. Cash and cash equivalents

	2017 Underlying £m	2017 BTL £m	2017 Total £m	2016 Underlying £m	2016 BTL £m	2016 Total £m
Cash at bank and in hand	**2.1**	**3.8**	**5.9**	2.2	-	2.2
Short-term deposits	**50.6**	**-**	**50.6**	520.3	-	520.3
Total	**52.7**	**3.8**	**56.5**	522.5	-	522.5

BTL cash represents amounts collected from wastewater customers, for the construction costs of the Thames Tideway Tunnel, which has not yet been paid at the reporting date.

17. Trade and other payables

	2017 Underlying £m	2017 BTL £m	2017 Total £m	2016 Underlying £m	2016 BTL £m	2016 Total £m
Non-current:						
Accruals and deferred income	**404.9**	**-**	**404.9**	362.3	-	362.3
Current:						
Trade payables – operating	**282.9**	**-**	**282.9**	302.0	-	302.0
Trade payables – capital	**179.5**	**-**	**179.5**	206.9	-	206.9
Amounts owed to group undertakings	**1.1**	**-**	**1.1**	51.7	-	51.7
Other taxation and social security	**6.7**	**-**	**6.7**	5.7	-	5.7
Amounts payable in respect of group relief	**17.7**	**2.2**	**19.9**	11.3	-	11.3
Accruals and deferred income	**429.4**	**0.2**	**429.6**	284.2	-	284.2
Amounts owed to Bazalgette Tunnel Limited	**-**	**4.2**	**4.2**	-	1.5	1.5
Other payables	**7.1**	**-**	**7.1**	7.6	-	7.6
	924.4	**6.6**	**931.0**	869.4	1.5	870.9
Total	**1,329.3**	**6.6**	**1,335.9**	1,231.7	1.5	1,233.2

Accruals and deferred income at 31 March 2017 includes £81.1 million (31 March 2016: £85.7 million) of receipts in advance from customers for water and wastewater charges, and £97.3 million (31 March 2016: £nil) of net proceeds in relation to the transfer of all non-household retail customers to Castle Water.

Amounts owed to group undertakings at 31 March 2017 includes £nil (31 March 2016: £51.7 million) relating to the settlement of group relief.

The Directors consider that the carrying amount of trade and other payables is approximately equal to their fair value.

18. Borrowings

	2017 £m	2016 £m
Secured bank loans	**1,890.8**	2,220.2
Amounts owed to group undertakings	**8,732.6**	8,547.4
	10,623.4	10,767.6
Interest payable on secured bank loans	**4.3**	3.8
Interest payable on amounts owed to group undertakings	**179.2**	193.5
	183.5	197.3
Total	**10,806.9**	10,964.9
Disclosed within current liabilities	**383.4**	1,036.9
Disclosed within non-current liabilities	**10,423.5**	9,928.0
Total	**10,806.9**	10,964.9

Secured bank loans refers to an arrangement whereby each Obligor (representing each of the companies within the securitisation group) has entered into a Security Trust and Intercompany Deed ("STID") with the Security Trustee. Pursuant to this arrangement, Thames Water Utilities Holdings Limited has guaranteed the obligations of each other Obligor under the finance agreement. Additionally, Thames Water Utilities Limited, and its wholly owned subsidiaries, has guaranteed the obligations of each other under the finance agreement, in each case to the Security Trustee.

As at 31 March 2017, amounts owed to group undertakings, including interest, are unsecured and include the following:

- £2,888.3 million (2016: £2,856.3 million) owed to Thames Water Utilities Finance Limited, a subsidiary undertaking. Financing costs arising in Thames Water Utilities Finance Limited are directly recharged under mirrored interest terms for all loans except for one loan, a £225.0 million 6.59% secured bond due in 2021, which was loaned on with a margin of one basis point.
- £6,023.4 million (2016: £5,884.6 million) owed to Thames Water Utilities Cayman Finance Limited, a subsidiary undertaking. All costs are directly recharged under mirrored interest terms, and an additional margin of ten basis points.

Maturity analysis with respect to borrowings is presented in note 19.

Breakdown of secured bank loans

	2017 £m	2016 £m
£200.0m floating rate loan due 2017 (a), (g)	**-**	200.0
£150.0m floating rate loan due 2017	**150.0**	150.0
£200.0m 0% index linked loan due 2017	**-**	200.5
£100.0m floating rate loan due 2018 (a)	**99.9**	99.8
£60.0m 1.23% index linked loan due 2019	**73.9**	72.0
£60.0m 1.415% index linked loan due 2020	**73.7**	71.8
£60.0m 1.513% index linked loan due 2020	**73.3**	71.4
£60.0m 1.38% index linked loan due 2020	**73.1**	71.2
£60.0m 1.356% index linked loan due 2020	**73.1**	71.3
£100.0m floating rate loan due 2020 (a), (c)	**99.8**	99.7
£75.0m 1.35% index linked loan due 2021 (e)	**83.7**	81.6
£100.0m floating rate loan due 2021 (a), (c)	**99.7**	99.6
£215.0m 0.46% index linked loan due 2023 (a)	**232.6**	226.8
£215.0m 0.38% index linked loan due 2032 (a), (b)	**227.0**	221.3
£100.0m 3.28% index linked loan due 2043 (a), (d)	**121.5**	118.4
£100.0m 0.790% index linked loan due 2025 (a), (e)	**103.1**	100.5
£125.0m 0.598% index linked loan due 2026 (a), (e)	**128.2**	125.0
£70.0m Class B 3.867% fixed rate loan due 2026 (a)	**69.7**	69.4
£50.0m Class B 3.875% fixed rate loan due 2026 (a)	**49.8**	50.0
£20.0m Class B floating rate loan due 2026 (a)	**19.9**	19.9
£39.0m Class B 3.918% fixed rate loan due 2026 (a)	**38.8**	-
Total secured bank loans	**1,890.8**	2,220.2

(a) These loans are shown net of issue costs.
(b) This debt amortises in equal tranches from 2017 onwards.
(c) The interest margins of these two loans are based on a ratings grid and will increase should the securitisation group senior debt credit rating be downgraded by both Standard and Poor's and Moody's.
(d) This debt amortises from 2023 to 2033 in tranches of £3.0 million, followed by tranches of £750,000 until maturity where there will be a bullet payment of £25.0 million.
(e) These loans contain a collar mechanism that limits total accretion repayment within a predetermined range.
(f) All loans are Class A except where highlighted.
(g) This loan facility was originally due in 2015 but was subsequently extended to 2017.

18. Borrowings (continued)

Breakdown of amounts owed to group undertakings

These amounts are intercompany loans from Thames Water Utilities Finance Limited and Thames Water Utilities Cayman Finance Limited.

