GLAS CYMRU

REPORT & ACCOUNTS
2017—2018

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CHAIRMAN'S STATEMENT

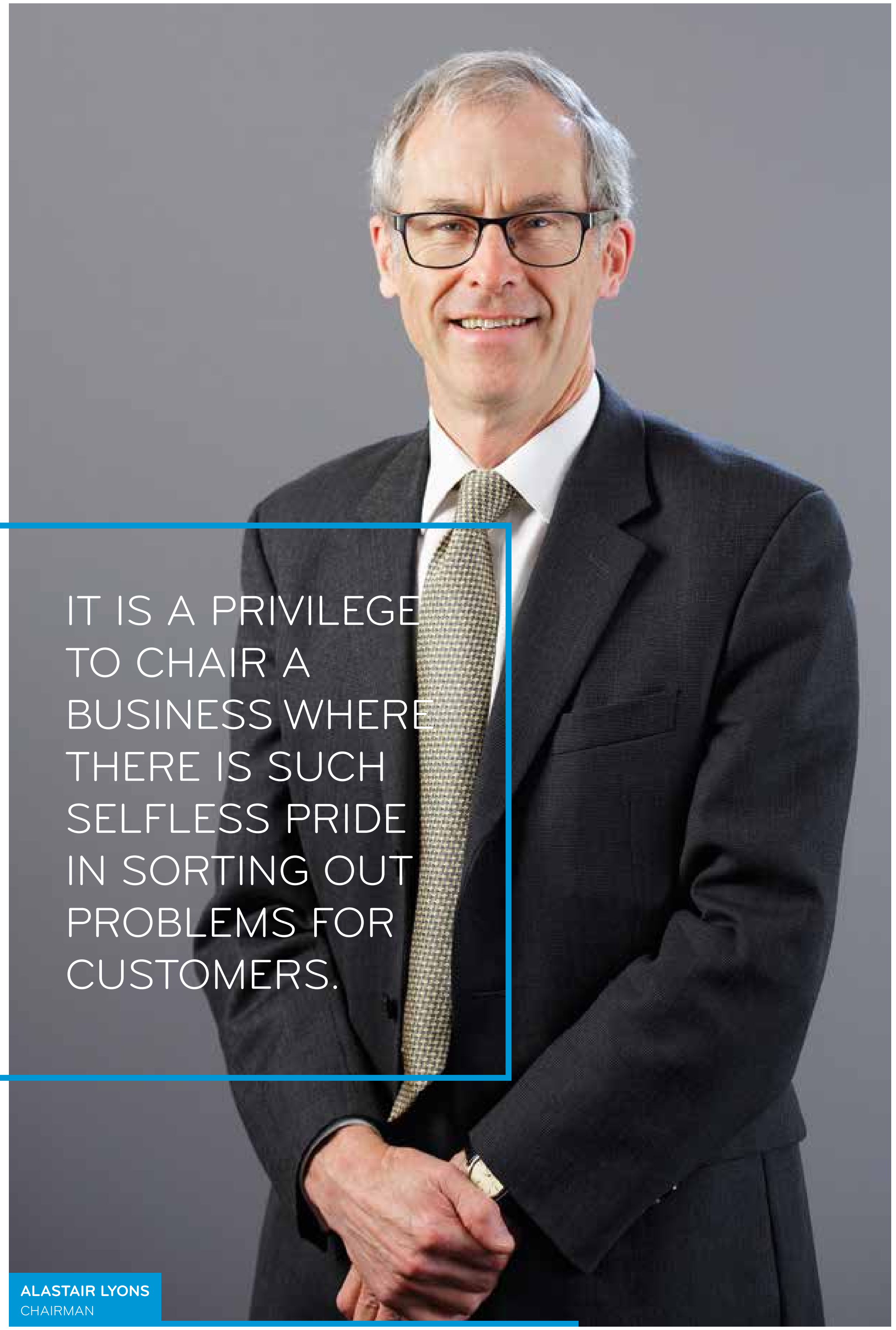
I began writing this statement whilst returning home from our early March board meeting – its second day should have run in Swansea from 9am until 2pm: in fact it ran in Cardiff from 8:30am until 10am. That's because 1st March turned out to be the worst day of winter weather since 2010 with a rare Met Office red weather warning in south Wales for snow. Our Executive Directors had more pressing operational matters to attend to than reporting on historical performance to the Board! I mention this because 1st March, and the subsequent days of harsh weather and following thaw, exemplified what makes the commitment of Welsh Water colleagues to our customers so special.

To bring this to life – in Gwent our maintenance team abandoned their vehicles and walked carrying their tools a mile through snow drifts up to two metres deep to fix problems at our Sluvad Water Treatment Works near Pontypool in order to maintain supply for nearly 600,000 customers in south-east Wales. At our call centre in St Mellons we had 150 of our people volunteer – and I mean volunteer! – to come in to help respond to the seven-fold increase in customer calls for support and help during the period of freeze followed by rapid thaw – with all the problems to which both extremes of weather gave rise. Over five days we had 1,800 people finding and fixing hundreds of leaks! In Ceredigion at our Strata Florida and Bontgoch water treatment works our operating team stayed at work all night to keep the works running despite then becoming snowed in by huge drifts.

It is a privilege to chair a business where there is such selfless pride in sorting out problems for customers, no matter the personal sacrifice of individual colleagues and teams.

Our business can be hugely unpredictable, in particular as a consequence of the weather we experience. Good weather in the summer can lead to high demand to put more water into the system quickly which in turn increases flow rates, disturbing sediment in areas of ageing cast iron trunk mains, and increasing customer contacts about the appearance of their water. Dry weather similarly reduces flows through the sewers, increasing the concentration of waste and making it more difficult to treat within prescribed environmental limits, and making odour issues more frequent. On the other hand frequent storms, of high intensity but short duration, trigger discharges into watercourses from the release mechanisms that prevent our sewers becoming overwhelmed whilst heavy rain on our upland catchments increases the run-off of pollutants, both natural and man-made, into our raw water sources, in turn changing the treatments required at our clean water production sites. So, after a dry hot period in 2017, our measure of customer acceptability did not achieve our objective whilst the trunk mains bursts that followed a cold snap shortly before Christmas, combined with the effects of Storm Emma, has led to failing our target for reliability of supply. However, to set these in context, we met, or over-achieved, against most of the other 25 operational water, wastewater and customer service targets for the year.

The role of the Board is, of course, to ensure the business is resilient to external shocks whether environmental, economic, or financial. Where that resilience is threatened, by single points of failure, ageing assets, scarce skills, or insufficient financial resources the Board needs to have a plan to achieve the required level of resilience. On the 14th March we launched Welsh Water 2050 at the Senedd, intended to provide a clear long-term framework for our future business planning to become a truly world class, resilient and sustainable water service for the benefit of future generations. Our not-for-shareholder ownership model makes it easier for us to focus on the long-term, particularly important for us as the provider



IT IS A PRIVILEGE TO CHAIR A BUSINESS WHERE THERE IS SUCH SELFLESS PRIDE IN SORTING OUT PROBLEMS FOR CUSTOMERS.

ALASTAIR LYONS
CHAIRMAN

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of an essential public service, with very long-lived assets. The opportunity to plan for the next 30 years differentiates us from companies which traditionally only planned for the length of the next price control, being five years. With an articulated vision of what type of business we would like to be in 2050, and what service we would aspire then to provide our customers, we can create the detailed plans of what we propose to achieve in each five-year price control along the journey to 2050: as I write the business is in the midst of creating these plans for innovation, incremental efficiency, and investment over the period of the next two price controls, being 2020-2030 and beyond, to achieve outcomes that are affordable, meet customers' service expectations and protect our environment for the benefit of future generations.

Welsh Water 2050 is centred around 18 strategic responses to the challenges that the future trends we can identify are likely to pose to our ability to deliver against our six fundamental customer promises:

- Clean, safe, drinking water for all
- Safeguard our environment for future generations
- Personal service that's right for you
- Fair bills for everyone
- Put things right if they go wrong
- A better future for all our communities

For each strategic response we outline in Welsh Water 2050 the outcomes we expect to achieve from the actions proposed, a broad indication of the range of possible investment required to deliver the actions, and how the outcomes meet the customer promises and the goals of the Well-being of Future Generations Act.

It is clear that significant investment will be required to deliver many of the strategic responses, particularly where the next 30 years will see a generational programme to replace aged iron mains or the creation of resilience by joining up supply systems to reduce the number of customers that can only be served from one supply source. However it is equally clear that over this timeframe there will be technological advances and new innovative practices that will present significant opportunities for reducing unit investment costs year on year. This is the challenge for management – to ensure that our objectives, and the plans that will make them possible, are affordable. One can, therefore, say that with such savings and in the context of our presently spending of the order of £500 million – £1 billion to improve service and resilience in each 5-yearly period, the direction of travel set out in Welsh Water 2050, whilst ambitious, is not implausible.

With our unique constitution Welsh Water exists to serve its customers and the communities of which they are a part. Whilst our management are expert in this industry and our Board has a depth of understanding from which to challenge management's plans of what we need to deliver to meet our regulatory requirements, it is for our customers to tell us what their priorities and their concerns are – which in turn form the base of our objectives. So we consulted deep and wide on Welsh Water 2050 across 2017 with input varying from 17 detailed responses from stakeholder groups and other interested parties to over 20,000 customers feeding back online and face-to-face. We have also been able to discuss all of this input over the period with our Customer Challenge Group, and I would like to thank Peter Davies (Chair of the Customer Challenge Group) for his regular contribution to our Board discussions.

WITH OUR UNIQUE CONSTITUTION WELSH WATER EXISTS TO SERVE ITS CUSTOMERS AND THE COMMUNITIES OF WHICH THEY ARE A PART

With inequality, debt, and poverty on the rise we must aim to ensure that our services remain affordable for all customers which includes providing support for those who struggle to pay. This is something on which we have also consulted with our customers who tell us both that they are willing to pay slightly higher bills so that we can offer a lower tariff to those who can't (rather than those who won't) pay a full bill, and that they are prepared for us to commit as support for such customers a part of the surplus that in other companies would be paid out as dividends to shareholders. With 105,000 customers on social tariffs as at 31 March 2018 Welsh Water has a greater take-up of such tariffs than any other UK water company and has added 27,520 over the course of the last year. At the same time it has become increasingly rigorous in pursuing those who won't pay, reducing the level of bad debt charge by around a quarter in recent years.

We recognise that being in financial difficulties is only one aspect of being potentially vulnerable as a customer. Also that vulnerability is a state that many people will experience at some point in their lives, particularly when the circumstances governing their lives change for some reason be it frailty in old age, ill health, bereavement, or loss of employment. Our challenge as a provider of an essential utility is to identify such vulnerable customers, determine how best to engage with them, and then develop ways we can mitigate those vulnerabilities, in particular by ensuring they are registered for priority services.
This is something to which the whole Welsh Water team can make a contribution from the meter reader who recognises that an elderly customer is somewhat frail and confused, to the maintenance gang who have to dig up the main outside the home of someone who is disabled, and the billing adviser who takes a call from a customer whose sight is so poor that the last bill cannot be read. We have ambitious targets to increase the number of our customers who are registered for Priority Services and the extent of take-up of those services.

IT IS CLEAR THAT SIGNIFICANT INVESTMENT WILL BE REQUIRED TO DELIVER MANY OF THE STRATEGIC RESPONSES

We have achieved an enormous amount over the last year – developing and consulting on Welsh Water 2050; using that framework to start to create the detailed plans for the next price control PR19 and the outline plans for the subsequent 10 years; and delivering in the round good outcomes for customers despite the challenges of wind and weather. May I, on behalf of the Board, say a huge thank you to everyone who has contributed to these achievements, whether directly employed by Welsh Water, or working alongside us within our Capital Alliance partners and our operational contractors. We are very fortunate to be supported by amazingly capable people within our supply chain. Last summer I visited the Caban Coch dam in the Elan Valley where we needed to replace four scour valves at the base of the dam which in turn made it necessary to block off temporarily on the wet side of the dam the pipes that lead to those valves. That required 150 deep water dives by specialist teams working at depths of up to 30 metres in practically zero visibility to isolate those pipes whilst maintaining the full supply from a live reservoir that serves three-quarters of a million households across Birmingham, Mid-Wales and Hereford – a truly spectacular achievement.

THE OPPORTUNITY TO PLAN FOR THE NEXT 30 YEARS DIFFERENTIATES US FROM THE WATER SECTOR AS A WHOLE

Finally I very much want to recognise the retirement from the Board of Stephen Palmer. Stephen joined the Board in 2009 and took over the chair of our Quality and Environmental Committee in 2013. Over this period he has made an enormous contribution to Welsh Water. With a scientific public health background as Professor of Epidemiology and Public Health at Cardiff University Stephen has brought an analytical rigour to the deliberations of the Quality and Environment Committee; and to our Board an incisive intellect and a deep concern for our impact on communities, particularly those in less fortunate circumstances. We will miss him greatly both as a director and as a friend.

As one door closes another opens – so we welcome Professor Tom Crick who was appointed a Non-Executive Director at the beginning of October. We count ourselves very fortunate to have Tom to replace Stephen. Like Stephen, Tom comes from a scientific background being Professor of Computer Science and Public Policy at Swansea University. He brings a deep domain knowledge of the digital world having previously advised the Office of the Chief Scientific Adviser for Wales and being currently an expert adviser to the Welsh Government and Chair of the National Network for Excellence in Science & Technology.

Alastair Lyons
Chairman

7 June 2018

STRATEGIC

THIS STRATEGIC REPORT DOCUMENTS OUR PERFORMANCE OVER THE YEAR, THE RISKS WE FACE AND HOW WE MITIGATE THEM, AND OUR FUTURE VISION AND STRATEGY.

STRATEGIC REPORT

CHIEF EXECUTIVE'S REVIEW

Our vision is "to earn the trust of our customers every day". This vision is fundamental to the way we work and is particularly appropriate for us as a non-shareholder owned company – the only one in the water sector in England and Wales.

The words "every day" have been particularly significant in the last year. We know that customers rely on us to deliver high-quality, safe and reliable services every day, no matter what is thrown at us by the weather or other operational challenges. They also need to be able to trust us to be planning well ahead, to ensure those services are sustainable and resilient over many decades to come. To achieve this, we will need ever greater efficiency and innovation, so that our major long-term programme of investment in our treatment works and networks can be balanced with keeping bills affordable for all.

The past year has presented good examples of the challenges we may face in future – including very hot summer periods which saw significantly increased demand on our water network, but punctuated with severe summer storms. We then faced several severe cold snaps in the winter – culminating in the widespread disruption we saw across our area from heavy snowfall during "Storm Emma" in March, which resulted in the greatest pressure on both our operational and customer service teams that we have seen since 2010.

While we have maintained a good overall operational performance last year, our challenge is not just to sustain high levels of service now but also to plan well ahead so that we can minimise the disruption experienced with similar events in the future.

WELSH WATER 2050

In March 2018, we published our final Welsh Water 2050 document, which sets out our long term vision for a truly resilient water business, which will help us to respond to the many challenges and opportunities that lie ahead – from climate and demographic change to the pace of technological progress and increasing customer expectations.

The 2050 vision sets out 18 "strategic responses" which we, our key stakeholders and our customers believe will help us to meet these challenges. Whilst many of these strategic responses will take a generation to fulfil, it is important that we make a start now to respond to foreseeable risks and trends, so that this can be done at an affordable pace and problems are not stored up for future generations to deal with in a reactive and ultimately much less efficient manner. We plan to carry out reviews of our long-term vision every five years to ensure it is delivering the best outcomes for our customers and we will report annually on our progress. It gives us considerable confidence in our innovative, long-term approach that our aims align so well with the well-being goals set out in the Welsh Government's Well-being of Future Generations Act 2015.

WE WILL NEED EVER GREATER EFFICIENCY AND INNOVATION

WELSH WATER 2050 SETS OUT OUR LONG TERM VISION FOR A TRULY RESILIENT WATER BUSINESS, WHICH WILL HELP US TO RESPOND TO THE MANY CHALLENGES AND OPPORTUNITIES THAT LIE AHEAD

EVERYTHING WE DO SHOULD BE GEARED TOWARDS THE BENEFIT OF OUR CUSTOMERS

CHRISTOPHER ALUN JONES
CHIEF EXECUTIVE

ONGOING ENGAGEMENT WITH CUSTOMERS

We can feel confident that our future strategy encompasses the broadest range of views possible following months of consultation – including an unprecedented 20,000 responses to our "Have Your Say" customer consultation in the summer of 2017. This represents our largest-ever volume of customer views – gathered from our presence at a number of high-profile events across Wales and Herefordshire, ongoing customer research, and digitally through our website and our bilingual chatbot – a world first!

Through the Have Your Say consultation and an in-depth customer research programme, we have developed a well-founded view of what our customers expect from us in terms of service and crucially the balance that they wish to see between investments to meet our long-term resilience plans, whilst keeping customer bills affordable. All this ongoing dialogue with customers will form the basis of our next five-year business plan, which we will submit to our regulator Ofwat in September 2018, setting an ambitious agenda for improved service to customers and investment in long-term resilience, while ensuring value for money and affordability.

We are committed to an ongoing programme of customer involvement on specific issues, such as how we can best-support customers in vulnerable circumstances. We also consult customers as to how we invest millions of pounds each year that in other companies would go to shareholders, so as to improve the service and value for money that we can deliver for customers in the future.

A positive development in this context is our new Online Community, which is an ongoing mechanism for customers who want to feed in to our plans on a regular basis – from our operational planning and customer communications, to how we best protect the natural environment. All our feedback from customers is vital to ensuring our customer-led way of working delivers the results that customers want and expect.

RESILIENCE

At the heart of Welsh Water 2050 is a plan to ensure our services are resilient to future shocks and challenges, and that we can ensure we provide the highest-quality services possible for decades to come.

For instance, we are planning investment over several five-year regulatory periods in drinking water resilience programmes that target areas that currently see the most frequent problems for our customers. We are already engaged in renewing over 20km of our water network in northern Herefordshire, while we are investing £23 million in a major upgrade of the drinking water network in the Rhondda Fach valley, to alleviate intermittent issues with loss of supply or discoloured water. Alongside this, we are piloting a project to create a first Water Resilient Community in the Rhondda Fach, making the local community a partner in all that we do to deliver local services. In an area which has some of the highest levels of deprivation that we serve, we are looking to take a different approach, which includes having an ongoing, genuine dialogue with local people to: minimise disruption from our essential work; provide guidance on how best to use our services more efficiently and save money, and raise awareness of the range of support available for those customers in vulnerable circumstances.

> CORPORATE AND FINANCIAL RESILIENCE ARE KEY TO MAINTAINING A TRULY RESILIENT BUSINESS IN THE LONG-TERM

We believe that resilience does not only mean having robust physical infrastructure but also applies more broadly to our activities. Corporate and financial resilience are key to maintaining a truly resilient business in the long-term. We are pleased that our strong financial position, built up over many years, means that we have the highest credit rating of all the utility companies in the UK, enabling us to continue to access low-cost borrowing such as the £300 million sterling bond issue in January this year. Such efficient financing plays a key part in enabling us to invest in our water and water services – with a record £431 million invested in our capital programme over the past 12 months – whilst keeping down price increases to customers – which rose on average by less than RPI inflation for the eighth year in a row.

AFFORDABILITY

One of our key priorities remains to continue our support for those who genuinely struggle to pay their water bills. It is a source of great pride to me that we and our customers as a whole now support around 105,000 low-earning households across the areas we serve – more than any other water company in the UK. We have worked with over 100 partner organisations to ensure that those who need our help most are supported in accessing it.

But our not-for-shareholder way of working also relies on customers who can pay their bills doing so – or we risk the rest of our customer base bearing an unfair burden. Our customers have consistently shown support for helping low-earning households, in part because of the trust they have in our not-for-shareholder model, but they do expect this to be balanced by everyone paying their fair share of the cost of providing this essential public service.

INNOVATION

We continue to embrace innovation across the company and believe that this will help make our future services better, faster and cheaper. With a range of external partner organisations, we hosted our first ever Hackathon (a "sprint-led design challenge") this year, which was aimed at helping us address a number of key challenges in wastewater services such as sewer blockages, environmental compliance and intermittent odour issues.

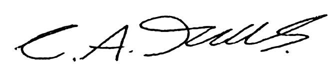
We held our annual Innovation Conference at Swansea University in January 2017, and at the Royal Welsh College of Music and Drama in Cardiff on 21 May 2018. Both events involved over 400 delegates in showcasing a range of ways we can deliver services more efficiently to communities – from programmes like our award-winning catchment management programme, which seeks to work with stakeholders across catchment areas to improve the quality of water before it reaches our treatment works, to the innovative use of data and technology to drive improvements in customer service. This includes technological advancements such as "augmented reality" – best encapsulated in our virtual reality "igloo" where we can project virtual images to provide a 360° visualisation to our designers, engineers and operational colleagues, enabling them to better design our future treatment works. These advances will deliver major efficiencies for our customers and allow us to do a better job for them and for the environment for years to come.

WELSH WATER PEOPLE

We can only hope to earn the trust of our customers through the extraordinary efforts and commitment of all our colleagues in Welsh Water and our wider network of contractors and partners. The past 12 months, particularly the challenges faced during Storm Emma, have again shown what skilled and dedicated colleagues we have, who will do their utmost to maintain services and do the right thing for the customers we serve and the environment which we all rely on.

> IT WILL BE ESSENTIAL THAT WE ALL STRIVE TO BUILD ON OUR SUCCESSES IN 2017-18

Whilst it is very encouraging to record that our latest, independent market research shows that 84% of our customers do believe that they can trust Welsh Water, it will be essential that we all strive to build on our successes in 2017-18, learning from the challenges that we have faced, so that we can continue to make significant steps on our journey to become a truly world class, resilient and sustainable water service for the benefit of future generations.



Chris Jones
Chief Executive

7 June 2018

OUR VALUES

OUR HISTORY: WHO WE ARE

Glas Cymru came into being in 2000 as a company "limited by guarantee", formed with the sole purpose of buying Dŵr Cymru Welsh Water, a goal which was achieved the following year.

Dŵr Cymru Welsh Water operates on a not-for-shareholder dividend basis – investing any money it makes back into the business to benefit customers and our networks; keeping bills down, and protecting the environment around us.

Since 2001, our primary objective has been to provide water and wastewater services, at an affordable price, to our customers. In such a capital-intensive industry, the way we operate and our corporate structure ensures we can finance large capital investment programmes necessary to ensure our services are high quality and reliable, at low risk and at as low as possible cost to our customers. Our capital investment programme is equivalent to over £1 million a day.

We are different from other water companies in England and Wales. We are not for shareholders, but for our customers. Serving our customers is our top priority – and we run all our services to benefit our customers.

WHAT DO WE DO?

OUR BUSINESS MODEL

We take water, treat it and distribute high-quality drinking water to three million people across our supply area.

We collect, treat, and safely return wastewater to our rivers and seas – protecting public health and the environment

We reuse part of our waste and convert it into energy that powers some of our sites, with the excess sold to the national grid so that we can ensure we keep prices for our customers as low as possible.

OUR VALUES

HOW WE DO IT

Welsh Water is the statutory undertaker for Water and Sewerage Services across its supply area, covering most of Wales, Herefordshire, and parts of Deeside and Cheshire. Our funding is regulated by Ofwat, the economic regulator of the water sector in England and Wales for five-year periods, the current period covering 2015-2020. The settlement (Price Review) at five yearly intervals determines the overall funding envelope within which we are challenged to provide services and to invest for the future in the most efficient way.

Our model is unique in the utilities sector, as any money the company makes doesn't go to shareholders in dividends, but back into the business to benefit our customers directly. This commitment to our customers forms the heart of our company vision.

Our focus on customer benefits has enabled us to:

- Keep average household bill price rises at, or below, the RPI rate of inflation for nine consecutive years – on course for a decade of such rises by 2020
- Obtain the best credit rating of any utility company in the UK, meaning we can borrow to invest in our services at the lowest possible cost for our customers
- Support more than 105,000 low-income customers to pay their water bills – more than any other company in England and Wales
- Generate added value for our household and business customers. Since 2001, we have applied over £353 million to the benefit of our customers through our not-for-shareholder "dividend".

In June 2017 we announced £34m Return of Value to be applied for the benefit of our customers which included commitments to invest

- £5m towards the cost of providing social tariffs for customers who struggle to pay the full amount of their bill;
- an additional £10 million in major replacement of ageing drinking water pipe network, including the Rhondda Valley, Hereford and Anglesey;
- more than £5 million towards extra investment in our visitor centres and recreational facilities, recreational access and biodiversity at Llyn Alaw reservoir on Anglesey, Swiss Valley reservoir in Llanelli and Lliw reservoir in Felindre, Swansea, and modernise our visitor centres at Llyn Brenig in Conwy and Elan Valley,
- £3.5 million extra to help reduce the 2,000 blockages a month in our sewer network which often result in flooding and pollution incidents, working with customers to "Stop the Block"
- £5 million for improvements to our water treatment works to make them more resilient to increased threats such as extreme weather
- £5 million to help improve customer service for households and businesses through new online systems, apps and over the telephone.

The primary focus of the Group is on ensuring that Welsh Water can carry out its fundamental obligation to provide water and wastewater services.

Our Commercial division (Welsh Water Infrastructure Limited) was set up in 2016 to undertake a limited number of projects connected to the water cycle or energy generation and based within the UK. These projects are designed to generate returns which either reduce operating costs or increase funds which can be part of our Return of Value to customers. In December 2017, Welsh Water Infrastructure Limited acquired the food and green waste recycling business of Kelda in Cardiff, which benefits from a contract to provide recycling services to Cardiff and Vale of Glamorgan Councils (page 39).

BUSINESS CUSTOMERS

Welsh Water serves around 110,000 business customers which range from water intensive manufacturers to small shops and hairdressers' salons. We know that the services we provide to businesses are essential – and we work to ensure we can help your business make the most efficient and cost effective use of water and wastewater services.

Business customers are supported to reduce their water usage, drive down energy costs, and reduce their carbon footprint.

DEVELOPER CUSTOMERS

Welsh Water provides services to housing, commercial and industrial developments, including major projects within our supply area, via our dedicated Developer Services team. In 2017-18, this team continued to attain consistently high levels of performance in the water sector's Levels of Service scheme for developers, as it has done since April 2015. This consistently high performance is industry leading across the sector in England and Wales.

OUR VALUES

HAVING YOUR SAY

Welsh Water is a customer-led company – we work to earn the trust of our customers every day, so they know that whatever happens, we are working in their interests. We recognise that in future, customers will expect a more personalised service and control over their use of services from us to ensure that these respond to their specific needs.

In line with our commitment to listen to our customers and act on what we hear, we launched our biggest ever consultation with customers last year. In the summer of 2017, we asked our customers how we should prioritise our investments for our next five-year business plan to 2025, but also for the long-term. This aligns with Welsh Water 2050 which sets out how we plan to tackle a range of long-term challenges facing the water industry.

We asked customers to prioritise the following options:

- Working with nature for cleaner water
- Making the water supply more reliable
- Better water quality for all
- Working with nature to reduce flooding and pollution risks
- Cleaner rivers and beaches
- Helping people who struggle to pay their bill
- Making things better for customers who are let down most often
- Giving more back to our communities

We reached a record of over 20,000 responses received over the 10 weeks the consultation was open, and we received the views of our customers in a number of ways, including:

- attendance at 10 key public events across Wales and Herefordshire including the National Eisteddfod, Royal Welsh Show and Pride Cymru;
- from a live bilingual Facebook Messenger chatbot;
- via feedback from our Customer Challenge Group;
- through our permanent customer forum Welsh Water Online Community

CASE STUDY

CHATBOT INNOVATION

Facebook now has around 44 million monthly active users in the UK. The chatbot, developed with Coup Media, meant we could engage with a huge potential audience on a platform they were familiar with using every day. It allowed us to reach demographic groups that are traditionally less likely to have their say—be that young people or hard-to-reach groups.

It was also a first for the Welsh language, with people able to have their say via a Messenger chatbot in the language for the very first time.

Over 2,942 customers took part in the 10-week consultation via the chatbot, with a further 17,000 having their say through our bespoke website and at events across the country.

This was coupled with detailed and ongoing input from customers through our Online Community, a range of customer focus groups and our new Youth Board. We also held a successful stakeholder launch event to gather the views of other key organisations and individuals. Over 100 stakeholders attended, including Glas Cymru Members.

WHAT HAVE WE DONE?

The results of our programme of engagement with customers and stakeholders have helped shape our Welsh Water 2050 vision, which helps us focus on the long-term, which is particularly important for us as the provider of an essential public service, and custodian of very long term assets.

We published this document in March 2018, following months of consultation, and will be using this as the basis to plan our long-term investments in our network, and the development of future services, to benefit our customers.

AWARDS

In December 2017, at the Utility Week Awards in London, our Communications and Customer Strategy Team won the Utility Week Marketing Initiative of the Year Award for the Have Your Say campaign. This was followed by three further awards at the UK-wide Chartered Institute of Marketing Awards in April 2018 with the campaign winning the Best Advertising Campaign, Best Brand Building Campaign and Best Use of Innovation.

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OUR WORK

YEAR IN REVIEW: 2017-18

APRIL 2017

OPEN WATER

On 1 April 2017, a new commercial retail market was introduced to increase competition in the water industry. More business customers can now choose their water and wastewater retailer. All business customers served by water companies based wholly or mainly in England can switch retailer for water and wastewater services. As a company "wholly or mainly" in Wales, the new market rules are different. Only Welsh Water's largest customer sites, those using more than 50 megalitres of water a year at a single site, can switch retailer, and only for clean water services. Our Commercial Retail Team provides business retail services for those eligible customers who don't want to switch to an alternative retailer. We are committed to providing all business customers, whether or not they can participate in the competitive retail market, with the highest standards of value and service.

MAY 2017

BLUE FLAGS

In May we received confirmation that Wales had received a record high 48 (45 beaches, three marinas) Blue Flags for the highest bathing water quality. Beaches and marinas must meet the highest, recommended European guideline standards and the beach must be clean, well-managed and promote sound environmental management. This reflects the work we have done to improve the quality of treated wastewater we release into our waterways, together with other organisations such as Welsh Government, Natural Resources Wales, the Environment Agency, and environmental charities.

JUNE 2017

CHAMPIONS' LEAGUE FINAL

Teams from across Water Distribution, Water Production, Wastewater Networks, Wastewater Production, Emergency Planning, Emergency Logistics, Streetworks, Sampling, the Operational Contact Centre and Communications were involved in preparation for the event, which saw more than 300,000 visitors visit Cardiff city centre. This particularly centred on preparing for widespread disruption to the city, but crucially made sure we were ready to respond to any emergencies, and that our network was ready to deal with significantly increased use of water and wastewater services.

JULY 2017

WOMENSPIRE AWARD

Our efforts to diversify our workforce and to encourage more women to take up careers in science, technology, engineering, and mathematics (STEM) areas was recognised by Welsh equality charity, Chwarae Teg, as Employer of the Year in their "Womenspire" Awards.

Employer of the Year in the Chwarae Teg "Womenspire" Awards

AUGUST 2017

HOT WEATHER WORK

Teams worked throughout the month to ensure services were maintained for customers – with a dry summer, interspersed with heavy rainfall events, meaning extra efforts were needed from our front line teams to maintain supply, avoid flooding, prevent leakage and ensure our waterways remained clear of pollution.

SEPTEMBER 2017

ABERCYNON AND ALWEN BURSTS

A burst on the major Taff trunk main near Abercynon meant colleagues were involved in a long-term repair to avoid any impact on the water supply of up to 26,000 households in the Taff Valley and Caerphilly areas. Operational teams also worked hard to maintain services following two consecutive bursts on the large diameter Alwen main in North East Wales.

OCTOBER 2017

DAM SAFETY

A second phase of highly complex, technical work to maintain the Caban Coch dam in the Elan Valley – involving specialist divers and the replacement of strategic scour valves – completed safely, ensuring the dam can operate efficiently for generations to come.

NOVEMBER 2017

YOUR COMMUNITY WORKS

We opened up a number of wastewater treatment works across our operating area – including Cog Moors, Treborth, Mold, and Leominster – to the public, so they could learn more about how our water and wastewater cycle works and how they can help us keep our networks flowing.

JANUARY 18

APPRENTICE AND GRADUATE RECRUITMENT

Our annual search for new talent across a number of apprenticeship and graduate positions opened – with roles covering Water Services, Wastewater Services, Retail Services, Developer Services and areas like data science and analysis, and in science, technology, engineering, and mathematics (STEM) roles.

FEBRUARY 2018

COLD WEATHER OPERATIONS

Extreme cold weather and significant snowfalls hit Wales on 28 February, which caused disruption across our network for the following two weeks, with pockets of the areas we serve experiencing prolonged disruption to our network. We operated on a round-the-clock, emergency footing – and managed to maintain 97.2% of our customers on supply throughout. However, this did represent the worst weather-related incident for Welsh Water since extreme cold weather in 2010 – with an estimated 7,000 customers off-supply for 24 hours or more when the rapid thaw led to a huge increase in the rate of leaks from our mains and customers' supply pipes.

We operated on a round-the-clock, emergency footing

DECEMBER 2017

WINTER BURSTS

Our operational teams were out working in the run up to Christmas on a series of bursts on a strategic water main in Aberdare – working for nearly 24 hours to maintain supplies and repair the damaged pipe. Colleagues in Cardiff also battled a burst which affected a number of properties in the Rumney and Llanrumney areas of Cardiff on Boxing Day, which saw teams working throughout the day and night to ensure customer supplies were restored as quickly as possible.

MARCH 18

WELSH WATER 2050

Our long-term strategy to tackle some of the biggest issues facing our services – ranging from climate change, to population growth, and the digital economy – was launched at a reception in the National Assembly for Wales in Cardiff Bay, attended by key stakeholders including Welsh Government Ministers, the Chief Executive of Ofwat and the Chair of National Resources Wales.

OUR WORK

EXTREME WEATHER — OUR CHALLENGE

We know that our customers place a particular emphasis on the reliability of essential services. One of the biggest challenges we faced over the past 12 months was the effect of extreme weather on our network — and the impact on some of our customers — in late February and March 2018 during "Storm Emma".

A period of very low temperatures and heavy snowfall, followed by a rapid thaw, placed unprecedented pressure on our network — both in terms of operational challenges in fixing burst pipes and leaks, and dealing with the concerns of our customers.

The initial cold weather — our operating area was in the centre of the exceptional 'red' weather warning for snow and ice — meant there was a greater risk of ground movement and damage to our water distribution network, particularly to our older, cast-iron pipes that still make up nearly 6,000km of our 27,500km network. It also meant it was very difficult for our engineers and operational colleagues to gain access to areas where there were significant snow drifts to repair the pipes, and to support customers who had lost their water supply. The severely adverse weather meant that large numbers of business premises remained unoccupied, and leaks on customer supply pipes were not quickly identifiable.

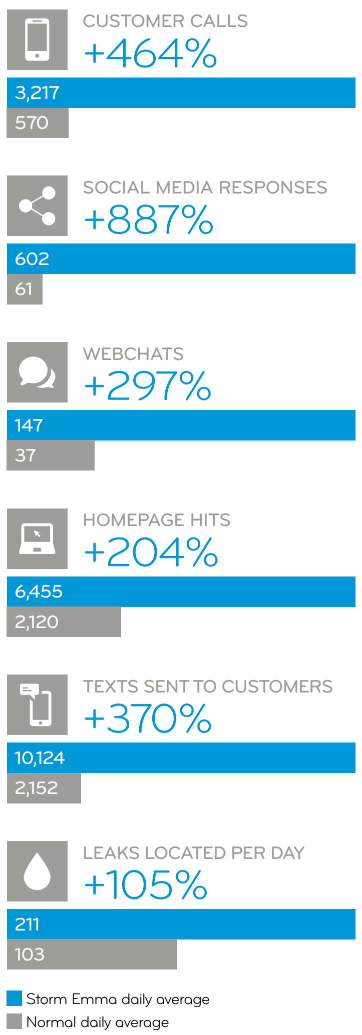
The rapid thaw caused some of our pipes to burst simultaneously across many areas of our network, meaning that some 2,541 incidents of supply interruptions were experienced across our network (affecting approximately 2.8% of our customers). In most cases, the interruptions to supply were brief and/or intermittent, however around 7,000 customers experienced interruptions to their water supply for 24 hours or more. This was particularly challenging in more rural, remote areas like Blaenau Ffestiniog, rural Pembrokeshire including St David's and Solva, areas of Anglesey, and rural parts of Mid Ceredigion. We are really sorry for the inconvenience and disruption caused to customers affected during this extremely challenging incident. During the thaw period our teams were repairing over 100 leaks per day.

Although we keep significant stocks of bottled water, getting this out to customers during the severe weather was particularly challenging. Colleagues from across the business helped out with distributing water supplies, capital projects teams assisted with emergency leakage repairs, and volunteers from support services teams worked shifts in our call centre to help respond to the additional demand from customers during this period.

The period was our largest incident response since similar extreme weather in 2010. Since then, we have invested money and resources in our preparation to respond to stresses on our network — and during Storm Emma we kept the water flowing to 97.2% of our customers throughout the cold snap and subsequent thaw.

STORM EMMA — IN NUMBERS

PERCENTAGE INCREASES



£7.2 MILLION

ESTIMATED ADDITIONAL COST INCURRED IN RESPONDING TO EXTREME WEATHER

300,000

LITRES OF WATER DELIVERED OR COLLECTED

240

LEAKS REPORTED PER DAY AT HEIGHT OF THAW

97.2%

OF CONNECTED PROPERTIES REMAINED ON SUPPLY THROUGHOUT

HOW DID WE PREPARE?

Following the cold snap of 2010, we built up one of the largest 4x4 fleets in Wales — meaning we could gain access to more rural, remote areas.

We also have one of the largest 'in-house' water tanker fleets of any UK water company with over 30 vehicles — and more tanker drivers on standby to help our immediate response to problems with our network.

We operated the military and wider civil emergency-based 'Bronze through to Gold' emergency planning standby arrangements. This was regionally-based and covered all our main operational response activities. Our Winter preparation plans were reviewed in November 2017.

We have two major emergency storage facilities with our primary centre at Clydach in Swansea and another at Dinas near Caernarfon. These house significant amounts of equipment. We had over 55,000 litres of bottled water in stock before the incident and purchased an additional 300,000 litres to assist with our response to customers who were off supply.

The first indication of severe weather was from the long range weather forecast, which is routinely monitored, on 24 February. Following this, our Winter response plans were checked across the business for readiness and additional leakage repair gangs were made available with the implications for resources assessed. Our website was modified to highlight our "Wrap up Wales" messaging, directing customers to specific advice on frozen pipes. Trigger points for further action in particular areas were established based on numbers of calls from customers reporting frozen supply pipes. We also reviewed our Priority Services Registers to assess vulnerability in freeze/thaw scenarios. From an operational perspective, the focus from this stage was on maintaining treatment works' outputs to maintain storage and avoid frozen pipes.

By 1 March, contingency travel measures were being put in place following the Met Office Red Weather Warning. In addition, amended staff rotas were brought into action, planning was taking place for anticipated high demand and bursts during the thaw period, and preparation was being made for alternative supplies through tankering, bowser and bottled water deployment. Our Bronze-Gold incident responses continued until 9 March.

But we know we have more work to do — and that for a small proportion of our customers, the service did not meet the high standards our customers can generally expect us to deliver.

In some rural and isolated communities, we took longer than we'd like to get their water supply restored — and to get support to them when they needed it. We will ensure that we take the learning points from this experience.

With increasingly volatile weather becoming more common, we review our serious incident planning regularly to see how we can achieve the optimal response to similar events in future. And we're investing to make sure our network is more resilient so the impact of these types of events will be minimised as much as possible.

PUTTING THINGS RIGHT

We recognise the scale of the problems during the severe weather was extremely disruptive for affected customers. So we decided to issue a goodwill payment to recognise that. Approximately 14,000 of those customers who were worst affected received a payment of £75, more than three times the payment issued under normal guaranteed standards of service, which we hope goes some way to show how committed we are to putting things right.

Our Zonal Studies programme is one of the initiatives that will help to make our network more resilient. This programme involves, over this five year investment period, £40 million of investment going into the areas that experience the most problems with the water supply — and the work includes replacing older cast-iron pipes with more resilient alternatives.

WHAT DID WE LEARN?

As this Annual Report goes to publication, we are awaiting the outcome of Ofwat's industry wide investigation into the response to the severe weather.

We have already carried out our own review and have identified areas of focus for future improvements to our response in extreme weather conditions:

- we will invest in additional "trace" heating at Water Treatment Works to lessen the likelihood of chemical lines freezing
- we will create a new role within the emergency response team to focus on providing quicker updates to local communities via our website and social media.
- we will invest in our own snow clearing capability to supplement highways authorities' provision in some rural areas
- we will put in place dedicated additional resource across the supply area to improve the distribution of bottled water where the mains supply is unavailable
- we will target part of our "Wrap Up Wales" winter campaign to business customers to try to raise awareness of the need to isolate supplies in unoccupied buildings during the winter period.

OUR WORK

HOW WE'RE DOING

To help us measure our performance, our Business Plan contains eight key 'outcomes' that we want to achieve by 2020 for our customers, communities and the wider environment. These outcomes are based on our customers' priorities from our consultation in 2013.

	MEASURE OF SUCCESS	OFWAT TARGET (2017-18 FD)	2017-18 OUTTURN VS OFWAT TARGET	2016-17	2017-18 OUTTURN	2017-18 VS PREVIOUS YEAR	2019-20 TARGET	ON COURSE TO MEET 2020 TARGET?
1	**HIGH QUALITY DRINKING WATER**							
A1A*	SAFETY IN DRINKING WATER (% COMPLIANCE)	-	-	99.99%	99.98%	✗	99.99%	✓
A1B*	SAFETY IN DRINKING WATER (MEAN ZONAL COMPLIANCE)	100%	✗	99.97%	99.96%	✗	100%	✗
A2*	CUSTOMER ACCEPTABILITY (CONTACTS P/1,000 POP)	-	-	2.88	2.79	✓	1.23	✗
A3	RELIABILITY OF SUPPLY (CUSTOMER MINUTES LOST)	12	✗	12.2	43.3	✗	12	✓
2	**PROTECTING THE ENVIRONMENT**							
B1	ABSTRACTION OF WATER FOR USE	100%	✓	100%	100%	✓	100%	✓
B2*	TREATING WASTEWATER	100%	✗	99.47%	98.21%	✗	100%	✗
B3A*	B3A PREVENTING POLLUTIONS (NUMBER OF POLLUTION INCIDENTS)	-	-	114	115	✗	131	✓
B3b*	B3B PREVENTING POLLUTIONS (CATEGORY 3 POLLUTION INCIDENTS ONLY)	131	✓	111	112	✗	131	✓
3	**RESPONDING TO CLIMATE CHANGE**							
C1	RESPONDING TO CLIMATE CHANGE	15,000	✓	13,661	15,097	✓	25,000	✓
C2	CARBON FOOTPRINT (GWH OF CLEAN ENERGY GENERATED)	70	✓	86.5	97.89	✓	100	✓

We measure our success towards achieving these outcomes against a number of targets — or Measures of Success — that we aim to meet or exceed every year. These targets are a combination of regulatory targets as agreed by our regulators and others set independently by the Glas Cymru Board. For further information, please see Appendix — Measures of Success: Definitions (page 138).

	MEASURE OF SUCCESS	OFWAT TARGET (2017-18 FD)	2017-18 OUTTURN VS OFWAT TARGET	2016-17	2017-18 OUTTURN	2017-18 VS PREVIOUS YEAR	2019-20 TARGET	ON COURSE TO MEET 2020 TARGET?
4	**CUSTOMER SERVICE**							
D1	SERVICE INCENTIVE MECHANISM (SIM)**	TOP QUARTILE	†	83	85	✓	TOP QUARTILE	✓
D2	AT RISK CUSTOMER SERVICE**	650	✓	575	613	✗	425	✓
D3	PROPERTIES FLOODED IN THE YEAR	292	✓	242	221	✓	269	✓
D4a	BUSINESS CUSTOMER SATISFACTION (%)			90.82	88	✗	-	-
D4b	NON HOUSEHOLD CUSTOMER SATISFACTION (%)	89%	✗	89	87	✗	90	✓
D5	EARNING THE TRUST OF CUSTOMERS (%)	68	✓	85	84	✗	75	✓
5	**AFFORDABLE BILLS**							
E1	AFFORDABLE BILLS (% BELOW INFLATION)	-1	✓	-1	-2	✓	-1	✓
E2	HELP FOR DISADVANTAGED CUSTOMERS	100,000		71,167	105.864	✓	100,000	✓
6	**LOOKING AFTER OUR ASSETS**							
F1	ASSET SERVICEABILITY	STABLE (X4)	✓	STABLE (X4)	STABLE (X4)	✓	STABLE	✓
F2	LEAKAGE (ML PER DAY)	173	✓	175.4	172.9	✓	169	✓
F3	ASSET RESILIENCE (WATER)	83	✓	89.5	90.4	✓	87	✓
F3	ASSET RESILIENCE (WASTE WATER)	74	✓	73.6	77.5	✓	78	✓
7	**DEVELOPING AND PROTECTING OUR PEOPLE**							
G1	RIDDOR INCIDENTS			12	14	✗	10	✓
G2	COMPETENCE IN ROLE			87%	82%	✗	95%	✓
8	**EFFICIENT BUSINESS**							
H1	FINANCING EFFICIENCY (CREDIT RATING)			A/A2/A	A/A2/A	✓	A/A3/A	✓

* Measured by the calendar year (January 2017 to December 2017). Other outcomes are measured by the financial year (April 2017 to March 2018).
** A definition of each Measure of Success can be found in Appendix 1 on pages 138-139.
† Final outturn not available until July 2018
A detailed comparison of our general performance on some key measures against that of other water and sewerage companies be viewed on **discoverwater.org**

OUR WORK – HOW WE'RE DOING

1

OUTCOME 1: HIGH QUALITY DRINKING WATER

FOR OUR CUSTOMERS, BEING ABLE TO RELY ON THE QUALITY OF THE WATER WE SUPPLY TO THEIR HOMES AND BUSINESSES IS THEIR HIGHEST PRIORITY AND EXPECTATION OF OUR SERVICE.

27,500KM

OF WATER PIPES ACROSS OUR AREA

£1.95 BILLION

INVESTED IN OUR ASSETS DURING THE CURRENT 5 YEAR INVESTMENT PERIOD

63

WATER TREATMENT WORKS ACROSS OUR AREA

Safety in Drinking Water
To protect water quality, we invested £213 million in our water services this year. Our water quality remains excellent but we had 46 failures of regulatory samples compared to 34 last year – which resulted in us just missing our targets for both performance measures (Compliance and Mean Zonal Compliance) which govern the safety of drinking water.

We measure water quality at our treatment works and storage reservoirs (which store treated water at points around the network). We delivered an excellent performance this year with just one instance of failure at our treatment works (2016-17: 1) and only two bacteriological failures at our service reservoirs (2016-17: 6) – our best ever performance.

Customer Acceptability
The number of contacts we receive from customers about the appearance, taste and odour of their water (Customer Acceptability) again improved this year to 2.79 complaints per 1,000 customers (2016-17: 2.88). While usually harmless, appearance, taste and odour issues can be off-putting for our customers. Such issues are often caused by changes in the velocity of water flows (for example, due to burst water mains or increased customer demand during hot weather), which can loosen iron sediments from within the pipes resulting in discoloured water.

During the year we dealt with some significant operational challenges, including having to supply up to 970 million litres per day during a period of hot weather in June when we normally supply approximately 800 million litres per day, but also by working to mitigate the customer impact of operational incidents during the year.

We continued to address the numbers of complaints about discolouration, by accelerating our pipe cleaning and replacement programme from 93.3km in 2016-17 to 320.8km this year. This work targets those communities most affected by this problem including the Rhondda in South Wales, Haverfordwest in Pembrokeshire and parts of Herefordshire and Anglesey. This is helping to reduce complaints about water discolouration but we still had 6,600 contacts from customers raising issues about discolouration of water supply over the year. We are planning to continue with this progress as we recognise that we have more to do in this area.

FLOW STOP REPAIR ON THE CADFOR, GWRYNE FAWR TRUNK MAIN SYSTEM

CASE STUDY

We pioneered new techniques of maintaining supplies to customers during operational incidents in 2017. Using 'flow stopping' technology, we successfully repaired two of our highest pressure pipelines in South and North Wales with minimal impact on customers. This helped us avoid having to interrupt water supplies to thousands of customers in order to carry out these works. We plan to use more of these innovative techniques in future to improve quality and reliability of supply for customers, whilst ensuring the safety of our colleagues and contractors.

Reliability of Supply
We always do our best to maintain water supply during any incidents by drawing in water from other parts of the network or tankering water directly into the network. This is not always possible due to engineering difficulties, problems with the surrounding network or due to health and safety risks faced by our colleagues, in particular during severe weather. As a result of the higher than usual number of operational incidents and the impact of the "Storm Emma" severe weather event, customers experienced an average of 43.3 minutes interruption to supply over the year, compared to an average interruption of 12 minutes 2 seconds the year before.

TO PROTECT WATER QUALITY, WE INVESTED £213 MILLION IN OUR WATER SERVICES THIS YEAR

1	HIGH QUALITY DRINKING WATER	2016-17	2017-18	17-18 VS 16-17
A1A	SAFETY IN DRINKING WATER (% COMPLIANCE)	99.99%	99.98	✗
A1B	SAFETY IN DRINKING WATER (% MEAN ZONAL COMPLIANCE)	99.97	99.96	✗
A2A	CUSTOMER ACCEPTABILITY (CONTACTS P/1,000 POP)*	2.88	2.79	✓
A3	RELIABILITY OF SUPPLY (MINUTES LOST/CUSTOMER)	12.2	43.3	✗

OUR WORK — HOW WE'RE DOING

2

OUTCOME 2: PROTECTING THE ENVIRONMENT

WE ARE WORKING TO ENSURE THAT THE BEAUTIFUL ENVIRONMENT AROUND US IS PROTECTED FOR FUTURE GENERATIONS

835
WASTEWATER TREATMENT WORKS

36,000KM
OF SEWER PIPES ACROSS OUR AREA

£7 MILLION
WE SPEND ANNUALLY UNBLOCKING SEWERS

Treating wastewater
Our environmental performance remained stable in 2017-18, with continued investment in our wastewater assets of £34 million helping to ensure 98.21% (down slightly from our best performance of 99.47% in 2016-17) of the wastewater being returned to our waterways met the standards required by Natural Resources Wales (NRW). This was made more challenging by periods of heavy rainfall and isolated failures of wastewater treatment works to meet required standards.

Preventing Pollution
We have continued to work with customers on our Let's Stop the Block campaign to raise awareness and improve education on disposing of appropriate material only into the sewer network to reduce blockages, which number around 2,000 a month and cost £7 million every year to correct. We are seeing good progress on reducing blockages generally, with sewer blockages down 7% in 2017-18 compared to the previous year.

The total number of pollution incidents in 2017-18 showed a very slight increase to 115 from 114 in the previous year. Of the total, the number of incidents from our wastewater system was 103, the fewest we have ever had. The remainder of the incidents were discharges from our Water Treatment Works, which can still have an impact on the environment. We are working to reduce the frequency of these incidents.

£34 MILLION INVESTMENT IN OUR WASTEWATER ASSETS

Bathing Water Quality
We also play an important role in ensuring the quality of bathing water around our operating areas is of the highest quality. We take the utmost care to ensure the water we treat and release into our rivers and seas is clean and safe and has minimal impact on the environment — and this is shown in the awarding of a record number of Blue Flag Awards given to beaches and marinas around Wales for 2017. A total of 43 beaches (plus 3 marinas and 1 boat operator) were recognised in Wales, which represents high standards in water quality and environmental management. All bathing water sites except one passed the required standards tested by NRW, with only Cemaes Bay on Anglesey receiving a "poor" rating. While there is no indication our activity has had a detrimental impact on water quality, we have been working with Anglesey Council, Llanbadrig Community Council, and NRW to help ensure water quality at this site improves in coming years.

WELSH WATER HOSTING MEMBERS OF THE UN'S URBAN RESILIENCE TEAM IN GRANGETOWN, CARDIFF

CASE STUDY

INVESTING OVER £2 MILLION IN GREENER GRANGETOWN

Cardiff Council, Welsh Water and Natural Resources Wales are investing over £2 million in Greener Grangetown, an innovative scheme to better manage rainwater in Cardiff's Grangetown area. Using the latest techniques, this scheme will collate and divert clean rainwater directly into the River Taff, instead of pumping it more than eight miles through the Vale of Glamorgan before treatment and discharge to the sea. As well as natural, planted areas that will help absorb rainwater, and increase biodiversity, the project will also provide the community with more green spaces to enjoy.

2	PROTECTING THE ENVIRONMENT	2016-17	2017-18	17-18 VS 16-17
B1	ABSTRACTION OF WATER FOR USE	100	100	✓
B2	TREATING WASTEWATER*	99.47%	98.21%	✕
B3A	B3A PREVENTING POLLUTIONS (NUMBER OF POLLUTION INCIDENTS)	114	115	✕
B3b	B3B PREVENTING POLLUTIONS (CATEGORY 3 POLLUTION INCIDENTS ONLY)	111	112	✕

OUR WORK – HOW WE'RE DOING

3

OUTCOME 3: RESPONDING TO CLIMATE CHANGE

WE WILL PLAY OUR PART IN MAKING OUR WORLD MORE SUSTAINABLE FOR FUTURE GENERATIONS

24,000

NUMBER OF SOLAR PANELS ACROSS OUR SITES

35 GWH

PRODUCED FROM OUR SLUDGE PROCESSING FACILITIES

20%

OF OUR ENERGY GENERATED FROM OUR OWN RENEWABLE SOURCES

Dramatic weather events continue to cause problems for our communities, and as a country with a large coastline and higher levels of deprivation than the average for the UK, our communities are more vulnerable than most to its effects.

At Welsh Water we are as determined as ever to help in the global effort to reduce the negative impacts on our planet's climate by reducing our own carbon emissions, but also to protect our customers and network from the effects of extreme weather events.

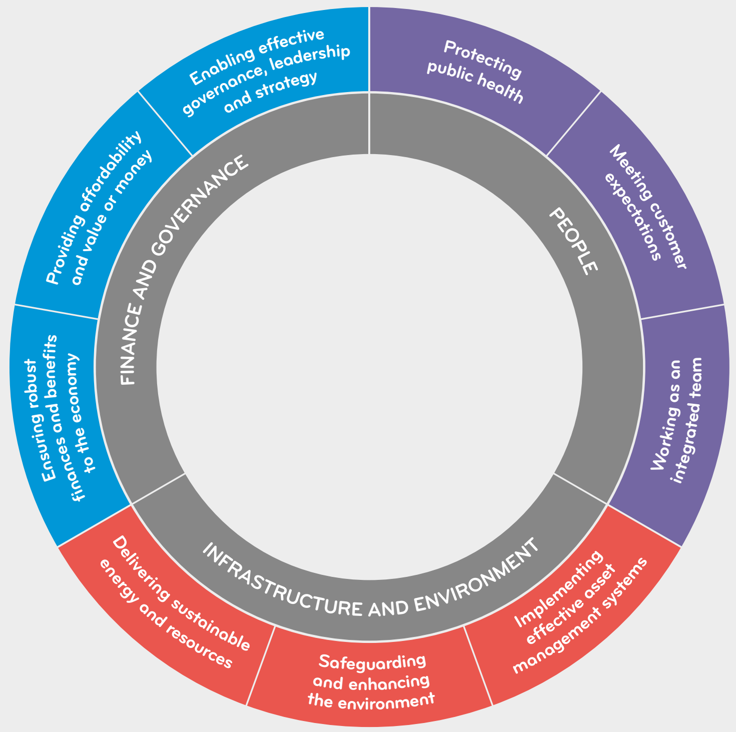
WE ARE DETERMINED TO HELP IN THE GLOBAL EFFORT TO REDUCE THE NEGATIVE IMPACTS ON OUR PLANET'S CLIMATE

Responding to climate change
Our progress in responding to the effects of climate change has been marked and very encouraging in the past year.

One of the key measures for this is the amount of surface water that we are preventing from entering our sewer network – the main aim of our innovative RainScape project in Llanelli and our Greener Grangetown project in Cardiff, both of which use natural methods to slow down, divert and retain rainwater before it enters our sewers. With more than 36,000km of sewers across our operating area – often built in the Victorian era – easing the stress on our network will become ever more important as the effects of climate change are felt.

While these areas remain our primary pilot projects for surface water removal, this principle is being embedded into planning for a range of other projects. As a result, in 2017-18 we have seen strong progress in this area – with the volume of rainfall runoff draining from an area equivalent to 15,097 household roofs removed from the system, compared to 13,661 in 2016-17. We will look to build on this advance in the coming years to further protect our communities from the effects of surface water flooding.

THE WELSH WATER RESILIENCE WHEEL



CASE STUDY

The Welsh Water "Resilience Wheel" is the guiding approach of our long-term vision, Welsh Water 2050. It brings together all areas of our business, including assets, people, systems, finance, governance and outside perspectives. It also enables comparisons to resilience reviews of 100 cities and institutions worldwide – and we will regularly review our progress against it to ensure we're meeting our 2050 objectives.

Carbon footprint
Our commitment to reducing our carbon footprint in recent years has been steadfast – with 20% of our energy now being generated from our own renewable sources. This has included the operation of our first two wind turbines, as well as hydro and solar schemes at works across our area. The acquisition of a food recycling facility near the Cardiff Wastewater Treatment Works in December 2017 means that 53% of the energy used by that works will be generated by the site itself through sustainable, renewable generation.

As a result, a total of 98GWh of renewable energy was generated on our sites in 2017-18, compared to 87GWh in the previous year.

WE WILL REGULARLY REVIEW OUR PROGRESS TO ENSURE WE'RE MEETING OUR 2050 OBJECTIVES

3	RESPONDING TO CLIMATE CHANGE	2016-17	2017-18	17-18 VS 16-17
C1	RESPONDING TO CLIMATE CHANGE	13,661	15,097	✓
C2	CARBON FOOTPRINT	86.5	97.89	✓

OUR WORK — HOW WE'RE DOING

4

OUTCOME 4: CUSTOMER SERVICE

OUR CUSTOMERS SHOULD EXPECT TO RECEIVE THE HIGHEST QUALITY SERVICE FROM US, EVERY TIME.