	2017 £m	2016 £m
£438.0m 3.64% fixed rate due 2016 (b)	-	438.1
£96.6m 5.20% class B fixed rate due 2019 (b), (d)	96.0	95.7
£100.0m 5.05% fixed rate due 2020 (c)	100.0	100.0
£225.0m 6.59% fixed rate due 2021 (c), (e)	225.0	225.0
£175.0m 3.38% index linked due 2021 (c), (d)	263.9	259.0
£100.0m 1.99% index linked due 2022 (b), (h)	112.9	110.0
£96.6m 4.15% fixed rate due 2022 (b)	96.6	96.6
£128.7m 4.30% fixed rate due 2024 (b)	128.8	128.8
£550.0m 5.37% class B Fixed rate due 2025 (b), (d), (i)	548.5	547.8
£161.1m 4.53% fixed rate due 2027 (b)	161.0	161.0
£330.0m 6.75% fixed rate due 2028 (c), (d)	327.3	327.2
£100.0m 1.79% index linked due 2029 (h), (c)	103.5	100.5
£300.0m 5.75% class B Fixed rate due 2030 (b), (j), (d)	297.5	297.2
£200.0m 6.50% fixed rate due 2032 (c), (d)	197.6	197.5
£300.0m 4.37% fixed rate due 2034 (b), (d)	295.3	295.1
£600.0m 5.13% fixed rate due 2037 (c), (d)	596.3	596.2
¥20.0bn 3.28% fixed rate due 2038 (b)	143.3	123.5
£200.0m 0.21% index linked due 2039 (c), (h)	209.3	203.3
£50.0m 3.85% index linked due 2040 (b), (f)	60.9	59.3
£500.0m 5.50% fixed rate due 2041 (b), (d)	489.4	489.6
£50.0m 1.98% index linked due 2042 (b)	64.4	62.9
£55.0m 2.09% index linked due 2042 (b), (d)	68.3	66.5
£40.0m 1.97% index linked due 2045 (b), (d)	45.6	45.5
£300.0m 4.63% fixed rate due 2046 (b), (d)	293.0	292.9
£100.0m 1.85% index linked due 2047 (b)	128.9	125.8
£200.0m 1.82% index linked due 2049 (b), (d)	257.3	251.0
£300.0m 1.68% index linked due 2053 (c), (d)	406.9	399.4
£300.0m 1.68% index linked due 2055 (c), (d)	406.9	399.4
£200.0m 1.77% index linked due 2057 (b), (d)	258.4	251.0
£400.0m 7.24% fixed rate due 2058 (a), (b), (d)	-	399.3
£100.0m index linked due 2060 (b)	103.7	100.6
£350.0m 1.76% index linked due 2062 (b), (d)	450.2	439.2
£500.0m 4.00% fixed rate due 2025 (b), (d)	494.8	494.3
£40.0m 0.75% index linked loan due 2034 (b), (d)	40.8	39.8
£45.0m 0.721% index linked loan due 2028 (b), (d)	45.8	44.6
£300.0m 3.5% fixed rate loan due 2028 (b), (d)	296.0	295.9
£400.0m 7.738% fixed rate bond due 2058 (a), (b), (d)	393.8	-
£250.0m 1.875% fixed rate bond due 2024 (b), (d)	247.4	-
£250.0m 2.625% fixed rate bond due 2032 (b), (d)	247.1	-
£42.0m floating rate loan due 2017 (b)	42.0	-
Fees (k)	(11.8)	(12.1)
Total amounts owed to group undertakings	8,732.6	8,547.4

(a) During the year, the £400m Class A Puttable, Callable, Resettable (PCR) bond issued by Thames Water Utilities Cayman Finance Limited with a final maturity of 9 April 2058 was exchanged for a new £400m Class A 2058 bond with the same final maturity.

(b) These loans are back-to-back inter-group loans from Thames Water Utilities Cayman Finance Limited to the Company. Thames Water Utilities Cayman Finance Limited charges the Company a margin of ten basis points in respect of the loans.

(c) These loans are back-to-back inter-group loans from Thames Water Utilities Finance Limited to the Company.

(d) These loans are shown net of issue costs.

(e) Thames Water Utilities Finance Limited charges the Company a margin of one basis point in respect of this loan.

(f) This is a Limited Price Index ("LPI") loan. Accretion charged is calculated using an adjusted UK Retail Price Index.

(g) All debt is class A except where highlighted.

(h) These amounts have been swapped into index linked debt within the financing subsidiary and the net proceeds lent to TWUL.

(i) In July 2017 this Bond has a 'Step Up and Call' meaning the interest rate changes to 3 months LIBOR plus 7.96% at which point the issuer can exercise a call option to redeem the nominal value of the debt at par value.

(j) In September 2022 this Bond has a 'Step Up and Call' meaning the interest rate changes to 3 months LIBOR plus 7.97% at which point the issuer can exercise a call option to redeem the nominal value of the debt at par value.

(k) These fees have been shown within amounts owed to group undertakings to reflect that they relate to index linked debt that was raised in Thames Water Utilities Cayman Finance Limited and passed on to TWUL.

19. Financial instruments

Categories of financial instruments

The carrying values of the financial assets and liabilities of the Company are as follows:

Financial assets:

	2017 £m	2016 £m
Fair value through profit and loss		
Options	-	336.4
Index Linked Swaps	83.0	-
Interest Rate Swaps	0.6	-
	83.6	336.4
Loans and receivables (including cash and cash equivalents)		
Amounts owed by group undertakings	2,291.5	2,319.4
Trade and other receivables	670.4	563.6
Short term investments	1.0	289.5
Cash and cash equivalents	56.5	522.5
Total	3,103.0	4,031.4

Financial liabilities:

	2017 £m	2016 £m
Fair value through profit and loss		
Options	-	(336.4)
Cross currency swaps – not hedge accounted	(71.6)	(86.4)
Interest rate swaps – not hedge accounted	(108.4)	(2.2)
Index-linked swaps – not hedge accounted	(589.2)	(296.5)
Derivatives designated as hedging instruments		
Forward starting interest rate swaps – cash flow hedges	(155.3)	(219.4)
	(924.5)	(940.9)
Other financial liabilities		
Trade and other payables	(1,335.9)	(1,233.2)
Borrowings	(10,806.9)	(10,964.9)
Total	(13,067.3)	(13,139.0)

Fair value measurements

The fair value of financial assets and liabilities represents the price that would be received to sell an asset or paid to transfer a liability between informed and willing parties, other than in a forced or liquidation sale at the measurement date. The techniques for determining the fair value of financial instruments are classified under the hierarchy defined in IFRS 13 *Fair Value Measurement* which categorises inputs to valuation techniques into levels 1-3 based on the degree to which the fair value is observable. Unless otherwise stated all of the Company's inputs to valuation techniques are level 2 – the fair value is determined from inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. The table below sets out the valuation basis of financial instruments held at fair value as at 31 March 2017:

	Level 2[1]	
	2017 £m	2016 £m
Financial assets – derivative financial instruments		
Options	-	336.4
Index-linked swaps	83.0	-
Interest rate swaps	0.6	-
Financial liabilities – derivative financial instruments		
Cross currency swaps	(71.6)	(86.4)
Interest rate swaps	(108.4)	(2.2)
Index-linked swaps	(589.2)	(296.5)
Forward starting interest rate swaps	(155.3)	(219.4)
Options	-	(336.4)
Net total	(840.9)	(604.5)

19. Financial instruments (continued)

[1]The fair value of derivative financial instruments, including interest rate swaps, cross currency swaps, index linked swaps and options, are measured using discounted cash flows. The future cash flows are estimated based on observable forward interest rates, inflation rates and discounted at a rate that reflects the credit risk of the Company and counterparties. Currency cash flows are translated at spot rate.