1.5 MILLION

NUMBER OF HOUSEHOLDS WE SERVE

90%

BUSINESS CUSTOMER SATISFACTION

98%

OF PLANNING APPLICATIONS FOR PROPOSED NEW DEVELOPMENTS SUPPORTED

Our Customer-led Success approach places the needs of our customers at the centre of everything we do.

We take a lot of pride in shaping our services around the needs of our customers – and delivering the best service possible is our top priority.

Customer Satisfaction

The Service Incentive Mechanism (SIM), is research conducted by our economic regulator Ofwat, designed to encourage water companies across Wales and England to improve their customer service, by comparing companies' performance – interviewing customers where something has gone wrong, as well as other customers who have contacted us for any other reason.

For the qualitative element of Ofwat's SIM measurement, our performance outturn at 5th place among the 10 Water and Sewerage Companies for 2017-18 (2016-17: 5th) with a score of 4.47 (compared to an average of 4.40 for all WASCs) was disappointing. Customer service suffered as a result of outages to a key software platform during one of the survey periods. We will continue to target being the best-performing company for customer service. Our focus on customer service was also reflected in the Moneywise Home Finance Award for Best Water Company in the UK, awarded in September 2017, which was given to Welsh Water because: "readers say the firm offers value for money, good customer service and sends clear and concise bills".

At-Risk Customer Service

We invest a great deal in the resilience of our networks to protect our customers from service failures. Customers who have seen their service repeatedly fall short, are deemed "at-risk" of further failures. We are disappointed that the number of customers registered as at-risk of failures like sewer flooding, odours, interruptions to services, and discolouration of water supply has risen to 613 in 2017-18 compared to the previous year (575). This was mainly due to new properties being added to the register as "at risk" despite our efforts to resolve the issues experienced by customers who were already on the list. We remain committed to addressing the underlying reasons to reduce the overall number of at-risk customers.

Flooding

Internal flooding of customer properties with sewage is the worst service failure for our customers – and we've made concerted efforts to reduce how often our network causes this and improve our support for customers when it does. As a result, we are encouraged to have reduced the number of internal floods from 242 last year, to 221 this year, despite volatile weather and periods of heavy rainfall – and we are determined to build on this progress in 2018/19.

Business and Non-Household Customer Satisfaction

The level of business customer and other non-household customer satisfaction has remained stable in the last year, though slightly below the 2017 level. Business customer satisfaction dropped to 87.6% (compared to 90.82% last year), while non-household customer satisfaction was ranked at 87% (2016-17: 89%). We are looking to improve the level of satisfaction in coming years, with a range of value-added services for customers – particularly looking at water-saving services such as audits and telemetry, electronic billing, consolidated billing for larger businesses with multiple sites, and dedicated account management.

Rhondda Fach Resilience Project

The Rhondda Fach project involves customers in day-to-day decisions on how we should provide services to them, in a way we haven't done before – in order to work with customers on solutions to challenges with our assets and in the community. The project is working alongside a £23 million investment in our drinking water network to make sure the work we're doing benefits customers in the local area.

What we want to achieve

We are ambitious to improve our services to customers further, and our key goals for 2018 include:

- Continued support, through social tariffs, for customers who struggle to pay their water bills
- A total of 50 water-efficiency home audits
- Development of our Priority Services Register to ensure we provide services appropriately for customers in vulnerable circumstances
- Creation of tailored education programmes to increase engagement in and awareness of, issues such as how the water and wastewater cycles work, how to stay safe around our sites, and how to protect the environment around us
- Alignment of investment plans to cause minimum disruption in areas where we're doing work

Developer Services

We have continued to provide a high standard of service to our Developer customers this year, supporting housing, commercial and industrial projects across our supply area. The Developer Services team attained 2nd place for water and 4th place for sewerage services in the water sector's Levels of Service measure 2017-18 for services to Developer customers, and has achieved the most consistent good performance in the industry since the scheme was launched in 2015. We are now also a statutory consultee in the planning process and we have supported 98% of all housing units included within planning applications.

Cambrian Utilities

April 2017 marked the official opening of the retail market in Wales and England, with customers in our supply area using more than 50 megalitres of water a year at a single site eligible to switch retailer, but only for clean water services.

Glas Cymru established Cambrian Utilities Ltd in 2016 as a separate subsidiary to act as a retailer for customers who wish to switch their sites in England and Wales to a single retailer. This subsidiary is currently inactive as we wait to see how the competitive market for retail business services develops.

Earning the trust of customers

Customer trust is key to us – which is why our company-wide vision is to "earn the trust of our customers, every day". Each year we conduct a survey of customers to gauge the level of trust they hold in us.

This year, the level of trust remained broadly stable at 84% (2016-17: 85%). This is despite a challenging year for operational incidents – particularly high-profile bursts in Aberdare and Cardiff around Christmas and Boxing Day, and the very demanding service interruptions across our area following the extreme cold weather in February and March 2018 during "Storm Emma".

Storm Emma generated an unprecedented level of customer contact during the extreme freeze and subsequent thaw – with five and a half times the normal daily average number of calls, nearly 10 times the usual number of social media contacts, nearly four times the number of web chats to our advisers, and nearly six times the average number of hits to our website. You can find details of the scale of this response on pages 20-21. This placed a great deal of pressure on our resources and ability to respond to customers quickly, and we are reviewing how we can further improve future resilience and capacity to deal with similar incidents.

In brief

In August 2017, our Customer Strategy Team was recognised for the customer feedback mobile application developed to make it easier for customers to provide us with valuable feedback on our services. The new app can be used after a visit to a customer is completed. It recorded customer satisfaction levels of more than 90% and was awarded the Customer Satisfaction Initiative of the Year award in the Water Industry Achievement Awards.

4	CUSTOMER SERVICE	2016-17	2017-18	17-18 VS 16-17
D1	SIM	83	85	✓
D2	AT RISK CUSTOMER SERVICE	575	613	✗
D3	PROPERTIES FLOODED IN THE YEAR	242	221	✓
D4a	BUSINESS CUSTOMER SATISFACTION (%)	90.82	88	✗
D4b	NON HOUSEHOLD CUSTOMER SATISFACTION (%)	89	87	✗
D5	EARNING THE TRUST OF CUSTOMERS (%)	85	84	✗

OUR WORK — HOW WE'RE DOING

5

OUTCOME 5: AFFORDABLE BILLS

WE WILL MAKE SURE OUR BILLS ARE FAIR AND AFFORDABLE FOR ALL OF OUR CUSTOMERS — AND WILL OFFER SUPPORT FOR THOSE WHO ARE STRUGGLING TO PAY.

105,000

LOW-INCOME HOUSEHOLDS SUPPORTED BY SOCIAL TARIFFS

£200

CAP ON ANNUAL BILLS FOR HELPU CUSTOMERS

£9.2M

RECOVERED IN DEBT COLLECTION ACTIVITIES FROM CUSTOMERS WHO CAN AFFORD TO PAY, BUT DON'T

We have a responsibility to balance investment to improve our services, with keeping bills to an affordable level to ensure that they are fair for customers. We also focus on supporting those in genuine financial need while pursuing those that can pay their water bill, but choose not to do so.

Affordable Bills
In our last overarching review of the charges to customers, we pledged that by 2020 we would have achieved a decade of average annual household bill rises that were at, or below, the rate of Retail Prices Index (RPI) inflation. This would ensure that even when times are tough, customers know that their water bills are affordable and as low as possible.

We are delighted that we have achieved nine consecutive years of below-RPI inflation average household bill rises, with our most-recent announcement in February 2018 confirming a 1.8% rise to an average combined bill of £439 (2016-17: 0.3%). This does represent a rise of £8 on the previous year, but was among the lowest proportional increases in the water industry across England and Wales.

WE HAVE A RESPONSIBILITY TO KEEP BILLS AT AN AFFORDABLE LEVEL FOR CUSTOMERS

Help for Disadvantaged Customers
Our operating area includes communities with some of the highest levels of deprivation in the UK — so when times are tough, our customers feel it more than most.

That's why we've placed such a big emphasis on supporting those customers who genuinely need support in paying their water bills. We had a target of supporting 100,000 or more of these customers by 2020, and we're delighted to report we have now met that threshold two years early — with more than 105,000 enrolled in our range of social tariffs, with 50,000+ now supported by our flagship HelpU tariff, which caps bills of eligible households at under £200 a year. This represents levels of support for low-earning households that is not matched by any other water company in England and Wales.

SOCIAL TARIFFS SUPPORT

CASE STUDY

We work with a range of organisations to identify customers who could benefit from our social tariffs and other support — as part of our commitment to help those who genuinely struggle to pay.

Phyllis Collins, from Port Talbot, was helped to sign up to our flagship tariff, HelpU, by Katrina Bradley from Warm Wales, which works with public and private partners to help provide homes with affordable warmth and to alleviate fuel poverty.

"Katrina from Warm Wales signed me up to the scheme and helped me fill in the forms. I was paying £45 a month but now paying £17 per month which is a great saving for me. I am very grateful for this" — HelpU customer Phyllis Collins, aged 85

WE AIM TO SUPPORT 100,000 CUSTOMERS WHO GENUINELY NEED SUPPORT IN PAYING THEIR WATER BILLS

We are also continuing to raise awareness of the availability of our social tariffs, including:

- Working with around 187 support organisations like StepChange, Citizens Advice, and Cardiff Foodbank to promote the tariffs to their service users
- Helping to train advisers from those organisations
- Promoting alternative support like Watersure Wales — which limits bills if you have a water meter and receive at least one of the qualifying benefits/tax credits — and the Customer Assistance Fund for those in severe financial hardship
- Making it easier for customers to move to a water meter which can save them money

5	AFFORDABLE BILLS	2016-17	2017-18	17-18 VS 16-17
E1	AFFORDABLE BILLS (% BELOW INFLATION)	-1	-2	✓
E2A	HELP FOR DISADVANTAGED CUSTOMERS	71,167	105,864	✓

OUR WORK — HOW WE'RE DOING

6

OUTCOME 6: LOOKING AFTER OUR ASSETS

WE WILL INVEST IN OUR ASSETS TO SERVE FUTURE GENERATIONS

£431 MILLION

CAPITAL INVESTMENTS IN 2017-18

172.9

MEGALITRES OF WATER LOST FROM THE NETWORK IN LEAKAGE LAST YEAR

£23 BILLION

TOTAL ESTIMATED VALUE OF ALL OUR ASSETS

With more than 27,500km of water mains, and over 36,000km of sewers, and hundreds of water and wastewater treatment works, our network is extensive — and includes challenging mountainous terrain, sparsely populated rural communities and urban centres.

The network requires a huge amount of investment to maintain. If we replaced all of our infrastructure at once, it would cost around £23 billion. As a result, we have been investing £213 million in our water assets, and £197 million in our wastewater assets over the past year. Our capital investment totals more than £1 million a day, and our capital investment for 2017-18 is a record high at more than £430 million (2016-17: £366 million).

Maintaining our assets for future generations is a critical part of our responsibility to customers — and one we take seriously.

Asset serviceability
This is assessed by a number of key measures for Ofwat to monitor how we are investing in our assets. Companies are rated either "improving", "stable", "marginal", or "deteriorating". For 2017-18, we have been rated as "stable" across all measures.

Leakage
Reducing leakage from our network is a key target for our Water Services teams, and one where Ofwat has set challenging levels for us to meet. We have responded to this by investing in new, emerging technology to detect and repair leaks and bursts faster than ever before. For instance, we have begun using drones to survey suspected leak areas to find leaks more quickly, and we use state of the art flow monitoring and alert systems to detect possible leaks when they appear.

This year was challenging in terms of operational incidents on our network, and severe weather. Despite this challenging year, we have reduced the amount of water lost from our network to 172.8 megalitres per day — meeting our target (175.43 2016-17).

Extreme weather from "Storm Emma" in late February and early March placed our assets under significant additional stress. During the initial freeze, there were very challenging road transport conditions which made access and maintaining mains power to our treatment works and pumping stations more difficult. During the thaw, we saw a peak in demand, compared to usual levels — with a 20% increase in demand equal to a sustained period of maximum output during the summer — and all 63 water treatment works working at maximum capacity throughout the period. We also saw more than 240 reports of leaks and bursts a day on our water network after the thaw, compared to a normal average of around 75.

DOLBENMAEN WATER TREATMENT WORKS OFFICIAL OPENING

CASE STUDY

In June 2017, Lesley Griffiths A.M., Cabinet Secretary for Energy, Planning and Rural Affairs (pictured here with Lord Dafydd Elis-Thomas A.M., Minister for Culture, Tourism and Sport, and Chris Jones, Chief Executive) officially opened the Dolbenmaen Water Treatment Works in Gwynedd after a £28 million upgrade programme to ensure customers in the Dolbenmaen and surrounding areas continued to receive a top quality drinking water supply. The works supply 20,000 people in the area, and formed part of our record £2 billion of capital commitments in the five years to 2020.

Asset Resilience (Water)
The long-term resilience of our assets is measured by Ofwat against a set of criteria which shows how they are performing and providing service to our customers. As a company, we invest around £213 million in our Water Services assets to ensure long-term resilience and service performance — particularly in our water treatment works and other assets. This is a particularly important part of our Welsh Water 2050 long-term vision which aims to strengthen the resilience of our assets to improve services to customers in future. As such, we are encouraged that our water assets resilience score has remained stable this year at 90.4 out of 100. This is primarily due to the overall performance of our water treatment works.

Asset Resilience (Wastewater)
With 36,000km of sewers across our operating area — enough to go from Wales to New South Wales and back — and more than 835 wastewater treatment works, our wastewater services network is vast and of huge strategic importance. Ofwat measure the performance and resilience of a snapshot of this network against a set of criteria to monitor whether they are delivering reliable services for customers. We are pleased to report we have improved the score to 77.5 out of 100, from 73.9 the previous year. The improvement is partly down to good work done by our Energy Team to improve the power resilience and the plans in place for security or emergency events for our wastewater treatment works and sewage pumping stations.

6	LOOKING AFTER OUR ASSETS	2016-17	2017-18	17-18 VS 16-17
F1	ASSET SERVICEABILITY	STABLE (X4)	STABLE (X4)	✓
F2	F2 LEAKAGE (ML PER DAY)	175.4	172.9	✓
F3	F3 ASSET RESILIENCE (WATER)	89.5	90.4	✓
F3	F3 ASSET RESILIENCE (WASTE WATER)	73.6	77.5	✓

OUR WORK – HOW WE'RE DOING

7

OUTCOME 7: DEVELOPING AND PROTECTING OUR PEOPLE

WE WILL PRESERVE AND DEVELOP THE BEST TALENT FOR THE FUTURE – IN A CULTURE THAT KEEPS OUR PEOPLE SAFE, HEALTHY AND HAPPY.

3,435
EMPLOYEES (AS AT 31 MARCH 2018)

5.8%
OUR MEAN GENDER PAY GAP

36
NEW GRADUATES AND APPRENTICES JOINED WELSH WATER IN 2017-18

80%
EMPLOYEE ENGAGEMENT SCORE

Health and Safety
Our people are our greatest assets – and our greatest ambassadors. So we prize the health and safety of our colleagues above all else and make sure that, whatever they do, they go home safely at the end of the day.

As a result, we have focused on building a culture where health and safety is paramount for every job we do. Our operational teams regularly hold "safety days" throughout the year to review best practice and to improve the procedures in each team. We also communicate with colleagues on how to remain safe in the winter months when conditions are more hazardous to work in, operating a "Safety Takes Every Person (STEP)" and "Take 5" approach (take 5 minutes) to assessing the safety of each job.

This year, we are happy that we have achieved our second-best ever performance in terms of RIDDOR injuries (Reporting of Injuries, Diseases and Dangerous Occurrences) – with 14 such incidents during the year. It is disappointing that this is two more than our performance last year (2017:12). We remain focused on preventing these most serious injuries over the coming year.

In brief
In July, Welsh Water and our Capital Delivery Alliance were both awarded the Royal Society for the Prevention of Accidents (RoSPA) Gold Award in recognition of our Health and Safety performance and Journey to Zero improvements. The awards consider entrants' overarching occupational health and safety management systems, alongside their last 5 years' performance.

Competence in role
We are also committed to helping all of our people grow and thrive in their careers at Welsh Water. This is particularly important as we have an ageing workforce in some roles and areas, and our Welsh Water 2050 vision identifies future-proofing our workforce to meet the challenges of the next 30-40 years, particularly the skills gap identified in the coming years in Wales across key STEM-related roles, as a key plank of our long-term strategy.

We therefore carry out regular reviews across the business to see whether the teams have the right skills to meet the challenges they will face. Our current score has gone down to 82% (2017: 87%), which may be in part as a result of the time taken to bring new starters up to a level of competency for their roles in the business and a delay in recruiting a new trainer.

APPRENTICE TRACEY MCGAULEY – CARMARTHEN

CASE STUDY

"I came across Welsh Water's Apprenticeship scheme and it immediately resonated with me, as I am someone who loves the outdoors and enjoys a good challenge. However, with no direct experience or knowledge I believed that I would not be a suitable candidate for the role, but as I was excited by the possibilities I continued to read and research both the company and job role. The more I read, the more I identified with the company and couldn't believe their not-for-profit business model – along with how strong their ethics and concerns for the environment were. They were so in line with my own way of thinking, I felt I really had to work for this company and had never wanted a job more."

Inclusivity
As a business, we have worked hard in recent years to attract more women to work at Welsh Water. Utility companies have traditionally been male-dominated, and achieving a better gender balance remains particularly challenging in operational or STEM-focused roles, where women are less well-represented.

Since 2014-15, we have raised the total proportion of women working here from 27% to 29%, and a total of 40% of our new hires in 2017-18 were women. We have also worked to tailor our annual recruitment of apprentices and graduates to attract more women to apply – which has seen the proportion of applications from women rise to 14% this year from 8% in 2014.

Women working at Welsh Water are supported by their peers to thrive and develop in their roles – with managers mentoring less experienced colleagues in their roles, and visiting local schools to talk about their careers in the water industry – helping inspire the next generation to enter our industry.

Welsh Water was recognised by the Welsh charity Chwarae Teg, which works to develop opportunities for women in the workplace, as Employer of the Year in 2017.

Gender Pay Gap Report
We are committed to making Welsh Water an inclusive place to work for everyone – and are working to ensure women have every opportunity to thrive in their careers with us.

The Gender Pay Gap report shows the overall median and mean gender pay and bonus gap regardless of role or seniority – and at Welsh Water the median gap is 7.5% (National average: 18.4%) and the mean gap is 5.8% (National average: 17.4%). It is important to note that this is different to the principle of equal pay – all men and women at Welsh Water receive equal pay for performing equal work. While we are pleased to be significantly below the national average Gender Pay Gap, we are fully committed to reducing this further until there is no Gender Pay Gap.

Employee Engagement
We know that to make Welsh Water a great, inclusive place to work that the culture needs to be led by our colleagues who already work here. As such, we are encouraged that in the last survey in November 2017, our employee engagement score rose to a record high of 80% (2016: 77%) and our response rate was also at a record high of 83% (2016: 81%). This progress was recognised in our being shortlisted for the Best Employee Engagement Initiative at the Chartered Institute of Personnel and Development (CIPD) Awards.

7	DEVELOPING AND PROTECTING OUR PEOPLE	2016-17	2017-18	17-18 VS 16-17
G1	RIDDOR INCIDENTS	12	14	✕
G2	COMPETENCE IN ROLE	87%	82%	✕

OUR WORK – HOW WE'RE DOING

8

OUTCOME 8: EFFICIENT BUSINESS

WE WILL RUN AN EFFICIENT BUSINESS WITH A STRONG FINANCIAL BASIS TO BENEFIT OUR CUSTOMERS.

£300M

BOND ISSUE – JANUARY 2018

A2/A

STRONGEST CREDIT RATINGS OF ANY UK UTILITY WITH MOODY'S AND STANDARD & POOR'S

£34M

RETURN OF VALUE INVESTMENTS ANNOUNCED IN JUNE 2017

We continue to invest to preserve and improve the essential services we provide for the future. In 2017-18, this amounted to more than £430 million in capital investment – our largest ever annual investment in our assets and infrastructure and in line with our £1.95bn (£250m extra Capital Programme) investment agreement with our regulator, Ofwat, for the 2015-2020 period.

This year has delivered a financial performance which is in line with our expectations – and balances our priority to invest in our network with keeping bills affordable for customers.

Continuous Improvement in Efficiency

We have worked with our Capital Alliance Partners during the ramp up in capital projects investments, to ensure that the increased investment has been carried out as efficiently as possible. We have shared efficiency gains with our Partners to ensure commitment from all parties to drive efficiencies and savings.

We have also continued to implement operational efficiencies across the business and have identified further costs reductions in our operational and support services teams as we prepare for the next regulatory investment period, 2020-2025.

WE HAVE INVESTED MORE THAN £430 MILLION

Strong Credit Rating

Since 2001 when Glas Cymru acquired Welsh Water, we have reduced our gearing from 93% to 57%, consistent with the Board's policy of maintaining gearing at or just below 60% to best balance our investments, our access to low-cost borrowing and our financial resilience.

Our credit rating from the leading rating agencies – particularly Moody's (A2) and Standard & Poor's (A) – means we are the highest-rated utility company in the UK, ensuring we are able to borrow money at low interest rates and invest with maximum value for our customers.

FOOD WASTE-TO-ENERGY PLANT, CARDIFF

Credit: Encon Construction

CASE STUDY

As part of Glas Cymru's strategy of investing in commercial projects to reduce costs or generate profit to reinvest for our customers, our new subsidiary, Welsh Water Infrastructure, completed the acquisition of the former Kelda food recycling and anaerobic digestion plant in Tremorfa, Cardiff, in December 2017. The site contributes to recycling levels for Cardiff and the Vale of Glamorgan, and anaerobic digestion of the food waste collected by Cardiff and Vale of Glamorgan Councils will generate electricity which, when combined with the existing generation on the treatment works, will meet around half of the total energy requirements of the site, saving significant operational costs. The combined effect of our generation from sludge and from food waste at Cardiff saved the business £2.3m in avoided electricity costs in 2017-18 (and these costs savings should continue to rise as production increases).

We successfully raised £300 million in a sterling bond issue in January 2018 to help us continue to invest in our business to benefit customers – through service improvements and in tackling long-term challenges facing us, such as climate change, protecting water resources, and the challenges of serving an ageing and growing population. Our strong credit rating ensures we can obtain funds for investment at sector-leading interest rates, while keeping customer bills as low as possible.

In brief

One of our responsibilities is to ensure we balance support for those who need help paying their bills, with pursuing those who genuinely can pay, but choose not to. Our Litigation Team are key to this – and we saw recognition for their work when Leon Hughes was named Support Manager of the Year at the Welsh Contact Centre Awards. During 2017-18, the team handled over 20,000 litigation accounts and helped recover more than £16 million in revenue.

Leon Hughes

8	EFFICIENT BUSINESS	2016-17	2017-18	17-18 VS 16-17
H1	FINANCING EFFICIENCY (CREDIT RATING)	A/A2/A	A/A2/A	✓

GLAS CYMRU HOLDINGS CYFYNGEDIG | ANNUAL REPORT & ACCOUNTS

OUR PEOPLE

OUR DIRECTORS

FULL BIOGRAPHIES PAGES 54-56

1
JOANNE KENRICK
NON-EXECUTIVE DIRECTOR

2
MENNA RICHARDS
SENIOR INDEPENDENT DIRECTOR

3
PROF. TOM CRICK
NON-EXECUTIVE DIRECTOR

4
ALASTAIR LYONS CBE
CHAIRMAN

5
CHRIS JONES
CHIEF EXECUTIVE

6
ANNA WALKER CBE
NON-EXECUTIVE DIRECTOR

7
JOHN WARREN
NON-EXECUTIVE DIRECTOR

8
GRAHAM EDWARDS
NON-EXECUTIVE DIRECTOR

9
PETER BRIDGEWATER
FINANCE AND COMMERCIAL DIRECTOR

10
PETER PERRY
MANAGING DIRECTOR

OUR WORK

OUR REGULATORS AND KEY STAKEHOLDERS

The water and wastewater industry in England and Wales is regulated in three key areas, namely: financial and economic, environmental, and water quality. These regulators aim to protect consumers and the environment and they monitor the performance of each company carefully.

We always try to maintain good relationships with these regulatory bodies and key stakeholders to help shape balanced investment programmes which address the needs of all of our customers and stakeholders.

Copies of the reports published by these regulators on Welsh Water's performance can be found on our website **dwrcymru.com** or on the website of the relevant regulator.

Ofwat
Welsh Water is regulated, on economic matters, by the Water Services Regulation Authority (Ofwat), which regulates all water and wastewater providers across Wales and England. Limits over water and wastewater charges are set on a five-yearly cycle by Ofwat, informed by the policy context set by the Welsh Government and other regulators.

ofwat.gov.uk

Health and Safety Executive
The national independent regulator for work-related health, safety and illness.

hse.gov.uk

Welsh Government
Sets the framework for public policy matters for Wales, including policy and legislation on water, sewerage and environmental matters.

gov.wales

Department for Environment, Food and Rural Affairs
The department responsible for UK Government input into the water and sewerage policy protocol with the Welsh Government.

defra.org.uk

Drinking Water Inspectorate
Drinking water quality is regulated and monitored by the Drinking Water Inspectorate.

dwi.gov.uk

The Consumer Council for Water
An independent body established to represent the interests of customers relating to price, service and value for money. It also investigates customer complaints about water quality.

ccwater.org.uk

The Water Redress Scheme (WATRS)
The independent adjudicator for disputes between customers and the water and wastewater companies of England and Wales.

watrs.org

The Information Commissioner's Office
The UK's independent authority set up to uphold information rights in the public interest, promoting openness by public bodies and data privacy for individuals.

ico.org.uk

Natural Resources Wales / Environment Agency
Our environmental performance, especially the way we abstract water from rivers and reservoirs and then discharge wastewater after it has been cleaned, is regulated by Natural Resources Wales and the Environment Agency. They oversee our management of designated sites for nature conservation and how we meet our obligations to conserve and improve biodiversity and our natural resources.

naturalresources.wales

gov.uk/government/organisations/environment-agency

Welsh Language Commissioner
The principal aim of the Welsh Language Commissioner is to promote and facilitate the use of the Welsh language. We submit an annual compliance report to the Commissioner's office detailing how we have complied with the provisions of our statutory Welsh Language Scheme which outlines how we provide bilingual services to our customers.

comisiynyddygymraeg.cymru/english

OUR APPROACH TO RISK MANAGEMENT

All colleagues play a part in ensuring effective risk management, which is essential to underpinning decision-making at all levels of the organisation, and ultimately to ensure the long term success of the business.

OUR PROCESS

- Our systems of internal control are designed to identify, evaluate and manage risks affecting the business and these systems or internal control are regularly considered and monitored by the Audit Committee.
- Having risks identified and changes in the assessment of risks highlighted means that the Board is able to undertake its own informed assessment of the principal risks facing the company and to work with the Executive to agree the Group's tolerance of risk in these key areas on a regular basis.
- This assessment is used on a day-to-day basis to inform decision making including decisions concerning our investment programme. Every strategic update paper presented to the Board and its Committees includes a risk report and where risks identify the need for further mitigation, will include action plans with agreed timescales to enable progress to be tracked.

OUR APPROACH TO RISK MANAGEMENT

- Individual teams within the business take responsibility for managing risks within their areas of responsibility.
- Each business unit feeds into a "bottom up" risk management system, escalating risks through our governance structure of committees and team meetings. Risks recorded through that process are discussed during a more "top down" discussion of risk every month at a meeting of the Executive team.
- The Executive team's update on strategic risks affecting the business is reviewed at every Board Meeting and the Board carries out an in-depth review of strategic risks twice every year. The Board assesses both the current and target level of each risk.
- The Audit Committee has accountability for overseeing the risk management processes and procedures and reports to the Board on the adequacy of internal controls.
- This bottom up and top down approach to risk management provides assurance that risks are being effectively managed by the business and identifies those areas where further mitigation steps are needed.

THREE LINES OF DEFENCE

We use the 'Three Lines of Defence' model to mitigate risk of non-compliance with our processes and policies:

1. First line of defence is ownership and management of risk. This is fulfilled by our operational teams and managers.
2. Second line of defence is risk management and risk control. This is fulfilled by our compliance team and internal committees.
3. Third line of defence is independent review and oversight. This is fulfilled by Internal and External Auditors, including our technical adviser on regulatory reporting issues (Jacobs Engineering Group).

KEY RISKS FACED BY THE GROUP

The analysis below focuses on those risks that would threaten the company's future performance, solvency or liquidity. The risks are not ranked in order of significance or severity.

Key risk and severity	Potential impact	Mitigation	Changes over the period	Trend relative to last year
Health and Safety major incident	The health and safety of our employees and the public in the provision of our services and on our sites is our utmost priority. Risks include the potential for an accident or death to a member of the public, on one or our sites or as a result of our actions, or to an employee in discharging their duties. We are responsible for the health & safety of 6,000 colleagues and partners. We take safety very seriously as on average there is one death a year in the sector caused by accidents. During a period of intense capital projects activity we are acutely aware of the potential risks and have increased focus on health, safety and wellbeing, working with our Alliance Partners.	– Clear and regularly reviewed health and safety policies – We follow industry best practice and regularly review our training schedules. – Continued focus on behavioural safety and positive intervention reporting. – Regular communications across the business. – Review of our lone working system and improved compliance with policy. – Reviewing lessons from cases elsewhere in the sector.	No movement in the period.	◀ ▶
Major public health incident	A sustained problem with drinking water quality could have a significant impact on our customers' health and wellbeing. It would require a widespread boil water notice and could lead to a high profile prosecution. Such an incident could be caused by asset failure, an unanticipated catchment risk, or deliberate sabotage. We aim to do all we can to mitigate the potential for a large scale public health incident. Following a cryptosporidium outbreak we experienced in 2005 we have considerably strengthened both our water treatment assets and water quality management capability. Overall, we are well placed to avoid the potential for a major incident as a result of the improvement in the last 10 years, however, there is an ongoing focus on further enhancement to improve performance and mitigate risk.	– ISO9001 Accredited Operating Procedures & emergency shutdown facilities. – Cryptosporidium Strategy & related academic study. – Water Regulations Inspection Programme. – Daily quality reporting to Managing Director of Water Services, Head of Water Quality & Managing Director of Welsh Water.	No movement in the period.	◀ ▶
Failure to achieve required performance levels and efficiencies during the period 2015-2020	Our vision is to earn the trust of our customers every day. Sustained deterioration in performance could lead to loss of customer confidence, impact reputation with stakeholders and give rise to regulatory action (including ODI performance penalties). Our aim is to deliver the very best levels of service and quality to our customers and to minimise impact on the environment. Performance against customer and level of service measures is very important in terms of our standing with our customers, regulators and other stakeholders.	– Zonal Studies innovative assessment and investment prioritisation strategy – Iron Compliance Strategy – Clean & Waste Water Improvement Strategies for Customer & Quality Performance – AMP 6 Capital Investment Programme	Following a prolonged dry period over the early part of the summer, there was a 20% increase in water put into supply. This led to an upturn in discolouration and respective contacts and complaints. The extreme freeze/thaw conditions at the beginning of March saw the operational teams facing unprecedented numbers of incidents on our clean water network. This impacted both leakage performance and discolouration contacts as a result of increased water in supply disturbing sediment in pipes.	▲

Key risk and severity	Potential impact	Mitigation	Changes over the period	Trend relative to last year
Strategic Asset Failure	Failure of a dam, treatment works or flooding incident with a risk to life. Alternatively, less serious (but still very significant) potential failure of a works with a potential loss of supply for thousands of customers.	– Reservoir Dam Safety Monitoring Programme / Annual Reservoir Safety Report to the Board and portfolio risk assessment. – Critical National Infrastructure & Security Emergency Measures Directive Procedures & Investment (anti-terrorist). – Emergency Planning Procedures, including annual simulation exercise programme. – 24/7 Standby support with competent specialist contractors. – Prioritised capital investment (with focus on increasing resilience) and operational maintenance.	We successfully completed the first stage of our pipework in dams repair and improvement scheme last summer, and work is ongoing over the course of this summer.	◀ ▶
Failure to deliver AMP6 efficiency plan, including Retail	The risk that the company will be unable to achieve its Wholesale and Retail cost reductions over the next two years to meet the reduced revenue allowances and cost budget. The risk is higher in Retail where failure to deliver stretching cost efficiency (specifically reduction in bad debt and efficiencies in customer service) could lead to a loss making retail business.	– AMP6 costs reduction plans are being implemented – bad debt reduction strategy in place and showing progress	– Bad debt is on target to be reduced to £19m by 2020. – Substantially ahead of target for numbers of customers on Social Tariffs and this will also help bad debt. – We are starting a further series of cost reductions in both operational and in support services teams to prepare for AMP7.	▼
Loss of key talent, capability and competence	The recent upturn in the economy and investment in industries where we compete for labour present an emerging risk to our ability to attract and retain employees with the skills and competence we require. We also face the risk that key individuals could be targeted by other water companies.	– Root cause analysis of turnover to ensure strategies address real not perceived problems – Rolling 5 year Resource Plan drive identifying risks and timing of recruitment – Continue with annual apprentice and graduate intake but reinforce the need for successful trainees to be willing to be geographically mobile. – Development and retention plans for key managers and identified 'rising stars'.	During the year we experienced some retention challenges. However, employee turnover levels currently remain at less than 10%. We continue to be proactive and implement preventative strategies to ensure we continue to be able to attract and retain electricians, instrument technicians, engineers, procurement specialists and our data analysis capability.	▲
ICT risk	A major loss of ICT service puts business performance at risk, whilst several business improvement plans are reliant on new ICT systems. Based on past experience we can experience 1 or 2 major system outages a year. These have tended to be resolved within 'hours' and are only very disruptive for a short period. We are alert to the ever changing threats to Cyber Security and are continuing to invest in the enhancement of our defensive measures via ongoing programmes of continuous improvement.	There have been increased threats to the sector as a whole this year and our Information Security team continues to liaise with the National Cyber Security Centre and other authorities regarding new threats. Information Security Steering Group. – Systems & Change Board governs major systems investment programme. – Cyber Essentials Plus achieved early in June 2017. – Ongoing investment in systems and proactive monitoring.	During the year we have undertaken live programme upgrades to SAP which led to some performance issues, however in general our systems and processes remain robust. There has been an increased number of external threats and perceived risks across the sector during 2017-18.	▲

Key: ▲ risk increasing ▼ risk decreasing

Key risk and severity	Potential impact	Mitigation	Changes over the period	Trend relative to last year
Tough regulatory settlement for AMP7	The current regulatory price review process to set investment and prices for 2020-25 is taking place against the backdrop of a complex political environment. Ofwat has set out an early view that cost of capital levels for the next period will be significantly reduced, and its Chair has talked about "putting the sector back in balance" (Ofwat consultation on changes to PR19 Methodology - May 2018). Although many of the governance issues raised by Ofwat do not apply directly to Welsh Water, there is a concern that a broad brush approach to the regulation of the sector might have unforeseen consequences for Welsh Water.	Extensive engagement with customers to ensure there is support for our draft Business Plan; Detailed work to ensure that Ofwat's methodology is correctly understood and that its concerns are addressed in our draft Business Plan	Heightened political criticism of the gains made in the sector; Political uncertainty in the run-up to Brexit.	
Uncertainty following Brexit	Political and financial market volatility in advance of, and following the UK's decision to leave the EU, leading to possible financial pressures. A recession could increase bad debt, and a devaluation of sterling could affect revenues and interest payments, while increasing power costs directly linked to the US$ Brexit may make raising new finance from banks more difficult or more expensive. Environmental obligations: There is unlikely to be any significant change to the stringent regulations deriving from EU Directives e.g. Urban Waste Water Treatment Directive. Welsh Government has signalled that whilst it is committed to the principles underlying most Directives e.g. Water Framework Directive, it may consider changes to regulations that deliver better environmental outcomes.	Roughly 90% of power requirements for the next 3 years are either already fixed or hedged. Our £3.6 billion of debt is fully hedged into fixed interest rates (30%) or RPI indexed-linked rates (70%). We are working closely with Welsh Government in considering environmental regulatory changes that will be necessary following Brexit.	Whilst some progress has been made in the negotiations between the UK Government and the EU, there remains uncertainty over future trading agreements. This may lead to an economic downturn and further sterling devaluation. We maximised our funding with EIB in 2016-17 and this year we have issued a £300m bond which will provide funding for AMP7 investment. We continue to benefit from the highest credit rating in the sector, which reduces our cost of borrowing.	This risk is reported against for the first time in 2017-18, although future funding risk and relationships with investors was reported against as a risk in 2016-17.
Failure to earn the trust and confidence of our customers	Failure to earn and maintain the trust and confidence of our customers leading to failure to achieve our corporate objective, reputational damage, increased customer service costs, damage to regulatory/ government relationships, loss of employee morale. This risk is inextricably linked to many of the other risks identified. We have a strong, positive reputation and high levels of trust with our customers. However, trust is built on customers' perception of good service and value for money and familiarity with the company. Welsh Water continues to perform strongly in terms of assessed customer trust, despite the ongoing political focus on renationalising the sector, ownership models and dividend policies, and the impact of Storm Emma. Our profile campaign raised awareness of non-shareholder status from 31% to 56% and achieved strong increases in perception of trust and value for money. Ensuring compliance with the General Data Protection Regulation from May 2018 will also be essential to maintaining and building the trust of our customers. We are putting together a project plan to ensure compliance of our systems and processes and to bring about culture change to enhance the protections we have in place and to ensure our customer data is secure and treated with respect.	Roll-out of Customer-led Success approach, across the business. – Profile raising and customer behaviour campaigns – Customer Challenge Group – Ambitious AMP6 Customer Engagement and Research Plan – Customer Led Success (including Pain Points) programme to deliver service improvements – Work with Institute of Customer Service – Further action to improve Employee Engagement scores. – Ongoing stakeholder and political engagement programme		

NOTE ON SIGNIFICANT DISPUTES WITH THE POTENTIAL TO IMPACT THE COMPANY

TATA STEEL

During the year the long-standing dispute with Tata Steel in relation to the pricing of industrial water supplies at its sites within our supply area was subject to a confidential final settlement on satisfactory terms and the amount concerned is not material to this Report and Accounts.

INFRACTION PROCEEDINGS IN RELATION TO THE LOUGHOR ESTUARY

In March 2014, the UK Government was informed of an impending infraction case alleging breaches of the Urban Wastewater Treatment Directive around the UK, including areas of the Loughor Estuary, Gowerton and Llanelli catchments. There is an ongoing programme of investment in the area, in particular with regard to sustainable urban drainage systems, which has been welcomed by the European Commission and which will be complete by the end of 2020. Despite this ongoing investment, in May 2017 the Court of Justice of the European Communities issued its judgment in the proceedings against the UK in respect of multiple sites including Llanelli and Gowerton, which found that the UK had failed to comply with the Directive by the required date of September 2014. It is not yet clear whether the programme of investment will be acceptable to the Commission.

CLAIMS UNDER THE ENVIRONMENTAL INFORMATION REGULATIONS 2001 (EIR)

The company was notified in 2017 of potential claims under the EIR relating to charges previously levied for drainage and water searches carried out since 2004, which it is claimed should have been provided free of charge. We have continued to monitor correspondence in relation to these potential claims. To date, very little detail has been provided in relation to the claims and the indicated potential quantum claimed is unclear. We intend to defend the claims, the quantum of which is not expected to be material in the context of the Report and Accounts.

LONG-TERM VIABILITY STATEMENT

Our vision is to earn the trust of our customers every day. Our customers need to know they can rely on the services we provide over the long term. Ensuring the long-term resilience of our business, including financial resilience, is therefore a key area of focus for us.

As we do not have shareholders (who could provide equity in the case of financial distress), maintaining ready access to low-cost debt is a key part of our not-for-shareholder ownership model. The benefits of this low cost finance are then passed on to customers in the form of lower bills.

When the ownership structure under Glas Cymru was established in 2001, a focal element of this financial resilience strategy was to reduce our gearing. Gearing is currently slightly below the Board's target of 60% and this reduction in gearing has created a strong buffer of financial reserves (now standing at £2.4bn).

Although not a listed company, we adhere to the UK Corporate Governance Code as far as possible for a company limited by guarantee.

OUR APPROACH TO CONSIDERING VIABILITY AND RISK

The Board's consideration of the Group's long-term viability is embedded in our business planning process; this includes robust risk management controls, financial forecasting and sensitivity analysis, as well as regular budget reviews. This process is underpinned by a culture of support and challenge that flows from our leadership team to all aspects of our operations. This year we have reconsidered the appropriate period over which viability should be reported: we consider that a period of up to twelve years is the most suitable period over which the Board should assess the prospects of the Group. It is within the period covered by our current business planning process and covers the next two regulatory review periods, to 2030. We have clarity of our current regulatory price controls to 2020, are developing detailed plans for the next regulatory period (AMP7) to 2025, and we are also developing outline plans for the following period (AMP8) to 2030 in the context of our strategic planning document "Welsh Water 2050".

The principal risks facing the Group (and how we mitigate these) are set out on pages 44-46 in relation to our ability to deliver our strategic objectives. Risks are identified and assessed through a continuous cycle of bottom-up reporting and review and top-down feedback and horizon scanning. We accept that embracing and managing risk is a necessary part of doing business, and our risk management process aims to capture a spectrum of risk from inherent to emerging, and across all business areas.

The Board has analysed the efficacy and robustness of its control framework in managing the likely causes and consequences of each risk, and has reviewed the Group's assumptions and contingency plans. The Board has discussed the potential financial and reputational impact of these principal risks against the Group's ability to deliver its 2018 business plan, which is being prepared for submission to Ofwat in respect of the PR19 price control and which principally covers the period April 2018 to the end of the next regulatory review period (AMP7) in March 2025, with financial forecasts stretching to 2035. Although we have developed plans for AMP9 (to 2035) we consider that the degree of uncertainty looking beyond two cumulative regulatory reviews makes such plans unsuitable for our viability and risk review. We have therefore used our plans and forecasts to 2030 for this review.

We have stress-tested our business plan forecasts to 2030 against a variety of financial scenarios which include the estimated impact of each of the principal risks and uncertainties occurring, both individually and together based on the Board's assessment of their likelihood and severity. We have also combined the forecast impact of these with high and low inflation scenarios over the period (5% and 0% respectively). In addition we have used "blanket" cost stresses of a 10% revenue reduction in every year and a 10% total expenditure (totex) overspend each year.

These scenarios have been picked as they provide a severe, plausible and reasonable test of overall flex in the financial plan, based on the principal risks to which the Board has identified that the Group is exposed. While it is highly unlikely that all of the identified scenarios will occur simultaneously, or even that they would all occur once during the period, we have modelled the impact of this to understand the level of resilience implicit in the forecasts. In assessing the financial impact of each scenario, management has taken into account both its own experience and other, publicly available, data.

The estimated impact of each scenario being overlaid on the Group's financial plan does not present any material threat to the Group's viability. High and low inflation scenarios also have a relatively small impact on the Group's viability, as both revenues and a significant proportion of net debt are inflation-linked. Even under a "crisis scenario", in which all principal risks and uncertainties occur in a low-inflation environment, the Directors do not expect to breach the gearing level trigger of 85% covenanted with our debt providers. While this is not considered a realistic scenario for the purpose of forecasting, it gives an indication of the overall level of financial resilience beyond the next regulatory review period.

In the case of all identified reasonably foreseeable scenarios arising, various options would be available to the Group in order to maintain liquidity so as to continue in operation. All funding is already in place to deliver the business plan to March 2020, including allowance for flex to the most extreme combination of adverse scenarios over this period. We are looking into additional funding sources for AMP7 and beyond and, given the success of our last bond issue (in January 2018), do not currently anticipate experiencing significant difficulties. The Group operates in a stable sector with predictable cash flows and a supportive regulator; levels of investor confidence have historically been high and likely changes to the regulatory environment and the Group's own principal risks are unlikely to have a material impact on the company's credit rating during the period under review. The Directors are therefore confident that, in all the identified scenarios, the Group should retain access to relevant markets for refinancing requirements.

The Board has assessed the potential impacts of these risks within the context of its risk appetite and is confident that the controls in place are sufficient to keep the Group's financial performance within appropriate tolerance levels. In making their assessment, the Directors have taken account of the Group's robust forecast and actual gearing of around 60%, its strong level of liquidity and its ability to raise finance. It is also important to recognise that Ofwat, the company's economic regulator, has a statutory duty to secure that efficient water companies can finance the proper carrying out of their functions correctly — although this has no direct bearing on our business planning activities.

COMMERCIAL PROJECTS

The Group's activities outside of the regulated monopoly business are restricted by our Common Terms Agreement with our debt providers to the UK utilities sector with a maximum investment of £100m (in 2016 prices). Such activities are therefore peripheral to the core business and have no material impact on the Group's overall viability or financial resilience, although they aim to generate additional funds that can be applied for the benefit of our customers, or to reduce costs in the operational business.

ASSURANCE PROCESSES

Our internal business planning workstreams separate the preparation of operational cash flow forecasts from the modelling of financing costs, which facilitates a robust two-way cross check on the robustness of the forecasts prior to review by the executive team, Audit Committee and Board. The financial model underpinning the forecasts has been subject to external agreed upon procedures designed to provide assurance over its integrity, with no exceptions identified, and we have also obtained external assurance on the key assumptions and forecast credit metrics in our draft plans for the period 2020 to 2025. This Viability Statement itself comprises part of the Annual Report and Accounts on which our external auditors provide an independent audit opinion.

CONCLUSION

As a result of this assessment, the Directors have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period to March 2030.

GOVERNANCE

GOVERNANCE REPORT

THIS CORPORATE GOVERNANCE REPORT PROVIDES INFORMATION ON THE BOARD AND COMMITTEES OF GLAS CYMRU, HOW WE MEET THE UK CORPORATE GOVERNANCE CODE REQUIREMENTS, DETAILS OF OUR MEMBERSHIP AND OUR APPROACH TO REMUNERATION

CHAIRMAN'S INTRODUCTION

ON BEHALF OF THE BOARD I AM PLEASED TO INTRODUCE THE GLAS CYMRU HOLDINGS CYFYNGEDIG CORPORATE GOVERNANCE REPORT FOR THE FINANCIAL YEAR ENDED 31 MARCH 2018.

Our not-for-shareholder structure means that we are entirely focused on providing the best service that we can to the 3.1 million people that we serve across our supply area. Welsh Water's vision is to Earn the Trust of our Customers Every Day. We understand that ensuring the highest standards of governance is crucial to earning the trust of our customers. Good corporate governance helps to embed culture and strengthens and supports decision making at all levels of the business. The Board is focused on ensuring good governance and follows the UK Corporate Governance Code as far as possible for a Group owned by a company that is limited by guarantee. This report outlines the governance framework we have in place and provides information on our Board and Committees.

This report also explains how we meet the UK Corporate Governance Code requirements, details of our Membership and our approach to remuneration.

Alastair Lyons
Chairman

7 June 2018

OUR CORPORATE STRUCTURE

OUR FINANCIAL STATEMENTS (FROM PAGE 100) COVER DETAILS OF THE FOLLOWING COMPANIES IN OUR GROUP STRUCTURE:

Glas Cymru Holdings Cyfyngedig (Glas Cymru) is a company limited by guarantee which was formed on 15 December 2015. We created this holding company as part of a corporate restructuring, which took effect on 1 March 2016, to allow us to create limited commercial investments in subsidiaries outside the terms of the Common Terms Agreement with investors.

Dŵr Cymru Cyfyngedig is a wholly owned subsidiary of Glas Cymru and is the Group's principal trading company – referred to as Welsh Water throughout this report. Its principal activity is the supply of water and treatment and disposal of wastewater under the Instrument of Appointment made by the Secretary of State for Wales under the Water Act 1989.

Glas Cymru Anghyfyngedig previously the parent company of the group of companies, funded under a Whole Business Securitisation Common Terms Agreement.

Glas Cymru (Securities) Cyfyngedig is the holding company for Dŵr Cymru (Holdings) Limited and its subsidiaries.

Dŵr Cymru (Holdings) Limited is the intermediate holding company of Dŵr Cymru Cyfyngedig and Dŵr Cymru (Financing) Limited.

Dŵr Cymru (Financing) Limited is the 'issuer' company for the Group's bonds, which are listed on the Luxembourg Bourse. Dŵr Cymru (Financing) Limited was established prior to the acquisition of Welsh Water by Glas Cymru in 2001, and is registered in the Cayman Islands and in England and Wales. It is managed, controlled and resident in the UK for tax purposes. The company on-lends the proceeds of any bond issues to Dŵr Cymru Cyfyngedig. We expect to transfer the debt held in this company to a new company registered in England and Wales by end December 2018.

Welsh Water Holdings Limited is the holding company for companies outside of the Common Terms Agreement:

- **Cambrian Utilities Limited** was created to offer retail services to business customers.
- **Welsh Water Infrastructure Limited** pursues commercial projects.
- **Welsh Water Organic Energy Limited** and **Welsh Water Organic Energy (Cardiff) Limited** were purchased in December 2017 and provide anaerobic food digestion and composting services to Cardiff and Vale of Glamorgan Councils.

THE BOARD OF DIRECTORS

CHAIRMAN

ALASTAIR LYONS CBE (64)
IN POST SINCE: MAY 2016
COMMITTEE MEMBERSHIP:
F R Q N CHAIR

Experience
A chartered accountant by training, Alastair has 18 years' experience as a non-executive chairman of both listed and private companies. During an extensive executive career in financial services, he was Chief Executive Officer of both the National Provident Institution and the National & Provincial Building Society, Managing Director of the Insurance Division of Abbey National plc, and Director of Corporate Projects at National Westminster Bank plc.

Current other Non-Executive Roles
He is Chairman of Harworth Group plc and of EUI and AECS, two of the operating subsidiaries of the Admiral Group.

Previous Non-Executive positions
Alastair previously served as Chairman of the Admiral Group, the direct motor insurer, from 2000 to 2017, Chairman of Towergate Insurance, Chairman of Serco, the international services group, and Senior Independent Director at Phoenix, the life assurance consolidator. He has also been a Non-Executive Director of both the Department for Transport and the Department for Work and Pensions. He was awarded the CBE in 2001 for services to social security.

CHIEF EXECUTIVE

CHRIS JONES (54)
IN POST SINCE: SEPT 2013
COMMITTEE MEMBERSHIP:
F N Q

Experience
Chris became Chief Executive in September 2013 having previously been Finance Director of Welsh Water since May 2001 and Glas Cymru since April 2000. He has also previously served as Director of Regulation of Welsh Water and South Wales Electricity plc. Before joining Welsh Water in 1995, he was a Director at National Economic Research Associates and, prior to that, worked for HM Treasury.

Current Non-Executive positions
Deputy Chairman of the Prince's Trust Cymru Advisory Council since 2009.

Previous Non-Executive positions
Non-Executive Director of the Principality Building Society.

Trustee of the Institute of Welsh Affairs.

A Audit
F Finance
N Nominations
R Remuneration
Q Quality and Environment

SENIOR INDEPENDENT DIRECTOR

MENNA RICHARDS (65)
JOINED: NOVEMBER 2010
IN POST SINCE: JULY 2014
COMMITTEE MEMBERSHIP:
N R

Experience
Menna's executive career was in broadcasting as Director BBC Cymru Wales (2000–2011) and previously Managing Director, HTV Wales.

Current other Non-Executive positions
Non-Executive Director of Welsh National Opera. Chair of the ALOUD charity. Vice President of the Royal Welsh College of Music and Drama.

Previous Non-Executive positions
Chair of Governors of the Royal Welsh College of Music and Drama. Board member of the Cardiff Bay Development Corporation, Non-Executive Director, Principality Building Society.

FINANCE AND COMMERCIAL DIRECTOR

PETER BRIDGEWATER (55)
IN POST SINCE: SEPT 2014
COMMITTEE MEMBERSHIP:
F

Experience
Peter joined Welsh Water in September 2014 with 15 years of experience in both Finance and Managing Director roles across the energy and water sectors, in the UK and overseas. Peter has been an Executive Director with E.ON and with Sembcorp Industries in regulated utilities and competitive industries, as well as a pension fund trustee. Prior to joining the energy industry in 1994 Peter was a chartered accountant and management consultant with PwC.

Current Non-Executive positions
Non-Executive Director of Ebico Limited (a not for profit gas and electricity provider).

MANAGING DIRECTOR

PETER PERRY (55)
IN POST SINCE: JULY 2006
COMMITTEE MEMBERSHIP:
Q

Experience
Peter was appointed Managing Director of Dŵr Cymru Welsh Water in October 2017 after four years as Chief Operating Officer. Appointed Operations Director of Welsh Water in July 2006, Peter has a civil engineering background and was formerly the Chief Operating Officer for United Utilities Operational Services (UUOS), having previously been the Operations Director for UUOS with responsibility for the operational contract with Welsh Water and UUOS 's water interests in Scotland and Ireland. Prior to joining UUOS he worked for Welsh Water for over 20 years.

Current Non-Executive positions
He was a Director (representing Wales) at The Water Regulations Advisory Scheme, the national body specifying standards for materials and workmanship used in potable water supply.

NON-EXECUTIVE DIRECTOR

GRAHAM EDWARDS (64)
JOINED: OCTOBER 2013
COMMITTEE MEMBERSHIP:
A Q CHAIR

Experience
Graham is currently Chief Executive Officer of Wales & West Utilities. He has significant senior management experience in the utility sector running electricity distribution and water businesses with South Wales Electricity, Hyder and Thames Water. Prior to working in utilities he held senior positions in various functions across a wide range of manufacturing businesses including Engineering, Production and Human Resources. Graham has an MBA from Cardiff Business School and is a Fellow of the Chartered Institute of Personnel & Development.

Current Non-Executive positions
Board member of University of South Wales.

Previous Non-Executive positions
Previous Chair of CBI Wales and Business in the Community Wales and Non-Executive Director of the Royal College of Music and Drama.

A Audit F Finance N Nominations R Remuneration Q Quality and Environment

JOANNE KENRICK (51)
JOINED: NOVEMBER 2015
COMMITTEE MEMBERSHIP:
A Q

Experience
Joanne was the Marketing Director for Homebase until the end of 2015. Prior to that, Joanne was CEO of Start, setting up and running HRH the Prince of Wales' public facing initiative for a more sustainable future. Former roles include Marketing and Customer Proposition Director for B&Q, Marketing Director for the National Lottery, and Group Sales and Marketing Director at Wilson Connolly. She has also worked for Woolworths, Asda, Pepsico and Masterfoods. Joanne has a degree in Law from Nottingham University, and whilst at college she was one of the first women ever trained to fly by the RAF.

Current other Non-Executive Positions
She is also a Non Executive Director at Coventry Building Society, BACS Payment Services Limited, Safestore, the UK's largest self-storage business and Chairman of trustees of the children's charity Make Some Noise.

Previous Non-Executive positions
Joanne was a Non-Executive Director at Principality Building Society for 7 years.

PROF. TOM CRICK (37)
JOINED: OCTOBER 2017
COMMITTEE MEMBERSHIP:
Q

Experience
Tom is Professor of Computer Science & Public Policy at Swansea University; his academic interests sit at the research/policy interface, solving data-driven and computationally-intensive problems across a range of domains. He has provided expert advice to the Welsh Government on science/innovation policy, data infrastructure, public service innovation and STEM education, and is Chair of the National Network for Excellence in Science & Technology. Tom was appointed MBE in the 2017 Birthday Honours for services to computer science and the promotion of computer science education.

Current other Non-Executive Positions
Independent Member/NED of Abertawe Bro Morgannwg University Health Board and Vice-President/Trustee of BCS, The Chartered Institute for IT.

ANNA WALKER CBE (67)
JOINED: MARCH 2011
COMMITTEE MEMBERSHIP:
A R CHAIR

Experience
Anna has a wealth of experience in regulation, customer service, policy making and working with governments. Anna undertook an independent review for government in 2008 into household water charging. Former roles include Chief Executive of the Healthcare Commission (2004-2009), Director General, Land Use and Rural Affairs at DEFRA, Director General, Energy Group at DTI, and Deputy Director General at Oftel, the telecoms sector regulator.

Current other Non-Executive positions
Anna, who was awarded a CB in 2003 for public service, is Deputy Chair of the Council of Which?, a member of the Competition Appeal Tribunal and a Non-Executive Director for South London and the Maudsley NHS Foundation Trust.

Previous Non-Executive positions
Anna was Chair of the Office of Rail Regulation from 2009-2015 and a former Vice Chair of Consumer Focus, the statutory consumer champion body.

JOHN WARREN (64)
JOINED: MAY 2012
COMMITTEE MEMBERSHIP:
R A CHAIR F CHAIR

Experience
John is a qualified accountant with more than 25 years' experience in senior finance roles and has extensive experience in chairing Audit Committees of UK listed companies. Until his retirement in 2005, he was Group Finance Director for WH Smith PLC and, before that, United Biscuits (Holdings) Plc.

Current other Non-Executive positions
He is currently a Non—Executive Director and Chairman of the Audit Committee for Greencore Group plc, 4imprint Group plc and Bloomsbury Publishing Plc.

Previous Non-Executive positions
John has been Non-Executive Director and Chairman of the Audit Committee of the following companies: Spectris plc, Rexam Plc, Bovis Homes Group PLC, Rank Group Plc, Uniq Plc, Arla Foods UK plc, BPP Holdings plc.

ROLES AND RESPONSIBILITIES

MEMBERS

As a Group owned by a company limited by guarantee, we counterbalance the fact that we do not have shareholders by having a Membership which carries out a vital governance role. Membership is personal, unpaid and Members have no financial stake in the business. This independence allows Members to hold the Board to account for the stewardship of our assets and for providing an essential public service in a manner which will be sustainable for future generations.

Our Members are appointed by the Board but are selected by an independent Member Selection Panel which is required to maintain a balanced and diverse membership, broadly reflective of the range of our customer and other stakeholders' interests and drawn from across our supply area. The independent Chair of the Member Selection Panel is Glyn Mathias, its other Members being Arthur Walford and Menna Richards. Glyn Mathias will step down in July 2018 after five years of service, and Sir Paul Silk has agreed to undertake the role of Chair, appointed with effect from 6 July 2018 for an initial three year period.

There are presently 66 independent Members of Glas Cymru. Under the Company's Articles of Association each Director is also a Member. During 2017-18, 17 Members stepped down and 14 were appointed.