As at 31 March 2016, the Company held two offsetting options with equal and opposite values of £336.4 million. The Low Strike Call Option (LSCO) was recognised as a financial liability equal to the cost to the Company of settling the option in cash. An Assignable Call Option (ACO) was recognised as a financial asset equal to the reciprocal value to the Company of, instead, choosing to remarket the original bond for a 40 year period. During the year holders of the LSCO exercised their right to have the ACO assigned to them; TWUL then assigned the ACO to the LSCO holders. On assignment TWUL de-recognised both, the financial liability in relation to LSCO and the financial asset in relation to ACO.

In mid-2014 the Company executed £2.25 billion of forward-starting fixed to floating interest rate swaps of a 5-7 year maturity with various financial institutions to fix the future interest costs of an element of the new debt to be issued from 2017 to 2020. £500.0 million of forward-starting swaps commenced and were reclassified from forward starting interest rate swaps to interest rate swaps. Subsequent to 13 September 2016 the fair value movement on these swaps has been recognised as changes in fair value through the income statement and the cash flow hedge has been discontinued prospectively. As at 13 September 2016, £54.8 million was recognised within the cash flow hedge reserve related to these swaps. On 24 January 2017, Thames Water Utilities Cayman Finance Limited issued new bonds totalling £500.0 million and lent the proceeds to TWUL. As at 31 March 2017, £2.1 million out of £54.8 million has been recycled to the income statement.

On 16 March 2017 a further £400.0 million of forward-starting swaps commenced and were reclassified from forward starting interest rate swaps to interest rate swaps. Subsequent to 16 March 2017 the fair value movement on these swaps has been recognised as changes in fair value through the income statement and the cash flow hedge has been discontinued prospectively.

Comparison of fair value of financial instruments with their carrying amounts

The carrying amounts of the Company's trade and other receivables and trade and other payables are considered to be approximate to their fair values. The fair values and carrying values of the Company's other financial assets and financial liabilities are set out in the tables below.

Financial liabilities:

	2017		2016	
	Book value £m	**Fair value £m**	Book value £m	Fair value £m
Non-current				
Bank loans				
Floating rate	**(319.4)**	**(319.4)**	469.0	469.0
Index linked	**(1,256.3)**	**(1,687.7)**	1,231.2	1,231.2
Fixed rate	**(158.2)**	**(189.5)**	119.4	119.4
Amounts owed to group undertakings	**(8,689.6)**	**(12,153.9)**	8,108.4	10,335.7
Derivative financial instruments				
Cross currency swaps	**(71.6)**	**(71.6)**	86.4	86.4
Interest rate swaps	**(107.3)**	**(107.3)**	2.2	2.2
Index linked swaps	**(566.5)**	**(566.5)**	296.5	296.5
Forward starting interest rate swaps	**(155.3)**	**(155.3)**	219.4	219.4
Options	**-**	**-**	336.4	336.4
	(11,324.2)	**(15,251.2)**	10,868.9	13,096.2
Current				
Bank loans				
Floating rate	**(150.0)**	**(150.0)**	200.0	200.0
Index linked	**(6.9)**	**(6.9)**	200.5	200.5
Amounts owed to group undertakings	**(43.0)**	**(43.0)**	439.0	444.4
Interest payable	**(183.5)**	**(183.5)**	197.4	197.4
Derivative financial instruments				
Index linked swaps	**(22.7)**	**(22.7)**	-	-
Interest rate swaps	**(1.1)**	**(1.1)**	-	-
	(407.2)	**(407.2)**	1,036.9	1,042.3
Total	**(11,731.4)**	**(15,658.4)**	11,905.8	14,138.5

19. Financial instruments (continued)

Financial assets:

	2017		2016	
	Book value £m	**Fair value £m**	Book value £m	Fair value £m
Non-current				
Amounts owed by group undertakings	**2,274.7**	**2,274.7**	2,315.0	2,315.0
Derivative financial instruments	**83.6**	**83.6**	336.4	336.4
	2,358.3	**2,358.3**	2,651.4	2,651.4
Current				
Short term investments	**1.0**	**1.0**	289.5	289.5
Cash and cash equivalents	**56.5**	**56.5**	522.5	522.5
Amounts owed by group undertakings	**16.8**	**16.8**	4.4	4.4
	74.3	**74.3**	816.4	816.4
Total	**2,432.6**	**2,432.6**	3,467.8	3,467.8

Amounts owed to group entities include bonds and private placements issued by subsidiary entities, which are publicly traded and the proceeds from these transactions are loaned to the Company through intercompany agreements. The Company does not issue any bonds directly to the public markets.

The fair value of amounts owed to group entities represents the market value of the publicly traded underlying bonds and associated derivatives. For private placements the fair value is determined by discounting expected future cash flows using a risk-free rate plus the Company's credit spread.

The fair value of floating rate debt instruments is assumed to be the nominal value of the primary loan and adjusted for credit risk if this is significant. The fair value of index linked debt instruments is based on the nominal value of the debt plus accretion already accrued and accretion expected to accrue to maturity.

Capital risk management

Details of the Company's capital risk management strategy can be found on pages 39 to 40.

The capital structure of the Company consists of net debt and equity as follows:

	2017 £m	2016 £m
Cash and cash equivalents	**56.5**	522.5
Short term investments	**1.0**	289.5
Secured bank loans	**(1,890.8)**	(2,220.2)
Amounts owed to group undertakings	**(8,732.6)**	(8,547.4)
Interest payable on secured bank loans	**(4.3)**	(3.8)
Interest payable on amounts owed to group undertakings	**(179.2)**	(193.5)
Net debt (statutory basis)	**(10,749.4)**	(10,152.9)
Amounts owed to group undertakings	**300.0**	300.0
Interest payable on secured bank loans	**4.3**	3.8
Interest payable on amounts owed to group undertakings	**179.2**	193.5
Unamortised debt issuance costs and discount	**(75.2)**	(69.1)
Derivative financial liabilities	**(208.4)**	(198.6)
Net debt (covenant basis)	**(10,549.5)**	(9,923.3)
Equity attributable to owners of the Company	**2,923.8**	3,113.7

Net debt includes accrued interest on debt and excludes derivative accretion and foreign exchange net debt. In the prior year financial statements, we disclosed net debt of £10,154.2 million. This net debt excluded £197.3 million accrued interest on debt and included £198.6 million relating solely to accretion on index-linked swaps and the effect of movement in foreign exchange rate on one cross currency swap held by TWUL. After including interest on debt and excluding derivative accretion and foreign exchange net debt as at 31 March 2016 would have been £10,152.9 million.

Net debt (covenant basis) excludes amounts owed to group undertakings for which there is no related external debt, accrued interest, unamortised debt issuance costs and discounts, and includes derivative financial liabilities related solely to accretion on index-linked swaps and the effect of movement in foreign exchange rate to one cross currency swap held in TWUL. Amount owed to group undertaking include loan from intermediate subsidiaries, Thames Water Utilities Cayman Finance Limited of £100.0 million (2016: £100.0 million), and Thames Water Utilities Finance Limited of £200.0 million (2016: £200.0 million).

19. Financial instruments (continued)

Financial risk management

The Company's activities expose it to a number of financial risks: market risk (including interest rate risk and exchange rate risk), credit risk, liquidity risk and inflation risk. Details of the nature of each of these risks along with the steps the Company has taken to manage them is described on pages 39 to 40.

(a) Market risk

Below is the effective interest rate and foreign currency risk profile of the debt held by the Company after taking into account the derivative financial instruments used to manage market risk:

As at 31 March 2017:	Total at fixed rates £m	Total at floating rates £m	Total at RPI linked rates £m	**Total £m**
Interest bearing loans and borrowings				
Net of corresponding swap assets				
- £ Sterling	5,238.0	76.4	5,517.4	**10,831.8**

As at 31 March 2016:	Total at fixed rates £m	Total at floating rates £m	Total at RPI linked rates £m	**Total £m**
Interest bearing loans and borrowings				
Net of corresponding swap assets				
- £ Sterling	4,859.7	634.3	5,472.2	**10,966.2**

The weighted average interest rates of the debt held by the Company, after taking into account the derivative financial instruments used to manage market risk, and the period until maturity for which the rate is fixed and index-linked, are given below:

	Weighted average interest rate		Weighted average period until maturity	
	2017 %	2016 %	**2017 Years**	2016 Years
Fixed	**5.1**	5.1	**13.9**	14.8
Index-Linked	**3.9**	2.6	**23.7**	23.5

(i) Interest rate risk sensitivity analysis

The table below summarises the impact, on pre-tax profits, of 1% increase or decrease in interest rate at 31 March 2017. This analysis considers effect of variable interest rate instruments and assumes that all other variables, in particular exchange rates, remain constant.

	2017	**2017**	2016	2016
2016	**+1% £m**	**-1% £m**	+1% £m	-1% £m
Profit	**171.5**	**(189.1)**	63.3	(80.6)
Equity	**250.2**	**(272.2)**	197.2	(225.6)

(ii) Exchange rate sensitivity analysis

The table below summarises the impact of changes in the year end valuations of financial assets and liabilities denominated in foreign currency on pre-tax profits of a 10% strengthening or weakening of GBP (£) against the respective currencies in which the financial assets and liabilities are denominated at 31 March 2017. This analysis assumes that all other variables in the valuation remain constant.

	2017	**2017**	2016	2016
	+10% £m	**-10% £m**	+10% £m	-10% £m
Profit	**(6.8)**	**8.3**	(7.2)	11.3
Equity	**(6.8)**	**8.3**	(7.2)	11.3

19. Financial instruments (continued)

(iii) Inflation risk sensitivity analysis

The table below summarises the impact on pre-tax profits of a 1% increase or decrease in inflation rates at 31 March 2017. This analysis assumes that all other variables, in particular exchange rates, remain constant.

	2017	**2017**	2016	2016
	+1% £m	**-1% £m**	+1% £m	-1% £m
Profit	**(493.7)**	**387.9**	(439.9)	393.3
Equity	**(493.7)**	**387.9**	(439.9)	393.3

(b) Credit risk

The Company's maximum exposure to credit risk is the carrying amount of financial assets recorded in the financial statements, which is net of impairment losses, less collateral cash held under the terms of the whole business securitisation agreement explained on page 121.

The following table summarises amounts held on short term investments by credit rating of counterparties.

	2017 £m	2016 £m
AA-	**-**	17.0
A+	**-**	60.0
A	**1.0**	212.5
Total	**1.0**	289.5

The following table summarises fair value of derivatives assets by credit rating of counterparties.

	2017 £m	2016 £m
AA-	**0.2**	-
A+	**83.2**	-
A	**0.2**	166.9
A-	**-**	-
BBB+	**-**	169.5
Total	**83.6**	336.4

(c) Liquidity risk

Details of the nature and management of the Company's liquidity risk is provided on page 40.

The maturity profile of interest bearing loans and borrowings disclosed in the statement of financial position are given below.

	2017 £m	2016 £m
Within one year	**199.9**	839.6
Between one and two years	**210.8**	150.0
Between two and three years	**481.7**	195.5
Between three and four years	**314.6**	457.4
Between four and five years	**684.1**	199.6
After more than five years	**8,732.3**	8,925.5
Total	**10,623.4**	10,767.6

19. Financial instruments (continued)

(i) Cash flows from non-derivative financial liabilities

The maturity profile of the anticipated future cash flows including interest in relation to the Company's non-derivative financial liabilities on an undiscounted basis (excluding non-current trade payables), which, therefore, differs from both the carrying value disclosed in the statement of financial position and fair values, is as follows:

Undiscounted amounts payable	**2017 £m**	2016 £m
Within one year	**(1,483.4)**	(2,098.7)
Between one and two years	**(601.9)**	(503.6)
Between two and three years	**(973.0)**	(569.9)
Between three and four years	**(717.2)**	(932.6)
Between four and five years	**(1,125.0)**	(682.9)
After more than five years	**(21,997.2)**	(21,174.1)
Total	**(26,897.7)**	(25,961.8)

(ii) Cash flows from derivative financial instruments

The maturity profile of the Company's financial derivatives (which include options, interest rate swaps, cross currency swaps and index linked swaps), based on undiscounted cash flows, is as follows:

Undiscounted amounts payable	**2017 £m**	2016 £m
Within one year	**(21.9)**	29.5
Between one and two years	**1.3**	(40.1)
Between two and three years	**17.4**	(1.2)
Between three and four years	**16.8**	29.4
Between four and five years	**21.2**	28.9
After more than five years	**(1,202.0)**	(745.7)
Total	**(1,167.2)**	(699.2)

Cash flow hedges

The Company has designated a number of contracts which qualify, in accordance with IAS 39 Financial Instruments: Recognition and Measurement, as cash flow hedges. The accounting policy on cash flow hedges is explained on page 121.

In mid-2014 the Company executed £2.25 billion of forward-starting fixed to floating interest rate swaps of a 5-7 year maturity with various financial institutions to fix the future interest costs of an element of the new debt to be issued from 2017 to 2020. This protects the Company against adverse movements in underlying interest rates by matching debt issuance against a derivative instrument with fixed cash flow.

During the year £900.0 million of forward starting swaps commenced. These were reclassified from forward starting interest rate swaps to interest rate swaps and the cash flow hedge for these swaps has been discontinued prospectively, see Fair value measurements section above for more details.