We hold an AGM and a second Members' meeting each year to provide a six-monthly update on our performance and strategy. We also hold two regional Members' meetings which we move around the supply area to provide a more informal opportunity to gain insight into our working sites, meet local teams or provide a more in-depth overview of our strategies. Members are invited to other meetings and workshops on an ad hoc basis throughout the year. During 2017-18, a Members regional meeting was held at Builth Wells and Elan Valley, and Member workshops on Welsh Water 2050 strategy and on the PR19 Price Review were held in Cardiff.

BOARD

The Group's Board of Directors is collectively responsible for its long-term success. The Board sets the Group's strategic aims, monitors the performance of management against the strategic aims, ensures good governance, sets the risk appetite and ensures that effective controls are in place in the business. The Boards of Glas Cymru Holdings Cyfyngedig and Dŵr Cymru Cyfyngedig (the licence holder/operating company) are identical, which ensures a unified approach.

CHAIRMAN

Our Chairman, Alastair Lyons, plays a key role in helping to ensure a unified Board, facilitating meetings, and ensuring good governance. Meeting agendas are agreed in consultation with the Chief Executive and Company Secretary, although any Director may request that an item be added to the agenda. At least once a year, the Chairman meets with the Non-Executive Directors without the Executive Directors present, to consider the performance of the Executive Directors and to provide feedback. The Chairman also meets individually with each Board Member to review individual performance at least once each year.

SENIOR INDEPENDENT DIRECTOR

Our Senior Independent Director, Menna Richards, liaises with our Members. The Senior Independent Director meets with the other Non-Executive Directors and the Executive Directors on an annual basis to review the performance of the Chairman.

NON-EXECUTIVE DIRECTORS

Non-Executive Directors are appointed to the Board in accordance with our Diversity Policy, to contribute their expertise and provide independent challenge and rigour in the Board's deliberations.

CHIEF EXECUTIVE

Beyond matters reserved for the Board, the Chief Executive has primary responsibility for managing the day to day affairs of the company. Our Chief Executive, Chris Jones, is supported by the Executive team in implementing strategy and day to day management.

COMPANY SECRETARY

Our Company Secretary, Nicola Williams is responsible for supporting the Chairman in ensuring that the Group demonstrates good governance. The Company Secretarial team is available to the Non-Executive Directors and works to ensure that there are good information flows between the Board, Committees and management of the company.

OUR GOVERNANCE

Strong corporate governance underpins the values set by the Board, and supports the decision-making framework of the Group. We voluntarily comply with the UK Corporate Governance Code as far as possible for a Group owned by a company limited by guarantee. We apply the provisions set out in relation to shareholders, as far as possible to our Glas Members and investors as far as appropriate. The details of our governance framework are set out on pages 58-62. Our economic regulator, Ofwat, has also developed a set of principles which complement the code and represent the minimum standards for Board leadership, transparency and governance for companies in the water sector. We respond to the Ofwat corporate governance requirements in our Governance Code. For further details, please refer to **dwrcymru.com/governance**.

Corporate governance is about more than how a company is controlled and directed, it is about the behaviour, culture and value of an organisation and the way that this can improve business effectiveness and improve trust. The culture of Glas Cymru Group is set by our Board and aligned to our strategy and vision, but this requires the support of our colleagues throughout the business. Some of the ways the Board and Dŵr Cymru Executive Team reinforce the culture, include:

- Our Chief Executive holds a monthly telephone conference call that all employees may join to hear updates on the company and ask questions;
- Our Chairman and Non-Executive Directors undertake regular operational site visits and meet with colleagues in the business. This is important in ensuring that the current issues in the business are understood in context;
- Six monthly Leadership Conferences comprise Senior Managers from across the business to hear from the Executive team;
- Regular employee Roadshows and 'Meet the Director' days with the Executive team are held across the business;
- Responding to feedback from our annual Employee Engagement Survey; and
- Promoting our whistleblowing policy, which includes an external helpline to reassure colleagues that they can raise any issues anonymously should they wish to do so.

UK CORPORATE GOVERNANCE CODE PROVISION — LEADERSHIP

- As we provide a vital public service, we understand that how we are governed is crucial to earning the trust of our customers. It is our vision to earn the trust of our customers every day;
- We are headed by an effective Board which is collectively responsible for the long-term success of the company;
- We have a clear division of responsibilities between the running of the Board and the executive responsibility for the running of the company's business. No one individual has unfettered powers of decision-making;
- Our Chairman is responsible for leadership of the Board and ensuring its effectiveness; and
- Non-Executive Directors constructively challenge and help develop proposals on strategy.

MATTERS RESERVED TO THE BOARD

We have a schedule of matters reserved for the Board under which the Board retains ultimate responsibility for areas such as strategy, risk and many other decisions. The schedule of matters reserved is periodically reviewed and updated, along with forward schedules and agendas.

The Board delegates responsibility to management for the day to day running of the business according to the strategy set, and to Committees for specific areas as set out in their terms of reference. A forward plan is maintained by the Company Secretary for Board and Committee meetings set in conjunction with the Chairman and Committee Chairs. The Board is encouraged to review the terms of reference for committees and to feed into the forward schedule annually.

The Board has overall responsibility for the operation and effectiveness of the Group's system of internal controls and risk management. The system of controls is designed to manage the risk of failure to achieve business objectives, and comprises audited policies and procedures aimed at identifying and managing the most significant risks faced by the business.

ACTIVITIES

During 2017-18 the areas of focus for the Board have included:

- Health & Safety policy and management;
- Oversight of operational performance;
- Business planning;
- Ofwat Price Review preparations;
- Efficiency reviews;
- Welsh Water 2050;
- Risk management processes and risk appetite;
- Commercial opportunities;
- Innovation.

BOARD MEETINGS AND ATTENDANCE

In 2017-18 the Board held 11 scheduled meetings and one additional meeting. Most of our scheduled meetings are held over two days to give the Board the time it needs to review progress against strategic objectives and to meet key business managers. During the year, our regular scheduled Board meetings were extended on some occasions to address particular issues arising from the preparation of Welsh Water's business plan for the PR19 Price Review process.

All Directors are expected to attend meetings of the Board and of those Committees of which they are a member. When a Director is unable to participate in a meeting the Chairman will seek their views on key items ahead of the meeting so that these can be added to the discussion. Directors' attendance is shown in the following table:

Director	Board	QEC	Audit	Remuneration	Nominations	Finance
Peter Bridgewater	12/12	-	5/5	-	-	0/0
Tom Crick *	6/7	3/3	-	-	-	-
Graham Edwards	12/12	6/6	4/5	-	3/3	-
Chris Jones	12/12	6/6	5/5	-	3/3	0/0
Joanne Kenrick	11/12	5/6	5/5	-	-	-
Alastair Lyons	12/12	6/6	-	5/6	3/3	0/0
Stephen Palmer **	8/9	4/4	-	-	-	-
Peter Perry	12/12	6/6	-	-	-	-
Menna Richards	11/12	-	-	5/6	3/3	-
Anna Walker	11/12	-	4/5	5/6	-	-
John Warren	12/12	-	5/5	6/6	-	0/0

*Tom Crick joined the Board in October 2017 **Stephen Palmer retired in December 2017

All of our Non-Executive Directors allocate sufficient time to fulfil their duties. During 2017-18 the Chairman took on the role of Chair at Harworth Group Plc and joined the Board of Vitality Health Limited, however, he stood down as Chairman of Admiral Group plc during the period.

APPOINTMENTS

The Board is committed to a transparent process for new appointments and the Board is committed to ensuring the right balance of skills and experience and diverse backgrounds. Directors must display independent judgement and an ability to challenge constructively. The search for Board candidates is conducted by the Nominations Committee on the basis of merit, against objective criteria set for the role, and with due regard to maintaining an appropriate balance of skills and experience and to the importance of ensuring diversity of representation on the Board. External selection companies are used to find candidates and support the process. In 2017, we used the external search company, Goodson Thomas, to find Tom Crick, who joined our Board in October 2017.

The Non-Executive Directors' letters of appointment are made available for public inspection upon request to the Company Secretary and are available at each Annual General Meeting for inspection by our Members.

Glas Cymru is committed to promoting diversity, non-discrimination, and equality of opportunity in the way we treat employees, prospective employees, visitors, clients, customers and suppliers. The Board has documented its approach to recruitment in a Diversity Policy which it is committed to following.

UK CORPORATE GOVERNANCE CODE PROVISIONS — EFFECTIVENESS

- The Board and its Committees have the appropriate balance of skills, experience, independence and knowledge of the company to enable them to discharge their respective duties and responsibilities effectively. The Board regularly reviews this in discussions with the Company Secretary, Nominations Committee and as part of our effectiveness review.
- Glas Cymru has a formal, rigorous and transparent procedure for the appointment of new Directors to the Board.
- Directors receive a tailored programme of induction on joining and ongoing educative and informative programmes on topics relevant to the operation and governance of the business.
- All Directors allocate sufficient time to the company to discharge their responsibilities effectively.
- Board and Committee meeting materials are provided a week in advance.
- Our Non-Executive Directors have access to the Company Secretary and external advisors to provide the Board with an external viewpoint.

INDUCTION AND DEVELOPMENT

INDUCTION

New Non-Executive Directors undergo a personalised induction process, including access to past Board and Committee papers, site visits and one to one meetings with senior managers. Where appropriate, new Non-Executive Directors also attend the Institute of Directors' course for new Directors.

UNDERSTANDING THE OPERATIONAL BUSINESS

This year our Quality and Environment Committee of the Board held two site visits around the business, at Nash WWTW and our RainScape scheme in Llanelli. Our Chairman undertakes regular operational site visits across the supply area and other Non-Executive Directors are encouraged to attend at last one of these visits during the year.

Visits in 2017/18 were as follows:

April 2017: Cefni WTW, Llangefni WWTW, Ganol WWTW

May 2017: Linea (overview of operational services including data science and data governance)

June 2017: Dolbenmaen WTW (for the official opening), Pen Y Cefn WTW, Dolgellau WWTW

July 2017: Bretton WTW, Cwellyn WTW, Llanberis WWTW, Five Fords

August 2017: Sluvad Training Rig, Llandegfedd, Court Farm WTW, Nash WWTW and Elan Valley

September 2017: Glien House & Bolton Hill WTW

October 2017: Kinmel Park, Glascoed WTW, Chester WWTW

March 2018: Linea & Llanishen/Lisvane Reservoir

Continuing development of our Directors — we ensure that developments in legislation, corporate governance and reporting are brought to the attention of the Board and Audit Committee as appropriate. Regular attendance from our auditors, KPMG LLP, at Board and Audit Committee meetings has also meant that Directors have been brought up to speed on current issues, including the FRC consultation on proposals to amend the UK Corporate Governance Code. This year there has been a particular focus on the preparation for the PR19 price review process, with a teach-in for the Board provided by the Director of Regulation and Strategy and sessions provided by external consultants on particular aspects of the process.

BALANCE AND INDEPENDENCE

The Board and Committees have an appropriate composition to undertake their responsibilities effectively, based on a wide range of backgrounds, ages, skills and experience. The Board is satisfied that all Directors have adequate time to commit to their role. All of our Non-Executive Directors are deemed to be independent in accordance with the Corporate Governance Code and free from any business or other relationship which could compromise their independent judgement.

EFFECTIVENESS REVIEW

The effectiveness of the Board and its Committees is reviewed annually and an independent externally facilitated review is conducted every three years.

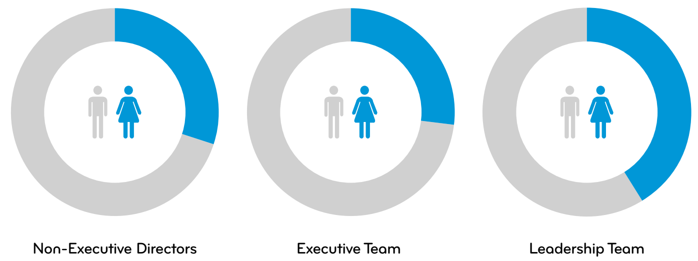
The 2018 Effectiveness review involved a detailed online survey of all Board Directors and regular Board attendees, followed by one-to-one meetings of each Director with the Chairman to discuss their particular comments and issues. While overall there was consensus from Directors that the Board and its Committees is operating very effectively, the detailed findings of the evaluation and proposals for further enhancement/improvement were discussed at the Board meeting in June and an action plan was agreed.

RE-ELECTION OF DIRECTORS

In accordance with the UK Corporate Governance Code, all Directors seek re-election every year by Members and any Director appointed during the year seeks election at the next AGM.

GENDER DIVERSITY

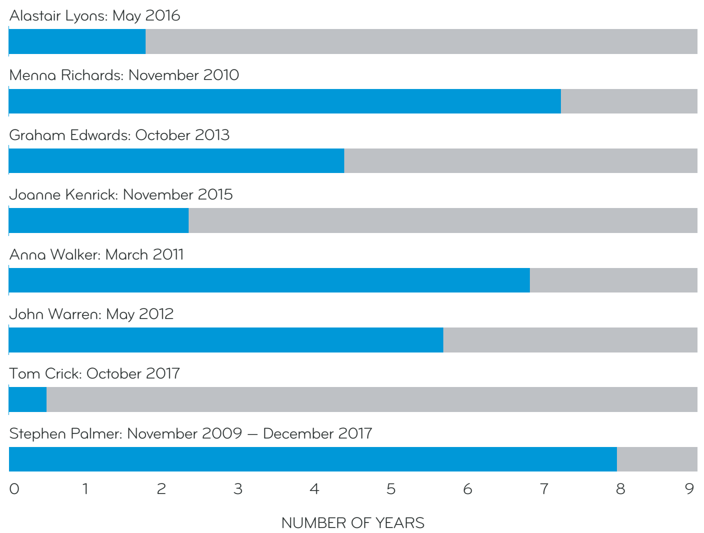
The Board is committed to having an appropriate level of diversity across all levels of the business. We currently exceed the Davies 2010 Report suggested targets at Board level for representation of women. Currently, women make up 30% of our Non-Executive Directors, 27% of the Executive team and 41.3% of the Group's wider Leadership Team. We published the Glas Cymru Gender Pay Gap Report on 8 March 2018. For further details please read the report on our website **dwrcymru.com/reports**.



CONFLICTS OF INTEREST

Under UK company law potential conflict situations must be authorised in advance to avoid a Director being in breach of their statutory duty. All Directors must immediately disclose conflicts, or potential conflicts, of interest. In addition, all Directors sign an annual declaration of their interests and disclose their external appointments. Directors also let the Chairman and Company Secretary know of any pending appointments and announce any new external appointments at the next Board meeting so that all of the Board are made aware.

LENGTH OF SERVICE



EXTERNAL APPOINTMENTS OF THE EXECUTIVE DIRECTORS

Peter Bridgewater is a Non-Executive Director of Ebico Limited, for which he is separately remunerated £15,000 per annum.

UK CORPORATE GOVERNANCE CODE PROVISION — ACCOUNTABILITY

The combined Board of Glas Cymru and Dŵr Cymru:

- ensures that the Annual Report & Accounts presents a fair, balanced and understandable assessment of the company's position and prospects.
- determines the appropriate risk appetite in achieving our strategic objectives, whilst ensuring sound risk management and internal control systems.
- has formal and transparent arrangements for considering how it should apply the corporate reporting, risk management and internal control principles and for maintaining an appropriate relationship with the company's auditors.
- All Directors stand for re-election by Members at each Annual General Meeting.
- Each Non-Executive Director holds office for a period of three years which may be extended until the end of nine years from appointment.

UK CORPORATE GOVERNANCE CODE PROVISION — REMUNERATION

- We have a Remuneration Committee whose report is set out in pages 69-81.
- Executive Directors' remuneration is designed to promote the long-term success of the company.
- Performance-related elements are transparent, stretching and rigorously applied.
- There is a formal and transparent procedure for developing policy on Executive remuneration and for fixing the remuneration packages of individual Directors.
- No Director is involved in deciding his or her own remuneration.
- The Remuneration Committee receives advice from external consultants.

UK CORPORATE GOVERNANCE CODE PROVISION — RELATIONS WITH SHAREHOLDERS

- We voluntarily apply the shareholder principles on governance to our Members and Investors.
- We have regular dialogue with Members and bond investors.
- Our Board uses general meetings to communicate with Members.
- The Company's Treasury team continues to ensure that our investors are well informed, through quarterly reports and the annual investor meeting in London, as well as regular informal meetings. The Board receives a report following meetings with investors and, where appropriate, takes into account the views expressed by investors on issues affecting the Company.
- Our Group Treasurer is always happy to arrange to meet with investors where requested. This year the following meetings were made available to all investors and potential investors:
- Annual Investor update (London) — 19th July 2017
- Bond Roadshow, Edinburgh 12th January 2018, London 15th and 16th January 2018 — leading to the launch of the Group's £300m B7 Bond Issue due 31st March 2036 at a fixed coupon of 2.5%.

ANNUAL GENERAL MEETING DETAILS

Our Members' AGM will be held on Friday 6 July 2018 at the Marriott Hotel, Swansea at 9:30am.

BOARD COMMITTEES

As explained earlier in the report, the Board reserves certain matters to itself. In order to ensure the Board fulfils its role effectively, certain responsibilities of the Board are delegated to Committees, which play an important role in working with management to ensure our business is financially strong, well governed and risks are identified and mitigated. Each Committee is chaired by a Non-Executive Director. Each Committee of the Board has written terms of reference which summarise the responsibilities delegated to it.

The terms of reference are regularly reviewed and approved by the Committee and the Board. Upon joining a Committee, Directors are provided with an appropriate induction and are offered ongoing training and education opportunities. After each meeting, a summary of matters discussed is reported to the Board, and Committee minutes are made available to Directors. Each Committee can engage the services of such advisors as it needs to fulfil its responsibilities.

Our principal Board Committees are:

Audit Committee
Chaired by John Warren
Report on page 64
2 2

Quality and Environment Committee
Chaired by Graham Edwards
Report on page 67
5 1

Nominations Committee
Chaired by Alastair Lyons
Report on page 68
2 1

Remuneration Committee
Chaired by Anna Walker
Report on page 69
2 2

Finance Committee
Chaired by John Warren
Report on page 68
4

Dŵr Cymru's Executive Team
Dŵr Cymru's Executive team (DCE) is our management Committee, made up of 11 members of the management team, (including the three Executive Directors). DCE is focused on ensuring that the business is run according to the strategy set by the Board and on reviewing Key Performance Indicators to ensure that the targets set by the Board are met. Numerous management committees and project groups report to DCE.

Non-Executive Directors
Our Non-Executive Directors have diverse skills. In addition to chairing or being a member of a Committee, each Non-Executive Director commits additional time and input on the following matters:

Alastair Lyons
General engagement with Executive Directors and operational involvement with regular local site visits

Graham Edwards
Operations and HR related issues

John Warren
Finance and audit

Menna Richards
Communications and Member relations

Anna Walker
Customer service, regulation and remuneration

Joanne Kenrick
Marketing, commercial and customer services

Tom Crick
Data science, education and Welsh Government policy

Some of our Non-Executive Directors also mentor some members of the management team.

GLAS CYMRU HOLDINGS CYFYNGEDIG | ANNUAL REPORT & ACCOUNTS

INTERNAL CONTROL

The Board has overall responsibility for the operation and effectiveness of the Group's system of internal controls and risk management. The system of controls is designed to manage the risk of failure to achieve business objectives, and comprises audited policies and procedures aimed at identifying and managing the most significant risks faced by the business.

A detailed review of risk is set out on pages 44-46. In considering the development of the system of controls, the Executive team reviewed the materiality and the relative cost benefit associated with each identified significant risk. The internal control systems are designed to provide reasonable assurance against misstatements, loss or failure. The key features of our system are typical for a business of our scale and complexity. They include:

- identification of key strategic risks and opportunities facing the business;
- reviewing emerging and current issues at meetings of the Executive and the Quality and Environment Committee;
- clear management accountability for risk management, supported by regular risk reporting to the Board, the Quality and Environment Committee and the Audit Committee;
- acceptable risk parameters set by the Board, particularly in the context of the business planning process for the purposes of the next five year period;
- implementing controls that recognise that the nature and balance of risk changes and evolves;
- implementing procedures that govern the approval and control of major items of capital expenditure, the acquisition and disposal of material assets, and commitment to any arrangement that could give rise to a material liability;
- ensuring that financial systems and procedures are fit for purpose for preparing management and financial accounts; and
- an appropriate design of management processes to ensure the effective direction and review of the business' operations supported by accurate and timely key performance indicators.

The Board receives assurance from independent work by Welsh Water's technical advisor on regulatory reporting issues (Jacobs Engineering Group) and from the programme of internal audit, the major findings from which are reviewed at the Audit Committee and the Quality and Environment Committee.

Risk is reviewed and considered at each meeting of the Board and a strategic review of risk against risk tolerances is considered twice a year under a process chaired by the Chief Executive, who submits an update to the Board of the Executive team's view of the key strategic risks facing the business so that this can be considered by the Board as a whole. The process to review the effectiveness of internal control includes discussion with management on significant risk issues and a review of plans for, and results from, internal and external audit. The Audit Committee reports the results of its review to the Board which then draws its collective conclusion on the effectiveness of the system of internal controls.

In fulfilling this responsibility, the Board considers periodic reports from the Audit Committee, Quality and Environment Committee and from management, and relies on its routine monitoring of key performance indicators and monthly reports of financial and operational performance. This enables the Board to review the effectiveness of the internal control system throughout the course of the year.

REPORT OF THE AUDIT COMMITTEE

Chair: John Warren
Members: Graham Edwards, Joanne Kenrick, Anna Walker

The Audit Committee has had a busy year with a focus on compliance issues, particularly in the light of the programme to ensure compliance with the new General Data Protection Regulation, applicable from May 2018, and on measures taken to mitigate information security risk in the business.

The Audit Committee meets the requirement to have relevant sector expertise as Graham Edwards is Chief Executive of another utility company and has previous experience of working for another company in the water sector.

As Chair of the Committee, I bring financial experience as a chartered accountant having previously worked as Finance Director of WH Smith and United Biscuits, and chaired Audit Committees in other large companies. The Chief Executive, Finance Director and Head of Business Assurance are regular attendees at meetings of the Committee.

The Audit Committee met on five occasions during 2017-18. Following the end of the financial year on 31 March 2018, the Committee met on a further two occasions as in previous years. The Committee received the report from the external auditors on the 2017-18 Annual Report, focusing in particular on the key areas of judgement in the financial statements. The Committee also critically reviewed a draft of the Annual Report for 2017-2018 in order to ensure that it presented a "fair, balanced and understandable" assessment of the company's financial status, in accordance with the UK Corporate Governance Code.

The Audit Committee is supported by the external auditors, KPMG LLP, who were appointed in September 2015 for a period of up to five years.

END OF YEAR FINANCIAL STATEMENTS

As in previous years, the Audit Committee and the external auditors have focused on those areas of the financial statements which involved the highest level of management judgement applied to them, and on those which are considered to be the most inherently risky. For the end of year financial statements, these were as follows:

Revenue recognition including accrued income on metered sales
Revenue represents the income receivable for services provided. Where services have been provided but no invoice raised, an estimate of the value is accrued and included in revenue — the measured income accrual. The billing system calculates the measured income accrual on an individual meter basis. At 31 March 2018 this estimate was £70.8m, an increase of £2m since the prior year end driven principally by growth in the metered customer base. Management reviews the assumptions used in the accrual including volume estimates and charges applied, and the Committee remained satisfied that the approach taken was consistent and balanced for the purposes of the accounts.

Classification of costs between operating expenditure and capital expenditure
The company continues to invest a high level of expenditure in fixed assets, including repair and maintenance as well as enhancement. There is judgement involved in determining whether costs, both initial and subsequent expenditure, on both infrastructure and non- infrastructure assets, meet the relevant criteria for capitalisation. The level of net capital expenditure rose in the year to £380.6m (2017: £342.3m) as anticipated as the capital delivery teams continued to build capacity during the third year of the five-year investment programme. The Committee was satisfied that the judgements made and the amounts capitalised were appropriate.

Provision for impairment of trade receivables
The level of provision required is based on an assessment of historical cash collection performance, having regard to ongoing economic uncertainty and the reform of the state welfare system. Recent increases in cash collections as a result of ongoing initiatives to improve performance were also taken into account. In making the recommendation to the Audit Committee, management examined cash collection performance for measured and unmeasured customers during 2017-18, concluding that Welsh Water could ultimately expect to collect some 55.7% of (non billed in- advance) debt outstanding at 31 March 2018 (2017: 48.7%).

Considering all the historical collection information, the Audit Committee agreed that Welsh Water's bad debt provision be set at £83.8 million (2017: £96 million) reflecting a higher write off of aged debt in the year, thereby reducing the balance sheet provision. The doubtful debt charge in the income statement ("trade receivables impairment") of £22.1 million at 31 March 2018 has marginally reduced on the prior year charge (31 March 2017: £23.3 million). This reflects new charging orders in 2017/18 increasing recoverability.

Retirement benefit obligations
Calculation of the defined benefit pension liability for inclusion in the balance sheet in accordance with IAS 19 requires the use of two key financial estimates, namely the discount rate to be applied to the future liabilities and future inflation of those liabilities. The assumed discount rate was derived from the yields of AA-rated corporate bonds, and the assumed level of inflation was determined having regard to the difference between the yields on fixed interest and index-linked government bonds as well as other sources of inflation forecasting. The committee discussed these assumptions with KPMG who noted that the assumptions were within an acceptable range. The fair value of the defined benefit pension assets has reduced by £6.8 million during the period. The Committee concluded that valuations have been performed consistently by individual fund managers who use a range of techniques which are exposed to market volatilities, hence the slight reduction in valuation.

The Committee concluded that the assumptions used were acceptable for the purposes of the accounts and in particular that the applied discount rate of 2.80% is within the acceptable range.

Derivative financial instruments
The fair values of derivative financial instruments are provided by swap counterparties. The Bloomberg financial dataset platform allows management to perform an independent valuation of these contracts which is compared to counterparties' confirmations before an appropriate "own credit risk" adjustment is applied. The total (net) balance sheet liability at 31 March 2018 amounted to £397.1 million (2017: £477.0 million). The Committee agreed that this was a reasonable figure to include in the accounts.

The Committee also noted the impact of IFRS 15 (revenue recognition) and IFRS 9 (classification and impairment of financial assets) which will need to be reported against in more detail in the 2019 Annual Report.

OTHER ACTIVITIES OF THE AUDIT COMMITTEE

The May and November meetings of the Audit Committee, as in previous years, focused on reviewing the Group's preliminary and interim financial results and related areas of judgement and accounting policy.

The Audit Committee relies on the active role played by the Business Assurance (internal audit) function in providing assurance and reviewing the adequacy of internal control and arrangements to manage risk, reporting on this to the Executive team and the Committee. The Committee reviews and approves the Business Assurance plan of work for the year and reviews progress against the plan.

The Head of Business Assurance took the Committee through a review of progress against the Business Assurance plan at the half year and again at year end, for both operational audits and process audits, and also developed a robust and challenging plan for 2018-19 which the Committee approved in February 2018. The Quality and Environment Committee had separately approved the Business Assurance plan as it concerned the audit of operational processes. The Business Assurance function is continuing to work closely with the Compliance team to improve policies and procedures in areas such as supplier management, prompt payment of supplier invoices and compliance with our Group Code of Conduct.

During 2017-18, the Committee continued to use private meetings to review investigations of issues raised by whistleblowers from within and outside the company, in accordance with the established whistleblowing policy. The policy encourages employees and others to report issues, protects individuals who make relevant disclosures and includes the provision of an independent hotline for the reporting of issues. The Committee considers the whistleblowing policy to be an essential element in the system of internal controls.

The Audit Committee also continued to receive independent advice and assurance in relation to the accuracy and completeness of regulatory reporting during 2017-18 from Welsh Water's technical adviser on regulatory reporting issues, Jacobs Engineering Group. Following a tender process, Jacobs were appointed for an initial period of three years in April 2016. Jacobs supported the preparation of the Annual Performance Report which was submitted to Ofwat in August 2017 and also provided input to the Assurance Plan and methodology statements to support the company's reporting against its Measures of Success from the 2016 Final Determination, which will underpin the reporting in the Annual Performance Report in August 2018.

The Committee holds private meetings at least once a year with each of the external auditors and the Head of Business Assurance.

OTHER TOPICS REVIEWED BY THE AUDIT COMMITTEE IN 2017-18 INCLUDED:

- Detailed consideration of the Group's financing strategy and recommendation to the Board of the proposal to enter into a new £300m bond facility;
- Oversight of the compliance programme to improve our systems and processes to ensure compliance with the General Data Protection Regulation from May 2018;
- Review of Treasury policies and controls, including the approval of new cash limits for our relationship bankers;
- Cyber-Security, information security issues and IT disaster recovery arrangements, including considering the comparative effectiveness of our procedures for managing risk in this area compared to those established in similar businesses;
- Supplier arrangements and compliance with procurement policies;
- The timetable and processes for finalising the Annual Performance Report;
- The steps taken by the Group to comply with Corporate Governance requirements, including the Modern Slavery Act 2015, and Gender Pay Gap reporting in March 2018;
- The outcomes of internal audit reports and timescales to complete the recommended actions.

The Committee also reviewed the results of an internal evaluation of Committee performance in March 2018 and has reviewed the performance of the external auditors during the year.