The expected cash flows of the Company's cash flow hedging instruments are as follows:

Undiscounted amounts payable	**2017 £m**	2016 £m
Interest rate swaps		
Within one year	**(4.6)**	(2.2)
Between one and two years	**(15.3)**	(12.8)
Between two and three years	**(23.1)**	(20.2)
Between three and four years	**(25.5)**	(25.4)
Between four and five years	**(25.5)**	(27.1)
After more than five years	**(45.7)**	(66.9)
Total	**(139.7)**	(154.6)

In respect of the above cash flow hedges, a loss of £50.7 million was recognised in other comprehensive income in the year (2016: loss of £65.0 million). The amount reclassified from equity to profit or loss for the year was £2.1 million (2016: £nil).

20. Deferred tax

An analysis of movements in the major deferred tax liabilities and assets recognised by the Company is set out below:

	Accelerated depreciation £m	Retirement benefits £m	Cash flow hedge £m	Other £m	**Total £m**
At 1 April 2015	(1,204.8)	70.8	80.1	15.1	**(1,038.8)**
Credit/(charge) to income	99.4	6.8	(12.2)	(14.9)	**79.1**
(Charge)/credit to other comprehensive income	-	(30.8)	8.7	-	**(22.1)**
At 31 March 2016	(1,105.4)	46.8	76.6	0.2	**(981.8)**
Credit/(charge) to income	43.0	(3.8)	27.7	9.8	**76.7**
Credit to other comprehensive income	-	21.6	6.1	-	**27.7**
At 31 March 2017	(1,062.4)	64.6	110.4	10.0	**(877.4)**

Deferred tax assets and liabilities have been offset in the balance sheet. The offset amounts, which are to be recovered/settled after more than 12 months are as follows:

	2017 £m	2016 £m
Deferred tax asset	**185.0**	123.6
Deferred tax liability	**(1,062.4)**	(1,105.4)
Total	**(877.4)**	(981.8)

A deferred tax liability arises in respect of accelerated tax depreciation, because the rate of tax relief specified in UK tax legislation on most of our capital expenditure is quicker than the rate of accounting depreciation on that expenditure. These temporary differences unwind and affect current tax over the life of the relevant assets, but the continued high levels of capital investment within TWUL mean that the temporary differences currently tend to increase every year. The deferred tax liability is also affected by the UK corporation tax rate. The deferred tax credit of £43.0 million shown above comprises a deferred tax charge of £19.4 million on the net increase in temporary differences in the year, less a deferred tax credit of £62.4 million which arose from the enactment of the announced change of the future corporation tax rate from 18% to 17%.

Deferred tax assets have arisen on the following temporary differences:

- Retirement benefit obligations: A deferred tax asset is provided on the retirement benefit obligations booked in the accounts. Current tax relief will be available in the future for pension contributions paid to reduce these obligations. Deferred tax movements will also arise on any non-cash changes in the obligations, for example those arising from actuarial valuations.
- Cash flow hedge: A deferred tax asset is provided on certain fair values booked in respect of financial instruments in the accounts. Current tax relief will be available in the future as the cash flows arise over the lives of the derivatives. Deferred tax movements will also arise on any non-cash changes in the fair value of the derivatives.
- Other: A deferred tax asset is provided on the temporary differences arising on amounts for which a tax deduction is spread over a number of years in accordance with tax legislation, including certain pension contributions. Current tax relief will be available in future when tax relief is available in accordance with the legislation.

21. Provisions for liabilities and charges

	Emissions provision £m	Insured liabilities £m	Restructuring provision £m	AMP4 provision £m	Other provisions £m	**Total £m**
At 1 April 2015	-	45.7	12.3	7.7	32.2	**97.9**
Utilised during the year	-	-	(6.3)	(1.4)	(1.8)	**(9.5)**
Charge/(credit) to income statement	7.0	(0.3)	(5.4)	-	10.3	**11.6**
Transfer to current liabilities	-	-	-	(2.4)	-	**(2.4)**
At 31 March 2016	7.0	45.4	0.6	3.9	40.7	**97.6**
Utilised during the year	(6.5)	-	(0.4)	(2.2)	(13.1)	**(22.2)**
Charge to income statement	6.5	22.0	0.5	-	3.8	**32.8**
Transfer (to)/from current liabilities	-	-	-	(0.2)	4.5	**4.3**
At 31 March 2017	7.0	67.4	0.7	1.5	35.9	**112.5**

Emissions provisions relate to the obligation to purchase carbon emissions allowances.

21. Provisions for liabilities and charges (continued)

The insured liability provision arises from insurance claims from third parties received by the Company, and represents the estimated cost of settlement. Where we have insurance cover for these claims, we recognise the reimbursement value from captive and third party insurance companies net of retentions. The receivable is disclosed in note 15. Timing of settlement for these claims is uncertain and therefore amounts provided have been classified as non-current.

The AMP4 provision represents agreed settlement in respect of an information request received from Ofwat issued under section 203 of the Water Industry Act 1991 concerning the properties claimed as safeguarded from internal sewer flooding by capital schemes completed in 2009/10. The provision is utilised against contributions to various charity schemes. The associated outflows are expected to arise over AMP6.

Other provisions principally relate to a number of contractual and legal claims against the Group and potential fines for non-compliance with the various regulations the Group is obliged to meet. The amount recorded and represents management's best estimate of the value of settlement and associated costs. Timing of settlement for these claims is uncertain and therefore amounts provided have been classified as non-current.

22. Share capital and other reserves

Share capital

	2017 £m	2016 £m
Allotted, called up and fully paid:		
29,050,000 ordinary shares of £1 each	**29.0**	29.0

The Company has one class of ordinary share which carries no right to fixed income. The holders of ordinary shares are entitled to receive dividends as declared and are entitled to one vote per share at meetings of the Company.

Other reserves

	2017 £m	2016 £m
Share premium	**100.0**	100.0
Cash flow hedge reserve	**(222.4)**	(179.9)
Revaluation reserve	**1,053.1**	1,071.9
Retained earnings	**1,964.1**	2,092.7
Total	**2,894.8**	3,084.7

The revaluation reserve reflects the revaluation of infrastructure assets to fair value on transition to IFRS, net of deferred tax.

The cash flow hedge reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

23. Retirement benefit obligations

Background

The Company operates three pension schemes, one of which is a defined contribution scheme and the other two are defined benefit schemes.

In addition to the cost of the UK Pension arrangements, the Company operates arrangements under which it augments benefits on retirement in certain cases of redundancy. These augmentations are funded by way of additional employer contributions to the schemes. In the year to 31 March 2017 these related payments amounted to £0.5 million (2016: £2.2 million).

The defined contribution scheme was set up in April 2011, managed through Standard Life, and is open to all new employees of the Company. The pension charge for the year represents contributions payable by the Company to the scheme and amounted to £6.8 million (2016: £5.2 million).

There were £0.9 million (2016: £0.7 million) of outstanding contributions at the end of the year. These were paid in the following financial year in line with the scheme rules.

Defined benefit arrangements for the Company's eligible employees are provided through two defined benefit Group pension schemes:

- Thames Water Pension Scheme ("TWPS"); and
- Thames Water Mirror Image Pension Scheme ("TWMIPS").