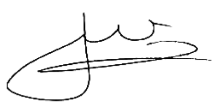
NON-AUDIT AUDITOR FEES

Our policy is that the external auditors will not generally be used for internal audit services, and that all non-audit matters will be subject to the Group's Procurement Policy.

All non-audit fees paid to Auditors must either be approved by the Committee in advance or in an urgent situation approved by the Chair and then reported to the Committee at the next meeting. During the period 2017-18 audit fees for the Group's financial statements totalled £159,000 and fees for other assurance services were £143,000. Fees paid in respect of non-audit related services amounted to £203,000. The ratio of other assurance and non-audit fees to audit fees was therefore 2.18x. The Audit Committee will continue to monitor the ratio of non-audit to audit fees in view of the forthcoming changes in guidance for listed companies. Further information is available in the financial statements on page 112.

MEETINGS WITH INVESTORS

The Committee members are available to meet with investors by prior arrangement with the Company Secretary. This year's formal Investor Meeting will take place at the Andaz Hotel, London at 8:30am, 11 July 2018.



John Warren
Chair of the Audit Committee

7 June 2018

REPORT OF THE QUALITY AND ENVIRONMENT COMMITTEE

Chair:
Graham Edwards (since January 2018),
Stephen Palmer (was chair until December 2017)

Members:
Chris Jones, Joanne Kenrick, Alastair Lyons, Peter Perry and Tom Crick (from October 2017)

Independent Scientific Advisors:
Steve Brown (Environment), Andrew Davies (Water) (until February 2018), Julian Dennis (Water) (appointed in February 2018)

The Board has delegated responsibility to the QEC for reviewing and monitoring strategic risk areas of Health and Safety major incidents, environmental regulation, failure to achieve required performance levels, strategic asset failure and major public health incident. The QEC is also responsible for scrutinising operational performance and assessing the appropriateness of improvement strategies for Welsh Water's water and waste water activities.

The QEC also:

- reviews, monitors and influences the health and safety management plan and its delivery;
- ensures that Welsh Water fulfils its public health responsibilities for the provision of safe;
- clean drinking water and waste water sanitation in line with all statutory standards;
- ensures the company has adequate emergency and security arrangements in place in line with current statutory guidance such as Critical National Infrastructure (CNI) and Security and Emergency Measures Directive (SEMD) standards;
- reviews and influences the company's non-financial audit programme and receives the findings of internal and external audit reports relating to water and waste water service provision.

The QEC meets key stakeholders on behalf of the Board. During 2017-18 senior management from the Drinking Water Inspectorate and Natural Resource Wales attended meetings.

The QEC plays an important role in encouraging the smart use of data and the adoption of appropriate new technology or other innovation that will improve service to customers and the environment. Examples of projects utilising smart use of data include chlorine mapping to improve customer experience and a model to support sewer blockage prediction.

The Committee reviews the findings of investigations into any water quality, environmental or customer service failure. Serious Incident Reviews are undertaken by the Chief Executive and Managing Director of Dŵr Cymru who meet with the relevant Managing Director of Water/Wastewater respectively for those failures deemed serious. A report is made to the QEC detailing root cause, lessons learnt and actions to follow. During 2017-18 Serious Incident Reviews were carried out in respect of water quality or pollution incidents at Ponsticill Water Treatment Works, Eign Wastewater Treatment Works and Gaerwen regarding a sub-contractor health and safety incident whilst undertaking capital works.

Examples of areas of focus for QEC involvement in 2017-18 included:

- H&S reports
- Performance reports for Water and Wastewater
- Dam Safety Annual Report
- Zonal Studies Strategy
- Iron and Acceptability Strategy
- Customer Minutes Lost Strategy
- Catchment Strategy
- Security and Emergency Measures Directive Audit Results
- Flooding Strategy
- Pollution Strategy
- Event Duration Monitors Strategy
- Odour Reduction Strategy

Graham Edwards
Chair of the Quality and Environment Committee

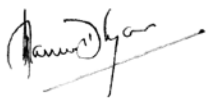
7 June 2018

REPORT OF THE NOMINATIONS COMMITTEE

Chair: Alastair Lyons
Members: Graham Edwards, Chris Jones and Menna Richards

The role of the Committee is to review the succession planning for the Board and to put in place processes to address this, reporting to the main Board. The Nominations Committee also reviews policies relevant to recruitment, in particular our Diversity Policy.

In 2017-18 the Nominations Committee commenced the process of identifying a successor to Professor Stephen Palmer. After a tender process, Goodson Thomas were appointed to advise the Committee and support the process. Professor Tom Crick was appointment to the Board in October 2017 and Stephen Palmer stepped down in December 2017.



Alastair Lyons
Chair of the Report of the Nominations Committee
7 June 2018

REPORT OF THE FINANCE COMMITTEE

Chair: John Warren
Members: Peter Bridgewater, Chris Jones, Alastair Lyons

The Finance Committee is established with authority to approve financial decisions quickly on an ad hoc basis between meetings. It is our intention to use this Committee rarely as we generally plan sufficiently far in advance to deal with such issues at Board or Audit Committee Meetings. The Finance Committee did not meet in 2017-18.

John Warren
Chair of the Report of the Finance Committee
7 June 2018

REPORT FROM THE CHAIR OF THE REMUNERATION COMMITTEE

Chair: Anna Walker
Members: Alastair Lyons, Menna Richards, John Warren

On behalf of the Board, I am pleased to present the Remuneration Committee and the Directors' Remuneration Reports for 2018. Ensuring value for money and good governance around remuneration policies are essential to building trust with our customers and other stakeholders.

THE ROLE OF THE COMMITTEE

The role of the Remuneration Committee is to recommend to the Board for approval, and keep under review, the Remuneration Policy of the Board as it applies across the business as a whole. More specifically the role of the Remuneration Committee is:

- to agree the Policy and framework and service contracts for the remuneration of the Chairman and the Executive Directors, and the remuneration framework for the Executive team in the context of remuneration policy across the Group; and
- to determine variable pay arrangements that encourage and recognise good performance and reward individuals in a fair and competitive manner for their contribution to the long-term success of the Group, and to develop the policies to support these principles.

In carrying out its role, the Committee applies certain key principles (set out below) which it agreed in 2015-16 and have been discussed with Glas Members.

During 2017-18, the main activities of the Remuneration Committee have included:

- consideration of remuneration trends and best practice;
- setting "stretch" performance targets for Executive Directors and monitoring progress against these;
- reviewing the target remuneration for the broader Executive team;
- reviewing the salaries of the Executive Directors and the Chairman's fee, and considering recommendations for the proposed annual increase;
- assessing performance achieved against the conditions attached to the 2017-18 Annual Variable Pay Scheme (AVPS) and AMP6 Long Term Variable Pay Scheme (LTVPS) and agreeing awards to be made to participants;
- approving the 2017 Remuneration Report;
- reviewing the work carried out by KPMG on gender pay gap reporting to enable reporting in March 2018 following approval by the Board of a plan to work towards further reducing the identified gap;
- considering the key elements of the Remuneration Policies which will apply to the business during 2020-25 and the external factors that will be relevant, as the Board begins to consider the framework for pay and rewards across the Glas Group for the next five year price control period.

THE ROLE OF GLAS MEMBERS

Glas Members play a key role in ensuring good governance in relation to the development and approval of remuneration policies.

Members approved the current remuneration policy at the 2015 Annual General Meeting (AGM) and the policy will be subject to Member approval again at the forthcoming 2018 AGM, when Glas Members will be asked to re-approve the policy for a further period to April 2020. From that date, a revised policy will be necessary which picks up the key performance issues for AMP7. This is also in accordance with the remuneration reporting regulations applying to UK quoted companies. Members approve the Remuneration Policy of the Board by binding vote, at least every three years (or where any significant change is proposed).

The Annual Report on Remuneration will also be subject to an advisory vote by Members at the forthcoming 2018 AGM, as usual. At last year's AGM, 100% of Glas Members voted in favour of the Annual Report on Remuneration.

At this year's AGM, the Committee will also update the Members on the initial work undertaken to date to prepare the policy which would apply to the period 2020-2025 and plans to involve Members in the development of the Remuneration Policy for the next AMP period.

The revised Remuneration Policy will be presented to Members for approval at the 2019 AGM. Remuneration targets will be linked to the performance measures the company will be targeting in the period 2020-2025, and will be consistent with the Group's longer term aims as set out in the Welsh Water 2050 strategy. The proposed revised remuneration policy would take effect from April 2020 when the new price control period begins.

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GLAS GROUP REMUNERATION PRINCIPLES

Agreed with Glas Members at the 2015 Annual General Meeting

- Remuneration should reward/incentivise the long term interests of the business and reflect its agreed future strategic approach
- Remuneration should help align the interests of directors and employees with the business' customers
- Remuneration should be focused on the issues of key concern to the business – water and environmental quality, customer service and financial performance
- Remuneration should reflect Welsh Water's aim to be one of the best performing companies in the sector
- Remuneration targets should be stretching both in relation to past performance and in comparison with other companies in the sector. Where possible, they should be hard numbers which can be audited. While some are annual, they should also align with the business' strategic and regulatory objectives
- Remuneration is intended to incentivise management in the absence of shareholders and share options
- Remuneration should be fair and competitive both in relation to the sector and internally so as to help attract and retain high calibre individuals
- A significant proportion of remuneration for the Executive directors should be variable (a 60/40 split fixed/variable is the current stated goal) so as to achieve the right balance in relation to risk taking
- The remuneration structure should be sufficiently clear so that those affected by it understand what it is aiming to achieve
- Remuneration will be transparent to Glas Members and subject to their regular approval.

EXTERNAL CHANGES AND DEVELOPMENTS RELEVANT TO REMUNERATION POLICIES

The last year has seen a continuation of the structure established for remuneration in the current AMP period (2015-2020) and a focus by the Committee on the external changes and challenges that will impact on the business over the next five year period. This includes consideration of the appropriate benchmarks against which to consider pay and reward, with reference to:

- The need to be able to plan for the longer term, and to attract and retain appropriate skills and talent, particularly given the significant future challenges identified in the Group's Welsh Water 2050 strategy document;
- Corporate governance developments including preparation for AMP7 and Ofwat's focus on transparency, and performance related pay that is clearly linked to the underlying performance of the company;
- The Group's structure and its non-shareholder owned status.

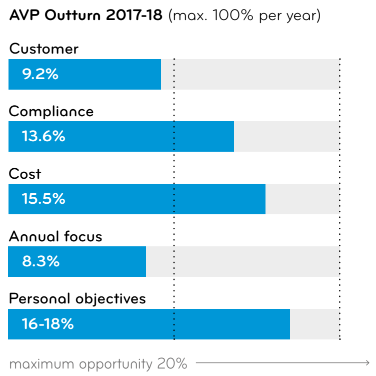
Having spent time considering the structure and content of the Group's remuneration policies against this variety of benchmarks, the Committee has also worked with its newly appointed consultants, Mercer, to consider the key elements proposed for the remuneration policies which will apply for the next five year funding period 2020-25. Pay must incentivise strong performance by Executive Directors, while not encouraging excessive risk taking. In considering the approach to structuring remuneration and the link to performance, the Committee has had in mind the content of the documented Welsh Water 2050 strategy, which focuses on addressing longer term risks and issues and building greater resilience.

During the year, a restructure of the Executive team has seen the appointment of Peter Perry as Managing Director of the regulated business (previously Chief Operating Officer), Samantha James as Managing Director for Household Customer Services, and Ian Wyatt as Director for Business Customer Services. There was also some restructuring of responsibilities among the executive team. This restructuring of the senior management teams has involved the Committee in considering the application of the current Group's Remuneration policies to the newly formed Executive team.

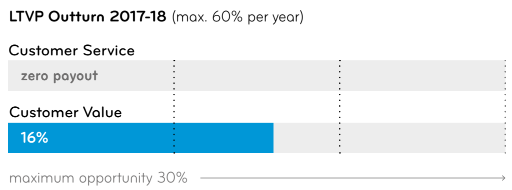
PERFORMANCE AND REWARD FOR 2017-18

Remuneration payable to the Executive Directors in respect of the financial year ended 31 March 2018 was as follows:

- a base salary (which had been increased by 1.6% in April 2017) plus pension (or equivalent payments) and private health and permanent health benefits;
- under the AVPS 2017-2018 awards have been made equivalent to 22.8% of base salary for performance against the Customer and Compliance element of the scheme, 15.5% for Total Expenditure (Totex) Cost Performance and between 24.3% and 26.3% against Strategic (Annual Focus) and Personal Objectives, making a total award of between 62.6% and 64.6% of base salary for each Executive Director; and



- under the LTVPS, payment has been made for performance relating to the Customer Value element of the scheme: no amount is payable in respect of the Customer Value element of the scheme, which depends on the outcome of Ofwat's SIM performance measure.



Customer Service: The final outturn for Welsh Water's Service Incentive Mechanism (SIM Customer Service) performance in 2017-18 will not be known until later in the summer. However, we estimate that Welsh Water will be ranked joint 6th out of the ten water and sewerage companies which will mean there is no award payable this year for the Customer Service element of the award, calculated on a rolling three year average SIM basis.
The award would be adjusted if the results required this. It should be noted that relatively small differences in SIM outcomes have led to substantial reward variations in the recent past.

Customer Value: a payment of 16% of salary (53.3% of the maximum for this element of the LTVPS) has been awarded under the scheme for the Customer Value element given the financial achievement in the period.

IMPLEMENTATION OF THE REMUNERATION POLICY IN 2018-19

The agreed Remuneration Principles emphasise that remuneration for the Executive Directors and the wider Executive team should align with the interests of the Group, and in particular with the interests of customers. This will continue to govern our approach in 2018-19. The key points in relation to the implementation of the Remuneration Policy in 2018-19 are:

- Salaries were increased by 3% with effect from 1 April 2018 in line with the pay award received by other employees. The 3% award was agreed in the light of comparative benchmarking and continuing good performance;
- under the AVPS the maximum that can be earned in 2018-19 remains 100% of salary. The Scheme will continue to focus on customer, compliance, cost and personal objectives, as well as a number of other critical measures of short- to medium-term success; and
- the LTVPS provides that the overall maximum that can be earned in the AMP6 five year regulatory period is 300% of base salary (i.e. 60% per annum). Half of the LTVPS is subject to Customer Service measures and half to Customer Value measures.

The Directors' Remuneration Report includes:

- a Remuneration Policy Report (pages 72-74). The Committee remains satisfied that the Remuneration Policy remains broadly appropriate and fit for purpose and intends to seek a further approval from Members at the 2018 AGM to extend the current policy to the end of the current AMP period – March 2020. Members will be asked to approve a new Group Remuneration Policy at the 2019 AGM which will take effect from April 2020 when the next price control period starts.
- an Annual Report on Remuneration (pages 75-82) which describes how the Remuneration Policy was implemented for 2017-18 and how we intend to apply it for 2018-19. This will be put to an advisory Member vote at the 2018 AGM.

The Committee is grateful to New Bridge Street (Aon Hewitt) for the professional advice provided until July 2017 and to Mercer, who succeeded New Bridge Street as Remuneration Consultants to the Remuneration Committee with effect from August 2017.

In approving this Annual Remuneration Report, the Committee has taken into account the requirements of Ofwat's guidance on transparency in its Regulatory Accounting Guidance 3.09, including the requirement to include a note which describes the link between directors' pay and standards of performance as required by section 35A of the Water Industry Act 1991 (inserted into that Act by section 50 of the Water Act 2003) – as to which please see pages 76-79.

Anna Walker

Anna Walker
Chair of the Remuneration Committee
7 June 2018

POLICY REPORT

Key parts of the Policy Report which was approved by Glas Members at the 2015 Annual General Meeting have been included again in this report for the purposes of clarity and transparency. The original Policy Report can be found on pages 76 to 78 in the 2015 Report and Accounts on the Company's website dwrcymru.com/reports

REMUNERATION POLICY

The principles and framework of the current Remuneration Policy were approved by Glas Members at the AGM on 3 July 2015 and were effective from that date.

The Policy aligns executive remuneration with the implementation of Welsh Water's strategy to deliver the best possible outcomes for our customers and to protect the environment. Under the policy, remuneration is linked to performance both annually and over the five year regulatory period that commenced in April 2015.

The Policy is implemented to ensure that:

- levels of base salary and total remuneration (when assessed periodically against the market) are considered to be fair and competitive having regard to an individual's experience and responsibility;
- performance improvement is encouraged by ensuring that a significant proportion of the total remuneration opportunity is linked to performance, while balancing this with base salary to ensure that excessive risk-taking is not incentivised;
- incentives are focused on the outcomes which are considered important for customers and callibrated against the prior year's performance and against the performance of other companies as assessed by Ofwat and other regulators, in order to incentivise sector-leading performance in a transparent and accountable way; and
- the LTVPS is focused on the long term strategic, customer value and financial performance of Welsh Water.

The Group negotiates salaries for the wider workforce with three recognised trade unions by means of a single table approach. The Remuneration Committee takes note of the process and the agreed increase for the wider employee base and also reviews market practice and conditions.

The Measures of Success and cost elements which form the basis of the AVPS for Executive Directors and the wider Executive team are also the basis of variable pay arrangements across the organisation. The Committee does not formally consult with employees on Executive pay, but does regularly seek the views of the Director of Human Resources and takes into account views expressed in dialogue with Glas Members as well as benchmarking and best practice.

DISCRETIONS RETAINED BY THE REMUNERATION COMMITTEE

The Committee will operate the AVPS and LTVPS according to their respective scheme policies and in accordance with the Listing Rules, UK Corporate Governance Code, and IA/ISS Guidelines where appropriate.

The Committee retains discretion, consistent with market practice, in relation to the operation and administration of these schemes. These include, but are not limited to, taking into account significant safety or reputational issues, or significant deterioration of performance. The scheme rules allow for clawback of variable pay from directors, whether before or after awards have vested.

OVERSIGHT OF REMUNERATION POLICIES FOR THE WIDER GROUP

As part of its ongoing review of policies, the Committee takes account of remuneration across the Group as a whole, and the appropriateness of targets, while recognising that the detail and implementation of pay policies for the wider workforce is a matter for the Executive team.

Figure 1 (right) summarises the components of the Executive Directors' remuneration packages in accordance with the Group's Remuneration Policy.

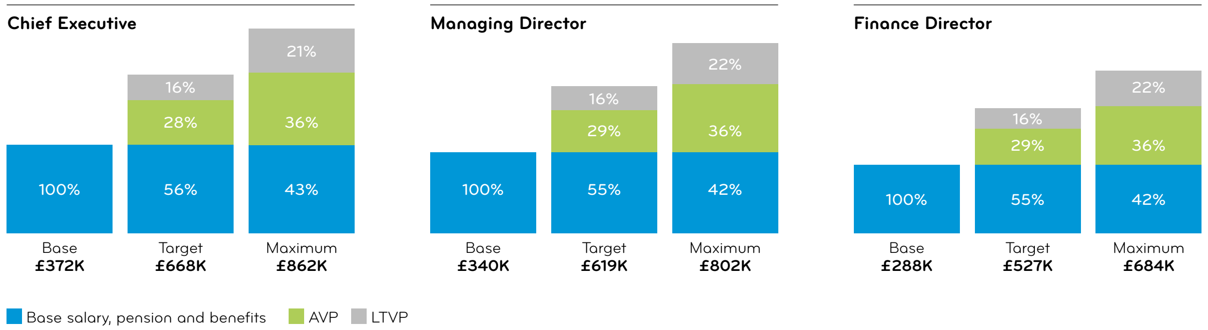
FIGURE 1: COMPONENTS CONSTITUTING THE EXECUTIVE DIRECTORS' REMUNERATION PACKAGES

	Purpose and link to strategy	Operation	Opportunity	Performance metrics
Base salary	To help recruit, retain and motivate high calibre employees	Normally reviewed annually and any increases applied with effect from 1 April. Review reflects: — role, experience and performance — wider economic conditions — increases awarded to the broader workforce — taking periodic account of levels in other utilities in the wider jobs market	Annual increases generally linked to those of the wider workforce, though the Remuneration Committee retains discretion to award increases to individuals above this level where appropriate. Current salaries are disclosed in the Annual Report on Remuneration	None
Benefits	To provide a market competitive benefits package to help recruit and retain Executives Healthcare benefits promote business continuity	Directors are entitled to private health cover and life insurance The Chief Executive and the Managing Director have a historic entitlement to permanent health insurance The Managing Director receives a car allowance of £5,000 with effect from 1 October 2017 Other benefits such as relocation expenses or travel/ accommodation allowances may be offered as appropriate.	Value of benefits is based on the cost to the Group and is not predetermined	None
Pension	To help recruit and retain high calibre employees Discrete post-retirement planning provision	From 1 April, 2017 previous active members of the DCWW Defined Benefit Pension Scheme transferring to the DCWW Group Personal Pension Plan (in line with other employees) receive an employer contribution of up to 24% of salary with the opportunity to opt out and receive a cash alternative allowance equivalent to the employer contribution. For other active members of the DCWW Group Personal Pension Plan the maximum employer contribution to the DCWW Group Personal Pension Plan is 11% providing the employee contributes 6% or more. New Executive Directors are automatically enrolled in the DCWW Group Personal Pension Plan with the opportunity to opt out and receive a cash allowance equivalent to the prevailing Employer contribution, adjusted for NI contributions.	Effective from 1 April 2017, the Chief Executive receives a cash alternative allowance of 21.1% of salary and the Managing Director receives a cash alternative allowance of 15.8% of salary. The value is commensurate with previous payments but delivered through an alternative vehicle.	None
AVPS	To incentivise the annual delivery of stretching targets and personal objectives	AVPS targets reviewed annually by the Committee Targets designed to relate to areas of the business over which the Executive has particular control Outturn is determined by the Remuneration Committee after the year end based on performance against targets and is: — paid as cash; — not pensionable Clawback provisions apply in the following circumstances: — restatement of accounts; — material misrepresentation; and — gross misconduct or reputational damage caused to the Company or Group Company The Committee also retains the discretion to withhold awards in the event of significant issues affecting the safety or the reputation of the company. AVPS awards may be clawed back either prior to the payment of the award for a particular financial year or for a period of six years from the date of payment.	Maximum 100% of salary	Measures well aligned to the Business Plan themes of Customer, Compliance and Cost with additional annual focus and personal targets (See page 76)

1. In approving this Remuneration Policy, authority was given to the Group to honour any commitments entered into with current or former Directors that have been disclosed in previous Remuneration Reports. Details of any payments to former Directors will be set out in the Annual Report on Remuneration as they arise as required under the Remuneration Regulations.

	Purpose and link to strategy	Operation	Opportunity	Performance metrics
LTVPS	To align the long-term interests of the Executive Directors with those of Welsh Water's customers and stakeholders To incentivise achievement of value creation over the long term	Cash awards based on stretching performance targets relating to: — rolling three year relative SIM performance — combined measure of the growth in Reserves and Transfers to the Customer Reserves Clawback provisions apply in the following circumstances: — restatement of accounts — material misrepresentation — gross misconduct or caused reputational damage to the Company or Group Company The Committee also retains the discretion to withhold rewards in the event of significant issues affecting the safety or the reputation of the company. LTVPS awards may be clawed back either prior to the payment of the award for a particular financial year or for a period of six years from the date of payment.	300% of salary over the five year regulatory period to 31 March 2020 (a maximum potential award of 60% per annum).	50% based on relative SIM performance 50% based on customer value generated (see page 77)
Non- Executive Directors' Fees	Provides an appropriate level of fixed fee to recruit and retain individuals with a broad range of experience and skill to support the Board in the delivery of its duties.	The Remuneration Committee determines the fee payable to the Chairman of the Board and, separately, the Executive Directors and the Chairman approve the fee level payable to the Non-Executive Directors. All Directors are paid for expenses incurred in connection with their role on the Board and any taxable benefit implications that may result.	Non-Executive Directors do not receive any fees for chairing Committees The Senior Independent Director is paid more to reflect the breadth of his/her duties.	None
New Executive Director appointments	Base salary levels will be set to reflect the experience of the individual, appropriate market data and internal relativities. If it is considered appropriate to appoint a new Executive Director on a below market salary they may be subject to a series of increases to the desired salary positioning over an appropriate timeframe subject to performance in post. This approach will apply to both internal and external appointments. The policy will be for the new Executive Director to participate in the remuneration structure detailed above. Exceptions to this could be setting different measures or implementing transitional arrangements should an Executive Director join part way through the five year regulatory period. For internal promotees to Executive Director, entitlement to previously accrued AVPS or LTVPS up to the appointment date will be unaffected. Should it be the case that the Remuneration Committee considers it necessary to buy out incentive pay which an individual would forfeit on leaving their current employer, such compensation, where possible, will be structured so that the terms of the buyout mirror the form and structure of the remuneration being replaced.			
Policy for payments to departing executives	The Executive Directors have service contracts that are subject to a 12 month notice period and which do not provide for compensation to be payable in the event of early termination by the Group. At the Group's discretion, an Executive Director may be paid base salary alone in lieu of notice. A significant element of mitigation is built into the contract should the Group choose to exercise its option to make a payment in lieu of notice. When an Executive Director leaves via redundancy and is not required to work his/her notice period, he/she will be entitled to Statutory Redundancy plus 12 months' pay in lieu of notice together with pay in lieu of accrued but untaken holidays. Should an Executive Director resign, he/she will be expected to work their notice period unless an alternative arrangement such as garden leave or a reduced notice period is agreed. In the event that the Group terminates the Executive's employment, the Group will take legal advice and will pay to the Executive only such amount as the Executive is legally entitled to receive. In the event of cessation of employment AVPS and LTVPS awards will be treated in line with the relevant scheme rules which describe the treatment of any payment with reference to 'good' or 'bad' leaver terms. Any vested amount already paid to the Executive prior to the date of cessation of employment may be retained in full by the Executive.			

The graphs below show for each Executive Director:
— the base level of remuneration, which is not dependent upon performance and comprises basic salary, benefits in kind and pension;
— the expected level of remuneration, reflecting a typical level of performance against targets for the AVP and LTVP; and
— the maximum level of remuneration, if all AVP and LTVP performance targets were fully achieved



ANNUAL REPORT ON REMUNERATION

Remuneration Policy for Executive Directors — implementation of the policy

SALARY

Following a review in March 2018 the Remuneration Committee set the base salaries for the Executive Directors for 2018-2019 (effective 1 April 2018) shown in Figure 2. This mirrors the 3% increase awarded to employees on 1 April 2018 in accordance with the five year pay deal agreed with the Group's three recognised trade unions (GMB, UNISON and UNITE) in 2015 and those employees not covered by the Working Together Agreement. Details of Executive Directors' base salaries within Welsh Water and the Water Industry generally were taken into account during negotiations for the wider workforce pay settlement.

FIGURE 2: EXECUTIVE DIRECTORS' BASE SALARIES

	Effective 1 April 2017	Effective 1 October 2017	Effective 1 April 2018
Chris Jones	£297,267	£297,267	£306,186
Peter Perry	£240,220	£280,000	£288,400
Peter Bridgewater	£240,220	£240,220	£247,427

Following the restructure of the Executive team in October 2017, Peter Perry's increase reflects the annual pay review and his new role as Managing Director of the regulated business of Welsh Water.

FEES PAYABLE TO THE CHAIRMAN

The fees payable to the Chairman were reviewed in March 2017 and the Committee resolved that the Chairman's fee should be increased from £212,000 to £215,400 per annum (1.6% rounded up) with effect from 1 April 2017 in line with the wider employee base. A further review took place in March 2018 and the Chairman's fee was further increased to £221,900 per annum (3% rounded up) with effect from 1 April 2018 again in line with the general increase to employees.

FEES PAYABLE TO NON-EXECUTIVE DIRECTORS

In March 2017 the Chairman and Executive Directors resolved that the fees for Non-Executive Directors should be increased from £58,900 to £59,850, with the fee for the Senior Independent Director rising from £69,700, to £70,820 (approximately 1.6% in each case) with effect from 1 April 2017. A further review took place in May 2018 and it was resolved that the fees for Non-Executive Directors should be increased to £61,650, with the fee for the Senior Independent Director rising to £72,950 (approximately 3% in each case) with effect from 1 April 2018. These increases are also in line with employees generally. The total amount of fees payable to Non-Executive Directors in 2017-18 was £600,421 (2016-17: £588,026).

ANNUAL VARIABLE PAY SCHEME (AVPS)

The maximum variable pay that Executive Directors can earn under the AVPS in 2018-19 is unchanged and equates to 100% of base salary. The achievement of variable pay is assessed across five components, consistent with how the AVPS was operated in 2017-18, as illustrated in Figure 3. Note that individual weightings per component have changed as illustrated below.