Both represent career average pension schemes. Their assets are held separately from the rest of the Kemble Water Holdings Limited Group in funds in the United Kingdom which are independently administered by the Pension Trustees. On 1 April 2011 the defined benefit arrangements were closed to new entrants and replaced with a defined contribution scheme.

The most recent full actuarial valuation was at 31 March 2013 on behalf of the Trustees by AON Hewitt Limited, the independent and professionally qualified consulting actuary to the schemes. The 2013 valuation has been updated to 31 March 2017 by PricewaterhouseCoopers LLP, an independent and professionally qualified consulting actuary, using revised assumptions that are consistent with the requirements of IAS 19R *Employee Benefits* and shown in this note to the financial statements.

23. Retirement benefit obligations (continued)

The Company made a pension deficit repair payment of £24.0 million on 31 March 2017 in relation to 2016/17 having made a similar payment of £23.8 million on 1 April 2016 in relation to 2015/16. The Company expects to contribute approximately £41.1 million in aggregate to the defined benefit pension schemes in the next financial year.

Amounts included in the statement of financial position in respect of defined benefit pension schemes

The net pension liability recognised within the statement of financial position is as follows:

	2017		2016	
	TWPS £m	TWMIPS £m	TWPS £m	TWMIPS £m
Equities	533.5	212.0	430.1	146.4
Corporate bonds	185.1	71.2	74.5	68.7
LDI portfolio	607.7	495.2	571.8	488.0
Property	61.4	45.8	62.5	46.6
Cash	23.7	4.3	3.9	3.5
Fair value of scheme assets	1,411.4	828.5	1,142.8	753.2
Present value of defined benefit obligations	(1,776.2)	(806.8)	(1,385.1)	(694.8)
(Deficit)/surplus	(364.8)	21.7	(242.3)	58.4
Effect of asset limit	-	(36.7)	-	(76.1)
Retirement benefit obligations	(364.8)	(15.0)	(242.3)	(17.7)

The Directors have reviewed the scheme rules of the defined benefit pension schemes and have concluded that, for the TWMIPS scheme, as the Company does not have an unconditional right to a refund of any surplus, including as a deduction to future contributions payable, the provisions of IFRIC 14 apply. Consequently the surplus for this scheme has been restricted with an obligation recognised for the present value of deficit funding contributions payable to the scheme.

The movements in the fair value of scheme assets were as follows:

	2017		2016	
	TWPS £m	TWMIPS £m	TWPS £m	TWMIPS £m
At 1 April	1,142.8	753.2	1,146.2	773.9
Interest income on scheme assets	41.8	25.8	37.9	24.2
Contributions by sponsoring employers	51.6	10.0	12.1	2.3
Contributions from scheme members	0.1	-	0.1	-
Administration costs paid from scheme assets	(3.4)	(1.1)	(2.5)	(1.4)
Benefits paid	(45.5)	(39.9)	(40.4)	(37.7)
Contributions for termination benefits	0.5	-	1.4	0.9
Gains/(losses) on assets above interest	223.5	80.5	(12.0)	(9.0)
At 31 March	1,411.4	828.5	1,142.8	753.2

The movement in the present value of the defined benefit obligations were as follows:

	2017		2016	
	TWPS £m	TWMIPS £m	TWPS £m	TWMIPS £m
At 1 April	1,385.1	694.8	1,478.8	748.8
Current service cost	13.9	3.0	14.9	3.2
Interest cost	50.0	23.7	49.1	23.4
Contributions from scheme members	0.1	-	0.1	-
Benefits paid	(45.5)	(39.9)	(40.4)	(37.7)
Termination benefits	0.5	-	1.4	0.9
Actuarial losses/(gains)	372.1	125.2	(118.8)	(43.8)
At 31 March	1,776.2	806.8	1,385.1	694.8

23. Retirement benefit obligations (continued)

Amounts recognised in the income statement in respect of defined benefit pension schemes

	2017		2016	
	TWPS £m	**TWMIPS £m**	TWPS £m	TWMIPS £m
Current service cost	**13.9**	**3.0**	14.9	3.2
Scheme administration expenses	**3.4**	**1.1**	2.5	1.4
Effect of restriction of surplus	**-**	**2.7**	-	1.5
Net interest cost/(income)	**8.2**	**(2.1)**	11.2	(0.8)
Total	**25.5**	**4.7**	28.6	5.3

The net expense is recognised in the following captions within the income statement:

	2017		2016	
	TWPS £m	**TWMIPS £m**	TWPS £m	TWMIPS £m
Operating expenses	**17.3**	**6.8**	17.4	6.1
Net finance expense/(income)	**8.2**	**(2.1)**	11.2	(0.8)
Total	**25.5**	**4.7**	28.6	5.3

Actuarial gains and losses have been recognised within other comprehensive income. An analysis of the amount presented is set out below:

	2017 £m	2016 £m
Actual return less expected return on pension scheme assets	**304.0**	(21.0)
Experience gain arising on scheme liabilities	**28.7**	39.7
(Loss)/gain arising due to change in assumptions	**(526.0)**	122.9
Change in asset ceiling	**42.1**	(28.2)
Total actuarial (loss)/gain	**(151.2)**	113.4
Cumulative actuarial losses recognised	**(558.7)**	(407.5)

Actuarial risk factors

The schemes are exposed to actuarial risks including investment risk, inflation risk and longevity risk.

Investment risk arises because the Company's contributions to the schemes are based on expected returns from scheme assets based on actuarial assumptions. If these assets underperform a deficit will be created against the scheme liabilities.

The benefits payable to the members of the schemes are linked to inflation and as such higher inflation will lead to higher liabilities. The Company's contributions to the schemes are based on assumptions about the future levels of inflation. Therefore an increase in inflation above that assumed in the actuarial calculations will create a deficit.

The schemes' obligations are dependent on the assumptions about the life expectancy of the members after retirement. If scheme members live longer than assumed in the actuarial calculations, a deficit will be created.

23. Retirement benefit obligations (continued)

Actuarial assumptions

The main financial assumptions used in the valuation of these schemes are as follows:

	2017		2016	
	TWPS	**TWMIPS**	TWPS	TWMIPS
Price inflation – RPI	**3.35%**	**3.30%**	3.05%	2.95%
Price inflation – CPI	**2.35%**	**2.30%**	2.05%	1.95%
Rate of increases in salaries	**-**	**-**	-	-
Rate of increase to pensions in payment – RPI	**3.35%**	**3.30%**	3.05%	2.95%
Rate of increase to pensions in payment – CPI	**2.35%**	**2.30%**	2.05%	1.95%
Discount rate	**2.65%**	**2.55%**	3.65%	3.50%

Both schemes provide benefits on a Career Average ("CARE") benefit structure whereby past entitlements are linked to movements in CPI therefore an assumption for increase in salary is not required. In valuing the liabilities of the pension schemes, mortality assumptions have been made as indicated below. These mortality assumptions are based on standard mortality tables and the recent actual mortality experience of members within the schemes. The assumptions also allow for future improvements to mortality rates.

	2017		2016	
	TWPS Years	**TWMIPS Years**	TWPS Years	TWMIPS Years
Life expectancy from age 60:				
Male	**27.9**	**26.9**	28.3	27.3
Female	**29.4**	**29.3**	29.7	29.7
Life expectancy from age 60 currently age 40:				
Male	**29.8**	**28.8**	30.4	30.4
Female	**31.4**	**31.3**	31.8	31.8

The sensitivity of the present value of scheme liabilities to changes in the principal assumptions used is set out below:

	2017		2016	
	TWPS £m	**TWMIPS £m**	TWPS £m	TWMIPS £m
Change in discount rate (+ 1% p.a.)	**380.0**	**120.0**	260.0	100.0
Change in rate of inflation (- 1% p.a.)	**280.0**	**80.0**	220.0	60.0
Change in life expectancy (- 1 year)	**50.0**	**25.0**	40.0	20.0

24. Capital commitments

	2017 £m	2016 £m
Contracted for but not provided	**305.6**	489.9

In addition to these commitments, the Company has long-term capital investment plans, under its business plan submitted to Ofwat, to provide for future growth and maintenance of the infrastructure network.

25. Contingent liabilities

There are claims arising in the normal course of business, which are in the process of negotiation. The Company has set aside amounts considered appropriate for all legal and similar claims.

As at 31 March 2016 a contingent liability was disclosed in relation to the low strike call option. During the year, the related £400.0 million bond with a final maturity date of 9 April 2058 was exchanged for a new £400.0 million bond with the same final maturity (see note 18). The financial liability in relation to the low strike call option and the financial asset in relation to the assignable call option were both derecognised (see note 19).

In a prior period a debt to one of the Company's defined benefit pension schemes under section 75 of the Pensions Act 1995 arose in Thames Water Limited ("TWL"), an intermediary entity between the Company's immediate and ultimate parent, for the TWMIPS pension scheme as a result of a trigger event under that legislation. During the year, the Company and TWL entered into a "Flexible Apportionment Agreement" whereby the debt, estimated at between £1.0 million and £2.0 million by Aon Hewitt Limited, actuarial advisers to the TWMIPS trustees, was transferred to the Company. There are no changes to reported pension liabilities in the Company as a result of this agreement.

26. Operating leases

Lease payments under operating leases of £16.1 million (2016: £10.9 million) were recognised as an expense in the year.

At the balance sheet date, the group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2017 £m	2016 £m
Within one year	**7.6**	6.8
Between one and five years	**28.6**	27.2
After more than five years	**60.1**	66.7
Total	**96.3**	100.7

Operating lease payments represent rentals payable by the Company for certain office properties, and plant and equipment.

27. Off-balance sheet arrangements

The Company is party to a number of contractual arrangements for the purposes of its principal activities that are not required to be included within the statement of financial position. These are:

- operating leases;
- outsourcing contracts; and
- guarantees.

In respect of outsourcing contracts, the Company has entered into various arrangements to outsource the provision of certain back-office and operational functions with third party providers. These outsourced arrangements include aspects of legal services, metering and capital delivery. These arrangements are on commercial terms and no associated penalty or termination clauses will have a material effect on the financial position of the Company.

The Company is part of a Whole Business Securitisation group. Thames Water Utilities Holdings Limited, Thames Water Utilities Limited and its direct subsidiaries are Obligators under the whole business securitisation entered into in 2007. The Obligators have all entered into a Security Trust and Inter-creditor Deed. Under this document each Obligator will guarantee the obligations of each other Obligator with their future cash flows. The guaranteed debt as at 31 March 2017 was £10.6 billion (2016: £10.7 billion).

28. Statement of cash flows

Reconciliation of operating profit to operating cash flows

		2017			2016	
	Underlying £m	**BTL £m**	**Total £m**	Underlying £m	BTL £m	Total £m
Profit for the financial year	**108.4**	**30.8**	**139.2**	566.4	-	566.4
Less finance income	**(94.5)**	**-**	**(94.5)**	(86.1)	-	(86.1)
Add finance expense	**456.3**	**-**	**456.3**	343.3	-	343.3
Add loss/less (gain) on fair value of financial instruments	**205.5**	**-**	**205.5**	(26.2)	-	(26.2)
Add taxation on profit on ordinary activities	**(70.3)**	**2.2**	**(68.1)**	(55.2)	-	(55.2)
					-	
Operating profit	**605.4**	**33.0**	**638.4**	742.2	-	742.2
Depreciation on property, plant and equipment	**492.0**	**-**	**492.0**	457.9	-	457.9
Amortisation of intangible assets	**25.0**	**-**	**25.0**	18.5	-	18.5
Write-off of costs from assets in development	**3.1**	**-**	**3.1**			
Profit on sale of property, plant and equipment	**(4.1)**	**-**	**(4.1)**	(48.5)	-	(48.5)
Difference between pension charge and cash contribution	**(37.5)**	**-**	**(37.5)**	9.1	-	9.1
Increase in inventory	**(0.9)**	**-**	**(0.9)**	(9.5)	-	(9.5)
Increase in trade and other receivables	**(72.5)**	**(32.9)**	**(105.4)**	(3.9)	-	(3.9)
Increase in trade and other payables	**73.4**	**3.7**	**77.1**	14.4	-	14.4
Decrease in group relief payable	**(52.8)**	**-**	**(52.8)**	(22.0)	-	(22.0)
Increase/(decrease) in provisions	**14.9**	**-**	**14.9**	(0.3)	-	(0.3)
Cash generated from operations	**1,046.0**	**3.8**	**1,049.8**	1,157.9	-	1,157.9

No additions to property, plant and equipment during the year, or the immediately preceding year, were financed through new finance leases. Assets transferred from developers and customers for nil consideration were recognised at their fair value.

28. Statement of cash flows (continued)

Movement in cash and cash equivalents

	2017 £m	2016 £m
Unrestricted cash movement	**3.7**	-
Restricted cash movement	**-**	(7.6)
Movement in short-term deposits	**(469.7)**	9.2
Total	**(466.0)**	1.6

The restricted cash above relates to collateral posted by derivative counterparties that have failed to meet minimum credit rating criteria assigned by Moody's.

29. Related party transactions

Details of transactions with associated companies as required by Ofwat's regulatory accounting guidelines can be also found under the 'supply of trade' disclosure in the Annual Performance Report 2016/17 which will be published by 15 July 2017.