FIGURE 3A: ANNUAL VARIABLE PAY SCHEME STRUCTURE 2018-2019

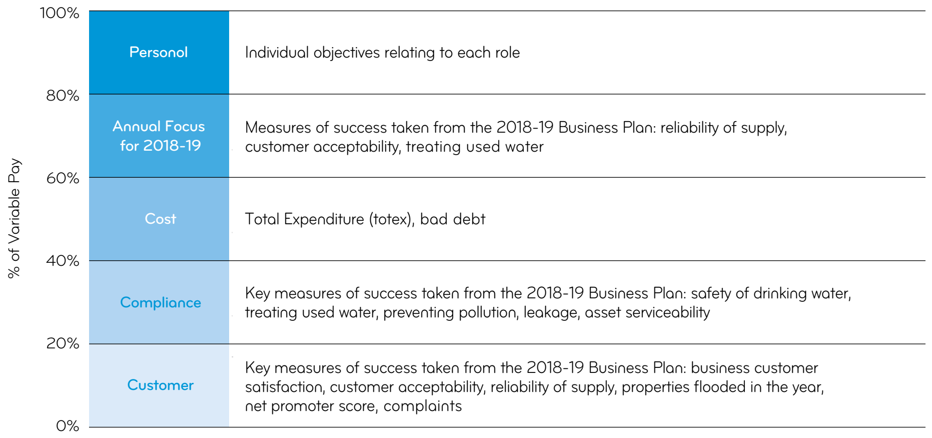


FIGURE 3B: AVPS PERFORMANCE MEASURES

	Customer	Compliance	Cost	Annual Focus	Personal
Performance measures	Key measures of success taken from the 2018-19 Business Plan: business customer satisfaction, customer acceptability, reliability of supply, properties flooded in the year, net promoter score, complaints	Key measures of success taken from the 2018-19 Business Plan: safety of drinking water, treating used water, preventing pollution, leakage, asset serviceability	Key measures of success taken from the 2018-19 Business Plan: Total Company totex, bad debt	Measures of success taken from the 2018-19 Business Plan: Reliability of supply, customer acceptability, treating used water	Individual objectives relating to each role
Rationale for selected measures	Linked to the 2018-2019 business plan	Linked to the 2018-2019 business plan	Linked to the 2018-2019 business plan	Linked to the 2018-2019 business plan	Linked to the 2018-2019 business plan
Performance Period	One year	One year	One year	One year	One year
Performance target	5 measures with total maximum 20% award: – 25% of award payable for achieving threshold performance – 62.5% of award payable for achieving target performance – 100% of award payable for achieving stretch performance	5 measures with total maximum 20% award: – 25% of award payable for achieving threshold performance – 62.5% of award payable for achieving target performance – 100% of award payable for achieving stretch performance	1 measure with maximum 20% award: – 25% of award payable for achieving threshold performance – 75% of award payable for achieving target performance – 100% of award payable for achieving stretch performance	5 measures with total maximum 20% award: – 20% of award payable for achieving threshold performance – 60% of award payable for achieving target performance – 100% of award payable for achieving stretch performance	Variable number of measures with total maximum 20% award

LONG TERM VARIABLE PAY SCHEME (LTVPS)

The objective of the LTVPS is to align the longer term aspects of total remuneration with Company performance over the course of the five year regulatory period ending on 31 March 2020. The awards comprise a cash payment. Under the LTVPS, awards can be made on the basis of performance against the following two discrete measures:

- a Customer Value Award, which combines two financial measures of the increase in Reserves (regulatory capital value less net debt) and Transfers to Customer Reserves (representing amounts available for Customer Distributions) over the regulatory period. The increase in Reserves (as a measure of financial position) and the transfers to the Customer Reserves (as a measure of financial flows), calculated separately but added together, captures the total value generated for customers (returned and retained) by the Group. Ultimately, this is the most important financial objective for the Executive Directors; and
- a Customer Service Award, which is measured by Welsh Water's average ranking in the Ofwat league table for SIM over a rolling three year period. The Customer Service Award is therefore informed by, and rewards, Welsh Water's performance relative to similar companies in the sector. SIM is used for the Customer Service Award and comprises two measures of customer service: a qualitative measure reflecting the results of independent research carried out on behalf of Ofwat to capture customer satisfaction with the service they have received; and a quantitative measure which covers customer complaints and unwanted calls.

The LTVPS performance targets reflect the Board's ambition that Welsh Water should rank alongside the leading companies in the industry on key measures for customer service and long term financial efficiency for the benefit of customers.

The performance targets under each of the LTVPS awards are described more fully in Figure 4.

FIGURE 4: LTVPS PERFORMANCE MEASURES

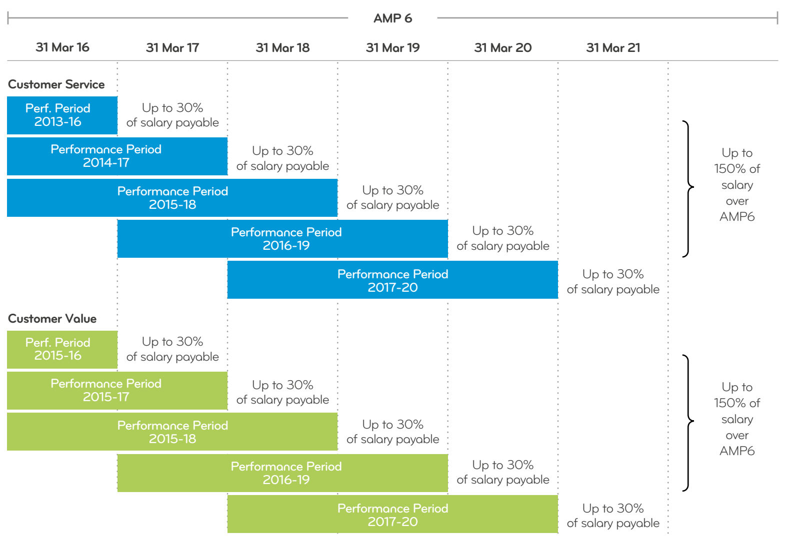
	Customer Service	Customer Value[1]
Performance measures	Measured by reference to Ofwat's SIM measure.	Actual customer value created (increase in reserves and transfers to Customer Reserves) at 31 March 2020 (the end of the AMP6 period) compared to targets.
Rationale for selected measures	Ofwat's SIM measure of important customer experience which is independent, objective and measurable, and allows performance to be compared relative to other water and sewerage companies	This is the strongest financial measure of the total value generated for customers by the Company.
Performance Period	Three financial years immediately prior to the financial year in which an award is made	1 April 2015 to 31 March 2020 – as shown in Figure 5 below
Performance target[2,3]	Out of UK's 10 water and sewerage companies: – 100% of award payable for achieving first position – 75% of award payable for achieving second position – 50% of award payable for achieving third position – 25% of award payable for achieving fourth position – 0% of award payable for a ranking of fifth or below.	Maximum 30% award each year if the value created is in line with the targets which are set each year but set three years in advance: – 100% of award payable for achieving stretch above target – 66% of award payable for achieving target – 0% for performance at or below threshold – Pro rata award payable for performance between these limits For the final two performance periods within AMP6, the Customer Value target for 2018-19 is £173million and for 2019-20 is £189 million.

Footnote to Figure 4

1. The customer value targets may be amended in certain circumstances at the discretion of the Committee. These circumstances include where (i) there are differences between actual inflation and the assumptions originally made; (ii) there are any other significant external factors which the Committee determines to be outside the influence of the Executive Directors.
2. Payment may be deferred at the discretion of the Committee in the event that there is a significant deterioration in performance. Deferral may be for up to two years, or until the shortfall has been remedied, whichever is the earlier.
3. When determining the level of any award the Committee will have regard to the rating of the Group's bonds and may, at its discretion, defer all or part of an award if the Group's bonds have been put on credit watch or downgraded.

The period over which performance is determined and the potential payment dates over the regulatory period are illustrated in schematic Figure 5. Details of payments made under the LTVPS for 2017-18 are set out in figure 6.

FIGURE 5: LTVPS PERFORMANCE PERIOD



WHAT WAS PAID IN 2017-2018 AND LINK BETWEEN PAY AND PERFORMANCE

PAYMENTS MADE TO DIRECTORS IN 2017-2018

Figure 6 sets out the Directors' emoluments in respect of the year ended 31 March 2018 in comparison to year ended 31 March 2017.

FIGURE 6: PAYMENTS AND BENEFITS EARNED BY DIRECTORS IN 2017-2018

	Salary/Fees		Taxable benefits[2]		Other		AVP[4]		LTVPS[5]		Pension Cash Alternative[6]		Total	
	2016/17	2017/18	2016/17	2017/18	2016/17	2017/18	2016/17	2017/18	2016/17	2017/18	2016/17	2017/18	2016/17	2017/18
	£	£	£	£	£	£	£	£	£	£	£	£	£	£
Chris Jones	292,585	297,267	1,068	1,250	-	-	220,609	192,034	114,840	47,563	-	62,723	629,102*	600,837
Peter Bridgewater	236,437	240,220	1,068	1,250	12,000	12,000	174,727	150,378	92,801	38,435	26,008	26,424	543,041	468,707
Peter Perry	236,437	260,110[1]	1,068	1,250	-	2,500	177,091	168,031	92,801	41,618	-	41,097	507,397*	514,606
Robert Ayling	58,048	-	-	-	-	-	-	-	-	-	-	-	58,048	-
Alastair Lyons	165,778	215,392	-	-	-	-	-	-	-	-	-	-	165,778	215,392
Stephen Palmer	58,900	44,882	-	-	-	-	-	-	-	-	-	-	58,900	44,882
Menna Richards	69,700	70,816	-	-	-	-	-	-	-	-	-	-	69,700	70,816
Anna Walker	58,900	59,850	-	-	-	-	-	-	-	-	-	-	58,900	59,850
John Warren	58,900	59,850	-	-	-	-	-	-	-	-	-	-	58,900	59,850
Graham Edwards	58,900	59,850	-	-	-	-	-	-	-	-	-	-	58,900	59,850
Joanne Kenrick	58,900	59,850	-	-	-	-	-	-	-	-	-	-	58,900	59,850
Tom Crick	-	29,925	-	-	-	-	-	-	-	-	-	-	-	29,925
Total	1,353,485	1,398,012	3,204	3,750	12,000	14,500	572,427	510,443	300,442	127,616	26,008	130,244	2,267,566	2,184,565

Notes to table

Changes of Director: Alastair Lyons was appointed to the Board on 1 May 2016 and appointed to the position of Chairman on 8 July 2016. Robert Ayling stood down from the Board on 8 July 2016. Stephen Palmer stood down from the Board on 31 December 2017. Tom Crick was appointed to the Board on 1 October 2017. The figures above are the amounts paid for the period in office.

1. Peter Perry was appointed to Managing Director effective 1 October 2017 with a salary increase to £280,000 increased to £288,400 with effect from 1 April 2018.
2. Taxable benefits relate to private health cover.
3. This represents six months of car allowance at £5,000 per annum as agreed as part of the remuneration package put in place in October 2017.
4. Please see determination of AVPS outcome on page 79. Performance against AVPS targets in 2017-18 resulted in a lower payment than in 2016-17.
5. Please see determination of LTVPS outcome on page 79.
6. Pension contribution for Peter Bridgewater is a cash alternative allowance. Cash alternative payments made in 2016/17 and 2017/18 are shown in Figure 6. Accrued pension benefits for 2017-18 in respect of the (closed) Defined Benefit pension scheme for Chris Jones and Peter Perry are disclosed separately in Figure 8.
7. The highest paid Director in 2017-18 was Chris Jones who received 600,837 (£629,102 in 2016-17). If changes in pensions accruals are included in this calculation, the highest paid director would be Peter Perry who received £721,750 (£636,982 in 2016-17). See Figure 8 for capitalised accrued values of Executive Director pension schemes.

*These figures differ from those in the 2017 Annual Report as they do not include accruals to the capital transfer value of retirement benefits.

DETERMINATION OF 2017-18 AVPS OUTCOME

For 2017-18, the Remuneration Committee measured performance against each target, linked directly to the achievement of the Company's strategy, as follows in the table below. Performance in 2017-18 resulted in an AVPS award of between 62% and 64% compared with an award of between 73.9% and 75.4% for the Executive Directors in 2016-17.

FIGURE 7: AVPS 2017-2018 OUTCOME (AUDITED)

Measure	Weighting	Summary of targets (% of salary)	Result	% of maximum
Customer – Business Customer Satisfaction – Customer Acceptability – Reliability of Supply – Properties Flooded in the Year – Net Promoter Score	20%	Threshold 5% Target 12.5% Stretch 20%	9.2%	46%
Compliance – Safety of Drinking Water – Treated Used Water – Preventing Pollution – Leakage – Asset Serviceability	20%	Threshold 4% Target 12.5% Stretch 20%	13.6%	68%
Cost – Total Company Totex	20%	Threshold 5% Target 15% Stretch 20%	15.5%	77.5%
Annual focus – Reliability of Supply – Customer Acceptability – Bad Debt – Complaints	20%	Threshold 4% Target 12% Stretch 20%	8.3%	41.5%
Personal	20%		16%-18%	80%-90%
Total	100%		62.6% - 64.6%	62.6% - 64.6%

Notes to table

Personal Objectives: The personal objectives (worth up to 20% of base salary) of the Executive Directors were aligned to the delivery of Welsh Water's key strategic objectives and the delivery of the business plan for 2017-18.

- Chris Jones' primary personal objective was to lead the finalisation of the Welsh Water 2050 strategy in consultation with key stakeholders. The Committee assessed that Chris Jones had substantially achieved his personal objectives and the payout awarded was 18% of salary.
- Peter Bridgewater's primary personal objective was to achieve excellent customer service for eligible business retail customers, and to purchase and integrate into the business the food waste business of Kelda in Cardiff. The Committee assessed that Peter had made material progress in achieving his primary personal objective and the payout awarded was 16% of salary.
- Peter Perry's primary personal objectives were to develop a clear costs reduction plan and to progress work on agreeing the National Environment Plan. The Committee assessed that Peter had substantially achieved his primary personal objectives and the payout awarded was 18% of salary.

DETERMINATION OF 2017-18 LTVPS OUTCOME

Welsh Water's SIM rating relative to the SIM rating of the other water and sewerage companies over the three year performance period to 31 March 2018 will not be known until later in the year. At this time, it is estimated to be ranked joint 6th, in which case no award would be payable. The actual award will be determined later in the year when full comparative information is published by Ofwat. The maximum potential is 30% of salary.

For the Customer Value element of the scheme measured from 1 April 2017 to 31 March 2018, a payment of 16% of salary (53.3% of maximum for this element) has been made. This has been based on the Remuneration Committee's determination that total value generated for LTVPS purposes in the year ended 31 March 2018 was £125 million against a target of £129 million (and a stretch of £139 million).

PENSION BENEFITS

For the period 1 April 2017 to 31 March 2017 Chris Jones and Peter Perry were active members of the DCWW Pension Scheme (the 'Scheme') which is a defined benefit pension arrangement.

Pensionable Service stopped accruing with effect from 31 March 2017 however future increases to Pensionable Earnings will be taken into account when calculating benefits. The Scheme also provides life cover of four times Pensionable Salary for death in service, a pension payable in the event of retirement due to ill health and a spouse's pension payable on the death of the member.

Chris Jones and Peter Perry are Lifetime Allowance and/or Annual Allowance Capped Members of the Scheme and where their Scheme benefits exceed HMRC limits additional benefits are provided via an Employer Financed Retirement Benefit Scheme (EFRBS). The Company's obligations under the EFRBS will not be funded, however such obligations constitute liabilities of the Company, payable when they are due.

Following consultation with the recognised Trade Unions in 2014-2015, a decision was made to remove the right to an unreduced pension upon redundancy or selective voluntary severance with effect from 1 April 2015; remove the right to draw a DCWW pension whilst remaining employed; and to close the DCWW Pension Scheme to accrual of Pensionable Service with effect from 31 March 2017.

As compensation, it was agreed that enhanced employer contributions to the Group Personal Pension Plan (GPPP) would be made for those affected by the scheme closure until 31 March 2020.

In April 2016 a cash alternative plan was introduced for senior managers.

The Chief Executive and Managing Director opted to receive a cash alternative allowance with effect from 1 April 2017. The Chief Executive was in a special member benefit category of the EFRBS (building up a pension at a rate of 1/45 of pensionable salary each year compared to the 1/60 of pensionable salary accrued by the wider DCWW Pension Scheme membership).

It was, therefore, agreed by the committee the respective proportionate enhancements would be provided to the Chief Executive and the Managing Director until 31 March 2020.

Effective from 1 April 2017, the Chief Executive receives a cash alternative allowance of 21.1% of salary and the Managing Director receives a cash alternative allowance of 15.8% of salary. The enhanced payments will only be paid until 31 March 2020. Effective from 1 April 2020, the Chief Executive will receive a cash alternative allowance of 12.9% of salary and the Managing Director will receive a cash alternative allowance of 9.7% of salary.

The pension benefits earned by the Directors in the Scheme during the year are shown in Figure 8 which has been audited.

Since his employment began on 1 September 2014, Peter Bridgewater has opted to receive a cash alternative allowance of 11% of salary.

OTHER BENEFITS

Executive Directors have the benefit of private health cover.

Chris Jones and Peter Perry also have permanent health insurance.

FIGURE 8: PENSION BENEFITS

Changes in accrued pensions benefits for the Chief Executive and Managing Director during the year are shown below (audited).

Year ending 31 March 2017

	Normal Retirement Age	Accrued pension at 31 March 2016	Capitalised value of accrued pension at 31 March 2016	Revalued capitalised value of accrued pension at 31 March 2016[1]	Accrued pension at 31 March 2017	Capitalised value of accrued pension at 31 March 2017	Member contributions paid during the year 2017	Pension Input Amount (net of member contributions 2017)[2]
		£	£	£	£	£	£	£
Chris Jones	60	134,978	2,699,562	2,699,562	143,505	2,870,094	26,333	144,199
Peter Perry	60	134,803	2,696,056	2,696,056	142,346	2,848,920	21,279	129,585

Year ending 31 March 2018

	Accrued pension at 31 March 2017	Capitalised value of accrued pension at 31 March 2017	Revalued capitalised value of accrued pension at 31 March 2017[1]	Accrued pension at 31 March 2018	Capitalised value of accrued pension at 31 March 2018	Member contributions paid during the year 2018	Pension Input Amount (net of member contributions) 2018[2]
Chris Jones	143,505	2,870,094	2,898,795	148,824	2,976,480	-	77,685
Peter Perry	142,346	2,846,920	2,875,390	154,855	3,097,100	-	221,710

In accordance with the approach applied for other employees upon closure of the defined benefit pension scheme to future accruals of pensionable service, the pension benefits for Chris Jones and Peter Perry continue to increase in line with increases in their base salary, and these increases are provided for in the Employer Funded Retirement Benefits Scheme. The capitalised value of the accrued entitlement represents the value of the assets that the pension scheme would transfer to another pension provider on transferring the scheme's liability in respect of a director's pension benefits. It does not represent sums payable to a director and therefore cannot be added meaningfully to annual remuneration.

Benefit notes:
1. Increased by the actual CPI growth figure at the previous September – 0% for the 2017 disclosure period and 1% for 2018.
2. Based on the capitalised value of accrued pension at the year-end, less the revalued capitalised value of accrued pension at the start of the year.
- The accrued pensions include previous Pensionable Service completed in Hyder Water and United Utilities Pension Schemes.
- The accrued pension figures include both the standard entitlements within the Scheme (which are restricted in accordance with HMRC limits) and the top-up benefits which are payable under the EFRBS.

COMPARISON OF OVERALL PAY AND PERFORMANCE

Figures 9 and 10 show how our pay awards have compared with performance and compares the total pay of our Chief Executive to year on year growth in Customer Reserves (i.e. financial reserves being Regulatory Capital Value less net debt) over the previous eight years.

FIGURE 9: CUSTOMER RESERVES OVER EIGHT YEARS TO 31 MARCH 2018

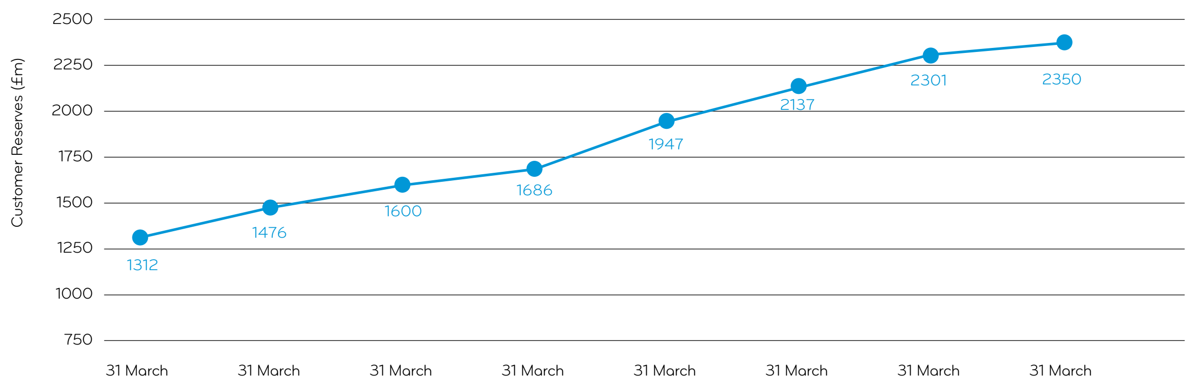


FIGURE 10: OVERALL PAY AND PERFORMANCE

	2011	2012	2013	2014	2015	2016	2017	2018
	£	£	£	£	£	£	£	£
Total remuneration for Chief Executive (Chris Jones)	-	-	-	741,569	973,688	746,430	629,102	600,837
Total remuneration for Managing Director (Nigel Annett)	665,965	677,770	590,210	709,890	-	-	-	
AVPS award (Chris Jones)	-	-	-	51.1%	79.4%	70.3%	75.4%	64.6%
AVPS award (Nigel Annett)	76.3%	77.6%	60.6%	49.9%	-	-	-	-
LTVPS for AMP6	-	-	-	-	-	39%	39.25%	16%
LTVPS for AMP5	25.0%	40.0%	50.0%	78.6%	90.6%	-	-	-

For 2014 full financial figures have been provided for Chris Jones and Nigel Annett and do not solely relate to the period as Chief Executive/Managing Director. LTVPS for AMP5 shows as a percentage of maximum rather than a percentage of salary awarded.

RELATIVE IMPORTANCE OF SPEND ON PAY

The Remuneration Committee considers the cost of remuneration in relation to other factors such as company performance. Figure 11 sets out the change in total expenditure, total employee remuneration costs and Customer Reserves in 2018 compared to 2017.

FIGURE 11: RELATIVE IMPORTANCE OF SPEND ON PAY

	2017	2018	Change	
	£m	£m	£m	%
Total expenditure[1]	868.5	980.7	112.2	12.9%
Employee remuneration costs	134.4	151.2	16.8	12.5%
Customer Reserves[2]	2301	2350	49	2.1%
Executive Director remuneration costs	1.68	1.58	(0.10)	(5.7%)

1. Operational expenditure, capital expenditure and financing costs.
2. Regulatory capital value less net debt. Customer equity metric included to enable comparisons with shareholder owned companies.

ALIGNMENT OF PAY ACROSS THE GROUP

The Committee recognises that pay should be fair throughout the Group. Therefore, in making decisions in relation to the structure of Executive pay, the Committee takes into account the pay structures throughout the business, in particular noting that the annual variable pay "colleague or employee bonus" is aligned to the same measures as the Executive annual variable pay scheme.

PERCENTAGE INCREASE IN THE REMUNERATION OF THE CHIEF EXECUTIVE OFFICER

Figure 12 shows the movement in salary, for Chris Jones as Chief Executive Officer between the current and previous financial year compared with that of the average employee. The Committee looks to ensure that the approach to fair pay is implemented in practice throughout the Group.

RATIO OF CHIEF EXECUTIVE TO AVERAGE EMPLOYEE SALARY

This ratio uses the figure for total CEO salary included in Figure 6. See the notes to this table for information as to how this has been calculated for 2017-18. If the capital transfer value in Figure 8 is included, the ratio would be 15:1.

FIGURE 12: PERCENTAGE CHANGE IN CEO'S SALARY COMPARED WITH OTHER EMPLOYEES

	Chief Executive % change from 2016-17	Employees % change from 2016-17
Salary	3%	3%

FIGURE 13: RATIO OF CHIEF EXECUTIVE TO AVERAGE EMPLOYEE SALARY

Chief Executive Remuneration: Average Employee Remuneration
13.5:1 (2016-17: 15.5:1)

DETAILS OF DIRECTORS' SERVICE CONTRACTS AND LETTERS OF APPOINTMENT

Dates of the service contracts of the Executive Directors and letters of appointment of the Non-Executive Directors in place at 31 March 2018 are as follows:

Chris Jones	4 July 2013
Peter Perry	17 September 2013
Peter Bridgewater	1 September 2014
Menna Richards	22 November 2010
Anna Walker	3 March 2011
John Warren	3 May 2012
Graham Edwards	1 October 2013
Joanne Kenrick	1 November 2015
Alastair Lyons	1 May 2016
Tom Crick	1 October 2017

Copies of the service contracts are available from the Company Secretary. For more information on the roles and responsibilities of the Board of Directors, please see page 57.

The Board considers that all the members of the Remuneration Committee are independent and, in the case of Alastair Lyons, that he was considered to be independent on his appointment as Chairman of the Company.

The Chief Executive and the Director of Human Resources attend meetings of the Remuneration Committee by invitation (except where their own remuneration is discussed). The Remuneration Committee was convened on six occasions in 2017-18.

From April – July 2017, the Remuneration Committee received independent advice from New Bridge Street (NBS), a trading name of Aon Hewitt Limited (an Aon plc company). The fees paid to NBS for this period totalled £15,906. For the remainder of 2017-18, the Committee received independent advice from Mercer, who were appointed with effect from July 2017 for a period of up to five years, following a competitive tender process. The fees payable to Mercer for the period 2017-18 totalled £52,340. Both NBS and Mercer are considered by the Committee to be independent, and are signatories to the Remuneration Consultants Group Code of Conduct and any advice given is governed by the Code.

DIRECTORS' REPORT

FINANCIAL PERFORMANCE

The Group is in a strong financial position as at 31 March 2018: gearing remains low at 57% and we have retained our sector-leading credit ratings.

REVENUE

Glas Cymru's turnover in the year to 31 March 2018 rose slightly to £757 million (2017: £744 million): a modest increase of 2.0% reflecting Ofwat's PR14 Final Determination pricing adjustment and increased consumption has been partially offset by reduced revenues due to a higher number of customers benefiting from affordability tariffs.

OPERATIONAL ITEMS

Glas Cymru incurred total operational costs (excluding infrastructure renewals expenditure on maintaining our underground pipe network and depreciation) of £319 million (2017: £313 million).

A number of specific cost increases (employment costs, energy prices and costs relating to the period of severe weather in March 2018) have been partially offset by the lower cost of renegotiated IT contracts, lower business rates following reductions in rateable values and refunds.

All water and sewerage companies use a lot of power, particularly for water treatment and pumping processes. The undulating topography across Wales makes this a particular challenge for us. Power costs during 2017-18 were £43 million (2017: £41 million).

There remains significant uncertainty over future energy costs, and we have forward purchased a proportion of the estimated power requirements of the business for the two years to March 2020.

Water and sewerage companies are not permitted to disconnect supplies to non-paying domestic customers, and despite a focus on other means of recovery, cash collection has continued to be challenging. The high priority and increased focus on debt recovery in the Retail business has resulted in further collections improvements during the year, and as a consequence the bad debt charge for the year has fallen, for the third year in a row, to £22 million (2017: £23 million). We are targeting customers who won't pay their bills, as opposed to those who can't pay, and the reduction comes principally from securing charging orders over property owned by customers, with some 4,000 orders secured over nearly £9 million of our customers' debt as at 31 March 2018.

FINANCING COSTS

Net interest payable of £172 million (excluding accounting gains or losses on derivatives noted below) was £31 million higher than the previous year primarily as a result of higher Retail Prices Index inflation.

Glas Cymru has a number of derivative swap contracts which fix or inflation-link the cost of debt which were entered into when the company was highly geared. While these are effective commercial hedges, they do not qualify for hedge accounting under IAS 39. Changes in market values create volatility in the income statement and fair value gains in 2017-18 amounted to £80 million (2017: losses of £63 million). There is, however, no impact on cash flows: the Group intends to hold its remaining swaps to the maturity of the underlying debt and, over the life of the swaps, such losses will revert to zero.

TAXATION

The Group continues to invest heavily in capital expenditure for the benefit of our customers. The tax relief for this capital expenditure and the interest we pay to fund it have the effect of delaying corporation tax payments to future periods.

A tax credit of £0.4m has been generated from the surrender of tax losses relating to our investment in energy efficient capital expenditure under a government-approved scheme. The company has also claimed a tax credit of £1.4m under the government's R&D Expenditure Credit (RDEC) initiative, which has been included within operating expenditure at note 3. The RDEC tax credit is taxable and the corresponding tax charge of £0.3m is included within current taxes at note 5.

The total tax credit in the income statement was £2.6m (2017: £28.9m credit). The tax credit for the year ended 31 March 2017 benefitted from a deferred tax credit of £12.4m resulting from the corporation tax rate used to calculate deferred taxes falling from 18% to 17% from 1 April 2020. As the Government has not announced any further changes to corporation tax rates, there is no deferred tax credit in the current year from corporation tax rate reductions.

There was a small tax credit of £0.1m relating to prior periods. If this is excluded from the total tax credit of £2.6m then the effective rate for the year is 16.9% (2017: 16.7%) which is broadly in line with the standard rate of corporation tax (19%). A reconciliation is provided at note 5.

LOSS BEFORE TAX

The consolidated income statement shows a loss before taxation of £15 million (2017: loss of £99 million) which takes into account the inflation and fair value movements as discussed above. Operating profit has fallen from £105m last year to £75m; infrastructure renewals expenditure has increased by £16 million in line with our record level of capital investment in year three of the five year investment programme. In addition, depreciation is £20 million higher than the prior year principally due to the revaluation of fixed assets.