Trading transactions

	2017		2016	
	Services provided by the Company £'000	**Services provided to the Company £'000**	Services provided by the Company £'000	Services provided to the Company £'000
Intermediaries between the immediate and ultimate parent				
Thames Water Limited	**1,606**	**82**	1,788	46
Immediate parent				
Thames Water Utilities Holdings Limited	**19,736**	**166,708**	21,516	108,525
Subsidiaries				
Thames Water Utilities Cayman Finance Limited	**1,607**	**284,006**	1,736	255,715
Thames Water Utilities Finance Limited	**5,271**	**112,759**	4,146	127,398
Other entities within the Kemble Water Holdings group				
Kennet Properties Limited	**33**	**8**	105	28
Thames Water Commercial Services Limited	**1,401**	**-**	1,564	-
Thames Water Investments Limited	**-**	**-**	-	81
Thames Water Property Services Limited	**29**	**334**	32	447
Entities external to the Kemble Water Holdings group				
Alder & Allan Group Ltd	**-**	**-**	-	176
Arqiva Limited	**-**	**22,531**	-	15,717
Cranfield University	**-**	**125**	-	63
Macquarie Infrastructure and Real Assets (Europe) Limited	**-**	**3,602**	-	3,560
Royal Mail Plc	**-**	**19**	-	51
The Crown Estate	**-**	**-**	-	3
The Financial Reporting Council Ltd	**-**	**8**	-	-
The Institute of Water	**-**	**17**	-	3
Water UK	**-**	**595**	-	603
Total	**29,683**	**590,794**	30,887	512,416

The related party transactions were made on terms equivalent to those that prevail in arm's length transactions.

As at 31 March 2017, the Macquarie Group held a 26.3% shareholding in Kemble Water Holdings ("KWH") Group and qualified as an entity related to the KWH Group. During the year ended 31 March 2017 Macquarie Infrastructure and Real Assets (Europe) Limited, a wholly owned member of the Macquarie Group, provided Thames Water Utilities Limited with advisory services of £3.6m (2016: £3.6m).

29. Related party transactions (continued)

Outstanding balances

The following amounts were owed to the Company from related entities, and owed to related entities by the Company at the balance sheet date:

	2017		2016	
	Amounts owed to the Company £'000	**Amounts owed by the Company £'000**	Amounts owed to the Company £'000	Amounts owed by the Company £'000
Ultimate parent				
Kemble Water Holdings Limited	**5**	**-**	5	-
Intermediaries between the immediate and ultimate parent				
Kemble Water Finance Limited	**964**	**-**	1,064	-
Thames Water Limited	**18**	**1,081**	12	-
Immediate parent				
Thames Water Utilities Holdings Limited	**1,981,971**	**20,600**	2,015,000	63,758
Subsidiaries				
Thames Water Utilities Cayman Finance Limited	**162,788**	**6,084,372**	155,531	5,938,345
Thames Water Utilities Finance Limited	**221,156**	**2,900,055**	216,372	2,868,477
Other entities within the Kemble Water Holdings group				
Trans4m Limited	**-**	**-**	31	-
Entities external to the Kemble Water Holdings group				
Arqiva Limited	**-**	**1,159**	-	4,842
Water UK	**-**	**26**	-	184
Cranfield University	**-**	**-**	-	6
The Institute of Water	**-**	**-**	-	2
Total	**2,366,902**	**9,007,293**	2,388,015	8,875,614

The amounts outstanding are unsecured and will be settled in cash. No guarantees have been given or received. No provisions have been made for doubtful debts in respect of the amounts owed by related parties.

Key management personnel

Key management personnel comprise the members of the Board and of the Executive Committee during the year.

The remuneration of the Directors is included within the amounts disclosed below. Further information about the remuneration of individual Directors is provided in the audited part of the Remuneration Committee Report on pages 72 to 85.

	2017 £'000	2016 £'000
Fees	**819**	1,038
Salary	**2,162**	1,951
Pension and pension allowance	**333**	415
Bonus	**256**	1,178
Long-term incentive plan	**530**	978
Payment on loss of office	**1,583**	-
Redundancy	**520**	321
Other benefits	**529**	115
Total	**6,732**	5,996

Information regarding transactions with post-employment benefits plans is included in note 23.

30. Intermediate and ultimate parent Company and controlling party

Thames Water Utilities Holdings Limited, a company incorporated in the United Kingdom, is the immediate parent company. Kemble Water Finance Limited, a company incorporated in the United Kingdom, is an intermediate parent company and is the smallest group to consolidate these financial statements. The Directors consider that Kemble Water Holdings Limited, a company incorporated in the United Kingdom, is the ultimate and controlling party and the largest group to consolidate these financial statements.

The address of the registered office of Thames Water Utilities Holdings Limited, Kemble Water Finance Limited and Kemble Water Holdings Limited is Clearwater Court, Vastern Road, Reading, Berkshire, RG1 8DB. Copies of the accounts for all entities may be obtained from The Company Secretary's Office at this address.

31. Post balance sheet events

Shareholder changes in the ultimate parent company

During the year ended 31 March 2017 Kemble Water International Holdings Limited, an entity managed by the Macquarie Group, agreed to sell its full 26.315% shareholding in Kemble Water Holdings Limited, the ultimate parent company of the Company.

The legal transfer of shares was made on 31 May 2017 from Kemble Water International Holdings Limited, a company registered in Guernsey. Of the total shareholding in Kemble Water Holdings Limited, Farmoor Holdings B.V., an entity registered in the Netherlands and managed by Borealis Infrastructure Management Inc., a Canadian investment manager of the Ontario Municipal Employees Retirement System, received 17.543%, and Wren House Infrastructure Management Limited, the global direct infrastructure investment arm of the Kuwait Investment Authority, received 8.772%.

During the year ended 31 March 2017 SAS Trustee Corporation, agreed to sell its 2.389% shareholding in Kemble Water Holdings Limited to Aquila GP Inc., a Canadian entity managed by the Aquila Sonnet Limited Partnership. The legal transfer of shares was made on 25 April 2017. Following the transfer Aquila GP Inc. holds 4.995% of the total shareholding in Kemble Water Holdings Limited.

During the year ended 31 March 2017 QIC Diversified Infrastructure Limited, a company registered in Jersey, agreed to sell 3.336% of the total shareholding in Kemble Water Holdings Limited to QS Infrastructure Pty Ltd, an entity registered in Australia and managed by the QS UK Infrastructure Trust No. 1. The legal transfer of shares was made on 28 April 2017.At the same time QIC Diversified Infrastructure Limited transferred the remainder of their holding, 5.352% to QIC Infrastructure Management Pty Limited.

There will be no direct financial effect on the financial statements of the Company.

Transfer of non-household retail customers to Castle Water

From 1 April 2017 the Water Act 2014 allows all non-household customers to choose their supplier of water and wastewater retail services. On 18 July 2016, we announced our decision to exit the non-household retail market, and transfer our non-household customers to Castle Water Limited from the date of retail non-household water market opening. The Company continues to recognise wholesale revenue from these customers. On 1 April 2017 all non-household retail customers of Thames Water were transferred to Castle Water Limited which will result in the recognition of a profit on sale of the business. The sale did not become unconditional until the date of market opening (post year-end) and therefore the profit on sale, which we expect to be between £85.0 million and £87.0 million, will be recognised during the next financial year.

New bonds issued

A total of £550.0 million in new class B sterling bonds were issued by Thames Water Utilities Cayman Finance Limited on 3rd May 2017, with a £300.0 million tranche maturing in 2023 and £250.0 million maturing in 2027. The proceeds are expected to be used to fund the redemption of the existing £550.0 million class B bonds which mature in 2025 but have their first call date in July 2017.