OUR GROUP TAX STRATEGY

OUR APPROACH TO RISK MANAGEMENT AND GOVERNANCE ARRANGEMENTS

Our Finance and Commercial Director has overall responsibility for tax governance and strategy with oversight from the Board and the Audit Committee.

Our tax strategy is supported by a detailed internal Group Tax Policy, together with a framework of internal systems and controls which govern the commercial operations of Glas Cymru Holdings and its subsidiaries (the Group). Our Head of Tax is responsible for the day-to-day application of the tax strategy and the management of the Group's tax affairs. Our Head of Tax works closely with the Finance and Commercial Director. All material tax issues, risks and developments are regularly communicated to the Audit Committee.

Our tax team comprises a small group of professionals with extensive experience of tax in the water sector. This expertise is supplemented by the use of reputable external advisers where required.

OUR APPROACH TO TAX PLANNING AND TAX RISK

All of our group companies are UK tax resident and subject to UK corporation tax on their profits.

Our focus is on compliance; ensuring that all taxes are correctly calculated, accurately reported and paid when due.

We do not engage in artificial arrangements with no commercial purpose, or transactions which are directed at exploiting tax legislation in order to reduce the tax we pay. We comply with the spirit of the law as well as the letter of the law.

Tax risks are held within the Group's risk register and are updated regularly.

Our key tax risks principally arise from business developments and changes to tax legislation which may result in unforeseen tax implications. Where possible we seek to mitigate tax risk so that residual risk is minimal.

Our tax team is involved in all significant business developments enabling a full assessment of the tax implications to be made.

We seek input from reputable external advisers where the tax implications are still unclear. In cases where residual uncertainty remains we liaise with HMRC to gain clarity.

Our tax team participates in a number of water industry tax forums. The team receives regular technical updates from our professional advisers and from our periodic meetings with HMRC.

This ensures that the team is kept informed of all relevant developments in tax law, enabling them to develop appropriate systems and controls to address legislative changes.

We actively contribute to the UK tax policy making process by participating in Government consultations.

OUR RELATIONSHIP WITH HMRC

We are committed to an open, transparent relationship with HMRC. Our policy is to fully disclose any issues or errors as they arise, and seek to resolve them as soon as practicable.

We meet HMRC biannually to formally discuss our business plans and developments, together with relevant changes to tax legislation.

The Group has been classified as low risk by HMRC from the inception of the Business Risk Review process in 2009. This is due for review in March 2019.

TAX RELIEFS AND INCENTIVES

Our Group has no shareholders and is run solely for the benefit of our customers. We therefore seek to utilise available tax reliefs and incentives put in place by the Government in order to maximise funds available to benefit our customers.

The Group invests heavily in capital expenditure, for example treatment works and our network of pipes and pumping stations, to continually improve the service we provide to our customers. We are therefore able to take advantage of tax reliefs which aim to stimulate this type of investment. A significant proportion of this capital expenditure can be deducted in calculating the Group's taxable profit. We are also able to deduct interest costs incurred to fund this capital investment. This effectively delays corporation tax payments to future periods. Our customers therefore also benefit from cheaper bills.

The Government's Research & Development (R&D) Expenditure Credit regime incentivises companies to increase their investment in R&D. The Group invests heavily in R&D and claims tax credits under this regime.

TRANSPARENCY

We understand the value of insightful financial reporting to our customers, investors and other stakeholders. Taxation is an area which can be difficult to understand. We therefore seek to give a clear and balanced view of our tax affairs. See pages 114-115.

CONTRIBUTION

The Group is subject to a range of taxes and duties, including corporation tax, business rates, environmental taxes, employment taxes, National Insurance, VAT, fuel duty and licences. The Group thus makes a significant contribution to public finances, as well as employing over 3,000 people and playing an important role in the regional economy.

OTHER DISCLOSURES

PENSION FUNDING

The statement of comprehensive income reports a defined benefit pension scheme actuarial gain of £12 million (2017: loss of £43 million) and the balance sheet liability as at 31 March 2018 was £80 million (2017: £95 million).

This valuation is on an IAS 19 basis for accounting purposes and is not consistent with the actuarial valuation of the scheme for funding purposes. The latest such valuation of the scheme, as at 31 March 2016, projected a deficit of £46 million, recoverable by payments of £7 million per annum until 2019 and then £3 million per annum until 2030. Exposure to any significant additional future liabilities is mitigated by the closure of most sections of the scheme with effect from 1 April 2017.

GOING CONCERN

The Directors are satisfied that the business has adequate resources to continue in business for the foreseeable future. Accordingly, the financial statements for the year ended 31 March 2018 have been prepared on the going concern basis.

DIVIDEND POLICY — APPOINTED BUSINESS (DŴR CYMRU CYFYNGEDIG)

In March 2016 the Glas Board approved a Dividend Policy to enable up to £100m of funds to be paid intra-Group, outside the regulatory ringfence, in order to enable the funding of commercial projects. During 2017-18, a dividend of £30m has been paid up to Glas Cymru Holdings for onward distribution via intra-Group loan to the commercial subsidiaries of Welsh Water Holdings Limited. £21.6m of this dividend to Glas Cymru Holdings was loaned to Welsh Water Holdings for the purchase of the food waste business of Kelda in Cardiff (Welsh Water Organic Energy Limited) in December 2017. (see page 39).

RETURN OF VALUE "DIVIDEND" TO CUSTOMERS

Our corporate structure ensures that all surpluses are applied for the benefit of customers. Since 2001, Glas Cymru has applied £353m in total for the benefit of customers. These distributions abide by the restrictions which would apply to payment of dividends in a shareholder-owned structure. Accordingly, Return of Value in 2017-18 was set at £34m in total. This ensured that the gearing target could be maintained, at just below 60% in 2020, to preserve a strong credit rating and financial resilience for the longer-term benefit of customers. It takes account of known and expected costs and also of the Group's pension funding position (including commitments to contribute to deficit payments). For further details of how these Return of Value distributions will be applied in respect of 2017-18, please see page 15.

CAPITAL INVESTMENT

Glas Cymru's strong financial position has been built up over the last 17 years, and provides a stable base from which it can respond positively to the challenges of economic uncertainty and drive forward its continuing large capital programme. Glas Cymru works with an alliance of partners to deliver the capital investment programme at the best value for money for customers. Total capital expenditure during the year (including infrastructure renewals expenditure) was £431 million (2017: £366 million). This is our highest ever level of investment and in line with our planned profiling of the AMP6 Capital Programme, including accelerated investment in our Zonal Studies programme.

We invested around £1.5 billion over the five year period from 2010 to 2015 in our AMP5 investment programme which brought sustained improvements in customer service, drinking water quality and the environment.

The Group plans to invest at least a further £1.7 billion over the course of the current five year regulatory period (AMP6, 2015-2020), our largest ever investment programme.

We are currently finalising our investment plans for AMP7 which will run from 2020 to 2025, prior to submission to our regulator, Ofwat, as part of the five-yearly price review process which will set allowed levels of customer bills for the next regulatory period.

CREDIT RATING AND INTEREST RATE MANAGEMENT

Glas Cymru has the strongest credit ratings in the water sector, reflecting the Group's high level of creditworthiness. The ratings of the Group's Class A and B debt at 31 March 2018 were A/A2/A from Standard & Poor's (S&P), Moody's and Fitch Ratings respectively.

As at 31 March 2018, approximately 65% of gross debt was index-linked via bonds and derivatives (2017: 65%), with the remainder at fixed interest rates. The expected maturity of the outstanding fixed-rate and index linked bonds ranges from 2021 to 2057, with not more than 20% falling due in any two-year period, in accordance with our refinancing policy.

GEARING POLICY

Glas Cymru's gearing to RCV policy is to target gearing at or around 60% and interest cover ratios commensurate with maintaining our sector leading 'A' grade credit ratings. This should help us to maintain our low risk profile giving the Group access to low cost financing throughout AMP6 and beyond in order to keep down funding costs for customers.

LIQUIDITY AND FINANCIAL RESERVES

Glas Cymru aims to offer a secure, low risk investment to investors. By building and maintaining a strong financial position, we intend to keep our borrowing costs low, enabling us to finance future investment efficiently.

During the year to March 2018, the group drew down a £60m loan facility with KfW Bank (18 May 2017) and on 17 January 2018 we announced a benchmark-sized GBP Class B bond transaction. The bond proceeds of £300 million were settled on 24 January 2018 with a maturity date of 31 March 2036 and a fixed coupon of 2.5%.

On Glas Cymru's acquisition of Welsh Water in May 2001, gearing (net debt/ Regulatory Capital Value) stood at 93%. Since then, the financial position has improved steadily. Gearing to RCV has fallen to 57% by 31 March 2018 and 'customer reserves' (RCV less net debt) were £2.4 billion. As at 31 March 2018, the Group had available total liquidity of £703 million, including cash balances of £283 million.

We have funding in place through to the end of the current regulatory period in March 2020 and have a further £170 million of undrawn revolving credit facilities.

EVENTS AFTER THE FINANCIAL YEAR END

There have been no post balance sheet events.

CORPORATE SOCIAL RESPONSIBILITY — OUR WIDER IMPACT

As one of the biggest employers in Wales and serving 3.1 million people across our supply area in Wales and England, we are acutely aware of our responsibility to our employees and to the wider community. We have set out details of the additional work we do in the communities and rural areas that we serve in our Impact Report. Please see our Impact report on our website **dwrcymru.com**.

This summarises the impact that we have on the world around us, from a customer, community and colleague perspective. It provides a review of our activity over the past 12 months, showcasing what we are doing to help realise our vision to earn the trust of our customers. Some of the areas where we have a wider impact are detailed below:

SUPPORTING OUR COLLEAGUES AND SUPPLY CHAIN

We are working closely with both colleagues and our supply chain to ensure that the key principles underpinning are essential policies are rolled out and understood as part of the values that apply in everything we do for customers.

Occupational Health and Safety

We are committed to high standards of occupational health and safety. During 2017-18 we have seen a reduction in the rate of HSE RIDDOR reportable incidents (RIR) and we have had the lowest RIR and All Injury Rates (AIR) for over 10 years. More information on our health and safety strategy and performance is provided in our 2017 Occupational Health and Safety Report which is available on **dwrcymru.com**

Health and Well-Being

During the first quarter of 2018 our Health, Safety & Wellbeing team led a campaign on mental health issues, and colleagues participated in a number of activities and started productive conversations as result of our participation in Time to Talk Day, which we hope will continue throughout the year. The team shared resources and information for those who needed help with, or wanted to know more about specific mental health conditions. We've also been working alongside mental health charity Mind Cymru to help us stay focused on reducing the stigma surrounding mental health issues in the long term, and to help us ensure that we do all we can to support colleagues in need of assistance.

Human Rights

We are committed to respecting human rights in relation to colleagues and our supply chain. Our Code of Conduct was relaunched in March 2018. This explicitly encourages colleagues to "speak up" if anything doesn't seem right to them, in order to reinforce our culture of "doing the right thing" and individual accountability.

The Code is supported by a number of Group policies, as well as associated procedures and guidance, including:

Anti-Bullying and Harassment

We respect human dignity and the rights of individuals. Our Group policy articulates how colleagues should behave towards each other. During 2018 the Executive Team and some senior managers undertook unconscious bias training to reinforce our commitment to a culture of inclusivity and respect.

Safeguarding

We are committed to ensuring that colleagues who work with children and vulnerable adults are properly trained for this and this year we have developed our policy in this area to support this.

Whistleblowing

A healthy culture where individuals feel able to speak out about anything that causes them concern is an important part of the "third line of defence" of our compliance model. This year we have communicated the availability of our external helpline which provides an additional confidential and secure means to enable our colleagues to raise concerns about conduct which is contrary to our values. We are fully committed to protecting any employee who reports a breach or suspected breach of the Code of Conduct or raises any other public interest disclosure.

Modern Slavery Act 2015

We are committed to meeting the aims of the Modern Slavery Act 2015. We strongly oppose slavery, human trafficking and child labour and we are working to raise awareness across the business and in our supply chains and any part of our business. To be trusted to do the right thing is one of our core values. We would never knowingly engage with suppliers or contractors involved in slavery or human trafficking. Our Anti-Slavery Policy sets out the Group's commitment to acting ethically and with integrity in our supply chain arrangements. As part of our procurement process, any potential contractor or supplier will be required to confirm that they comply with the Modern Slavery Act and, if appointed, we require that they flow down the requirements we place on them to any sub-contractors they use to provide their services to us. Our terms and conditions will include contractual provisions relating to compliance with the Modern Slavery Act. We are implementing these new provisions in all new agreements, upon renewal of key agreements and upon issue of purchase orders. We have written to our existing key suppliers to remind them of the requirements of the Act and our policy in this area. Our Human Resources team maintains recruitment polices to protect against slavery and human trafficking in our own operations and we are working towards meeting the Welsh Government's 12 commitments in its Code of Practice on Ethical Employment in supply chains. Further details and our anti-slavery statement can be found on the following link: **dwrcymru.com/Company-Statements**.

Anti-Bribery & Corruption and Anti-Fraud
Our Group policy make clear that we will not tolerate any acts of fraud, dishonesty, bribery, corruption, theft of assets or improper disclosure of confidential information. The Group treats these issues very seriously and expects all occurrences to be reported immediately. This is reinforced by our strict policy on Hospitality and Gifts from suppliers which is regularly monitored and enforced. The Audit Committee carries out an annual review of our systems of internal controls as part of our ongoing efforts to prevent bribery and corruption in our business and our supply chain.

Conflicts of Interest
We require our employees to perform their duties honestly and to avoid conflict between any personal financial or commercial interests and their responsibilities to Welsh Water.

Competition Law Compliance
Welsh Water is entirely supportive of open and fair competition and committed to adhering strictly to all competition laws.

Supplier Payment Policy
During the year our Group Finance team has worked to improve our payment terms for all suppliers. Where suppliers comply with the terms and conditions of their appointment, including the provision of a compliant invoice with relevant supporting documentation, our policy is that payment should be processed within 30 days of the date receipt of the invoice. We are working to improve our performance against these clear policy objectives and monthly updates are being provided to the Executive Team.

SUPPORTING OUR CUSTOMERS AND COMMUNITIES

Access and Recreation
We are the custodian of approximately 40,000 hectares (99,000 acres) of land that is rich in scenery and biodiversity. This enables us to provide excellent opportunities for public recreation, with around a million visitors a year visiting one of our 17 major reservoir sites where we provide a range of sporting, recreational and leisure facilities. We also have established Visitor and Activity Centres at our Llandegfedd (Gwent), Brenig (Denbighshire), Llys y Fran (Pembrokeshire) and Elan Valley (Powys) sites. For more information on our contribution to public access and tourism please see our Impact report on our website **dwrcymru.com**.

Biodiversity
From December 2019, under the Environment (Wales) Act 2016 we will report on a three-yearly basis on compliance with our duty to strengthen biodiversity and ecosystems across our supply area.

WELSH WATER COMMUNITY FUND

During the year, we launched the Welsh Water Community Fund to support those communities where our operational investment may have caused disruption.

The Community Fund is a chance for communities to boost fundraising efforts for good causes in their area. In making awards from this fund, our Community Fund committee gives priority to areas where Welsh Water has been carrying out works that may have impacted the local community. The scheme has been a huge success to date, with over 200 applications received since its launch in September 2017. For further information please see our Impact report on our website **dwrcymru.com**.

Our Impact Report


Staff at Marie Curie Hospice in Penarth


Whitehead Graig United Under 6s football team, in Newport

GLAS CYMRU HOLDINGS CYFYNGEDIG | ANNUAL REPORT & ACCOUNTS

DATA PROTECTION AND INFORMATION SECURITY

We have undertaken a Group-wide compliance and awareness programme during the year in preparation for the General Data Protection Regulation which came into force in May 2018. This aimed to reinforce awareness across the Group that the personal data we hold belongs to individual customers or colleagues and highlighted the importance of protecting the privacy of the individual in relation to the personal information we hold We have established key principles that govern the collection, use and handling of personal information and provides individuals with important rights. Our Privacy Notice is available on our website **dwrcymru.com/privacy**.

Our policies also reinforce the role of individuals in keeping information more generally secure and accurate. The Audit Committee regularly reviews our approach to Cyber-Security risk. During the year, we attained Cyber-Essentials plus certification and we are working towards ISO 27001 accreditation for our information security controls.

INNOVATION

Our innovation portfolio continues to grow with 300 ideas and proposals now assessed through our iLab process since April 2015. We have completed some 78 projects, winning over 8 innovation awards in the process and worked with 121 partner organisations investing some £5.9m in 2017/18 on innovation on behalf of our customers. This work continues to drive efficiencies, reducing our environmental footprint, and improving our health and safety in particular. As well as investing in driving innovative change, we continue to work closely with our Independent Environmental Advisory Panel (made up of regulators, academics and environmental stakeholders) who advise the business on the science and research we undertake. The Panel continues to assists us to tap into the expertise and resources available in such bodies and to build our relationships with them, so as to leverage funding and expertise into our science and research work. More generally, we continue to drive elements of the national research agenda through our strategic relationship with the Natural Environmental Research Council (NERC) and by participation in water industry research initiatives, most notably through membership of the UK Water Industry Research partnership (UKWIR) which manages and coordinates the research interests of UK water companies.

POLITICAL DONATIONS

It is Board policy not to make donations to political parties or to incur political expenditure. During the year a payment of £33,750 was made to Citizens Advice, to fund a debt advisor providing advice to our customers in Rhondda Cynon Taff, and a payment of £18,000 was made to Step Change to support the work the charity does in providing debt advice to our customers. We are disclosing these payments as both organisations also campaign for government policy change, including on debt issues, however, the funding provided was earmarked for specific debt advice. Other than this, no donations or payments were made which are required to be disclosed under section 366 of the Companies Act 2006.

GREENHOUSE GASES

We try to minimise our effect on the environment in everything we do including seeking to reduce our emissions of greenhouse gases. We measure this through the calculation of our operational carbon emissions. In previous years, these emissions have been dominated by grid supplied energy (electricity and gas). However, in 2017/18 we began a new electricity supply arrangement with Orsted (formally known as DONG) which ensures all our electricity is from green renewable sources (backed by the Renewable Energy Guarantees of Origin (REGO) scheme). This change means that our electricity supply can be declared as having zero carbon emissions, save for some emissions associated with the transmission and distribution of the electricity, a reduction of 134ktCO2e (at 2017/18 emissions factors).

In 2017-18 our operational carbon emissions fell 71% to 62ktCO2e (2016/17: 212 ktCO2e). Had we not changed electricity supply contract the carbon emissions would have fallen by 7% to 197ktCO2e mainly due to the ongoing reduction in the carbon content of electricity as UK coal based generation has now largely been replaced by gas. Our underlying electricity consumption rose to 466 GWh (2016/17: 451 GWh) partially offset by our renewable energy generation rising to 98GWh (2016: 87 GWh) with increases in hydro generation (to 42 from 37 GWh) and our first full year of wind energy generation (6 GWh). Carbon emissions from other parts of the business, mainly from sludge processing and transport use as well as our fuel consumption, rose from previous year by 4ktCO2e.

EMPLOYEES

At 31 March 2018, the Group had 3435 employees. We know that our success is fundamentally dependent upon our highly committed and motivated people and we are committed to developing our people to meet the challenges of operating our business in the future and to encouraging a diverse workforce that fully reflects the communities that we serve.

Improving the diversity of our workforce
We do not discriminate against applicants or employees on the basis of age, disability, gender reassignment, marital or civil partner status, pregnancy or maternity, race, colour, nationality, ethnic or national origin, religion or belief, sex or sexual orientation ("protected characteristics" in accordance with the Equality Act 2010) or any other personal characteristic. If an employee is disabled or becomes disabled, we consider any reasonable adjustments that would help overcome or minimise the disability. It is the policy of the Group that the training, career development and promotion of a disabled person should, as far as possible, be identical to that of a person who does not suffer from a disability.

WELSH LANGUAGE SCHEME

We have adopted the principle that in the context of conducting our public business in Wales we will treat the Welsh and English languages on a basis of equality.

We welcome dealing with customers and other stakeholders in Welsh or English and aim to provide an effective standard of service in both languages.

Our Welsh Language Scheme is an approved scheme under the provisions of the Welsh Language Act 1993. We are working closely with the Welsh Language Commissioner's office to prepare for the implementation of the provisions of the Welsh Language (Wales) Measure 2011. This report is available in Welsh.

WATERAID

As befits our operating model, we do not engage in corporate sponsorship but we continue to provide support to WaterAid. For further details please see our Social Impact Report.

PERSONS OF SIGNIFICANT CONTROL

We maintain a Register of People with Significant Control to comply with the requirements of the Small Business, Enterprise and Employment Act 2015 (2015 Act). The company has identified registrable relevant legal entities (RRLEs) within our Group structure.

DIRECTORS' STATEMENT

The Directors consider that the Annual Report and Accounts, the consolidated financial statements of Glas Cymru, taken as a whole, are fair, balanced and understandable and provide the information necessary for stakeholders to assess the Group's performance, business model and strategy.

In order to arrive at this position, the Board was assisted in the following ways:

- the Annual Report was drafted by senior management and overall co-ordination overseen by the General Counsel and Company Secretary to ensure consistency
- reviews of drafts were undertaken by members of the Executive team and a verification process involving the Group's auditors has been undertaken
- the final draft was reviewed by the Audit Committee prior to review and approval by the Board, and submission to Members.

The Board has prepared a Strategic Report which provides a summary of the development and performance of the Group's business in the year ended 31 March 2018 and covers likely future developments. Glas Cymru Holdings Cyfyngedig (Company number 09917809) is a company limited by guarantee, incorporated in England and Wales. Our registered office is Pentwyn Road, Nelson, CF46 6LY.

This Annual Report and Accounts document consolidates the activity and results of Glas Cymru Holdings Cyfyngedig ('Glas Cymru') and its subsidiaries. More information on Principal Activities can be found on page 15.

ANNUAL PERFORMANCE REPORT

Condition F of the Instrument of Appointment, under which Welsh Water operates, requires that we publish additional financial information as an 'appointed business'. A copy of this information is published on our website.

ANNUAL GENERAL MEETING

The 2018 AGM will be held on Friday 6 July 2018 at The Marriot Hotel, Swansea. The business of the AGM includes:

- receiving the Directors' Report;
- receiving the Financial Statements for the year ended 31 March 2018;
- approval of the Remuneration Report for the year ended 31 March 2018 and approval of the extension of the Remuneration Policy for a further two-year period;
- the re-election of all Directors;
- a resolution to authorise the Group to make donations to EU political organisations and to incur EU political expenditure up to defined limits;
- resolutions to appoint the auditors and to authorise the Audit Committee to fix their fees.

These resolutions are all matters of ordinary business. There is no special business.

Further information in respect of all resolutions is provided in the Notice of 2018 AGM sent to the Members of Glas Cymru Holdings Cyfyngedig.

EDUCATION

Investing in education and engaging with the communities we serve so that the next generation understand the part they have to play in helping us achieve our vision is a key part of our service. We have four Discovery Centres (Elan Valley near Rhayader, Cilfynydd near Pontypridd, Cog Moors near Dinas Powys and Brenig in the Denbighshire moors), visited by over 14,000 children every year. They offer a range of fun, practical activities and programmes so children and families can experience the world of water at first hand.

To extend the reach of our education provision, we also have an outreach programme where our teachers regularly visit primary and secondary schools to deliver workshops on the behavioural change campaigns we undertake involving water efficiency (Love Dŵr) and pollution (Let's Stop the Block). Around 41,000 pupils a year benefit from this programme.

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ANNUAL REPORT AND THE FINANCIAL STATEMENTS

The Directors are responsible for preparing the Annual Report and the Group and parent Company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and parent Company financial statements for each financial year. Under that law they have elected to prepare the Group and parent Company financial statements in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the 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 Group and parent Company and of their profit or loss for that period. In preparing each of the Group and parent Company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- assess the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the parent Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

The Directors have prepared a Corporate Governance Statement as if the company were required to comply with the Listing Rules and the Disclosure Guidance and Transparency Rules of the Financial Conduct Authority in relation to those matters.

Under applicable law and regulations, the Directors are also responsible for preparing a Strategic Report and a Directors' Report that complies with that law and those regulations.

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

We consider the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy.

By order of the Board

N Williams.

Nicola Williams
General Counsel and Company Secretary
7 June 2018

AUDITORS

KPMG act as auditors to Glas Cymru for the accounts for the year ended 31 March 2018. As part of the audit process we have confirmed that, as far as each Director is aware, there is no relevant audit information of which the auditors are unaware, that they have taken any necessary steps to be made aware of any such information and to establish that the Group's auditors are aware of that information. We confirm that to the best of our knowledge:

- The financial statements, prepared in accordance with the applicable accounting standards, give a true and fair view of the Group's performance.
- The strategic report includes a fair review of the performance of the business, its risks and strategy for the future.
- The Directors consider the annual report to be fair, balanced and understandable.

In considering the development of the system of controls, the management team reviews the materiality and the relative cost benefit associated with each identified significant risk. The internal control systems are designed to provide reasonable assurance against misstatements, loss or failure. The process to review the effectiveness of internal control includes discussion with management on significant risk issues and a review of plans for, and results from, internal and external audit.

The Audit Committee reports the results of its review to the Board which then draws its collective conclusion on the effectiveness of the system of internal controls. In fulfilling this responsibility, the Board considers regular reports from the Audit Committee, Quality and Environment Committee and from management, and relies on its routine monitoring of key performance indicators and monthly reports of financial and operational performance. Taken as a whole, these processes enable the Board to review the effectiveness of the internal control system during the course of the year.

FINANCE

FINANCIAL REVIEW AND RESULTS

Independent Auditor's report to the Directors of Glas Cymru Holdings Cyfyngedig

1. Our opinion is unmodified

We have audited the financial statements of Glas Cymru Holdings Cyfyngedig ("the Company") for the year ended 31 March 2018 which comprise the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity, consolidated balance sheet, parent company balance sheet, parent company statement of changes in reserves, consolidated cash flow statement, parent company cash flow statement and the related notes, including the accounting policies in note 1.

In our opinion:

the financial statements give a true and fair view of the state of the Group's and of the parent Company's affairs as at 31 March 2018 and of the Group's loss for the year then ended;

- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- the parent Company financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below.

We have fulfilled our ethical responsibilities under, and are independent of the Group in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to listed entities. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion.

Overview		
Materiality: group financial statements as a whole	£11.0m (2017:£10.0m) 0.17% (2017: 0.17%) of Total Assets	
Coverage	100% (2017:100%) of group loss (2016: loss) before tax	
Risks of material misstatement vs 2017		
Recurring risks	Measured income accrual	◀▶
	Fixed assets	◀▶
	Provision for trade receivables	◀▶
	Group pension obligation	◀▶
Parent company risks	Parent company's investment	◀▶

2. Key audit matters: our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In arriving at our audit opinion above, the key audit matters, in decreasing order of audit significance, were as follows (unchanged from 2017):

	The risk	Our response
Measured income accrual (£70.8 million; 2017: £68.8 million) Refer to page 65 (Audit Committee Report), page 106 (accounting policy) and page 110 (financial disclosures).	**Subjective estimate** The calculation of unbilled metered income includes an estimate of the value of water supplied to metered customers between the last meter reading and the end of the financial year. This estimate is based on the number of customers on meters, the price per unit of water, and where appropriate, historical billing information adjusted for changes in external factors such as weather, which could be inaccurately stated.	**Our procedures included:** Test of detail: we re-calculated the accrual for a sample of customers and we critically assessed the arithmetic workings of the calculation, agreeing tariffs to the scheme of charges and average usage to recent bills and bank statements. Expectation vs outcome: An expectation of measured income including the related accrual was formed, taking into account key drivers of the balance, including customer numbers, price changes based on the group's published scheme of charges and if appropriate any external factors such as weather, and compared with actual measured income recognised; and Assessing transparency: we also assessed the adequacy of the group's disclosures in respect of the degree of estimation involved in arriving at the income accrual.

	The risk	Our response
Classification of costs between operating expenditure and capital expenditure Additions: (£349.4 million; 2017: £308.5 million) Refer to page 65 (Audit Committee Report), page 107 (accounting policy) and page 116 (financial disclosures).	**Accounting treatment** The group incurs a high level of expenditure on PPE ("property, plant and equipment"), including repair and maintenance, and enhancement costs. There is a high degree of judgement involved in determining whether costs, both initial and subsequent expenditure, including employee and other internal expenditure, on both infrastructure and non-infrastructure assets, meet the relevant criteria for capitalisation and therefore are included in the carrying value of PPE, or alternatively should be expensed immediately. Due to the risk that such costs could be inappropriately capitalised, based on the judgements made by directors or the third party engaged by the group in respect of non-infrastructure and infrastructure expenditure respectively, this is one of the key focus areas in our audit.	**Our procedures included:** Accounting analysis: we assessed the group's capitalisation policy against the requirements of the accounting standards; Control design: we tested controls over a sample of capital projects throughout the financial year to check that the controls operated as described with regards to the classification of expenditure as either capital or operating being in line with policy and subject to review and authorisation from the appropriate level within the business hierarchy; Sector experience: on a sample basis, we challenged the judgements made by both the group (non-infrastructure expenditure) and the independent third party engaged by the group (infrastructure expenditure) over the level of capitalisation based on the group's accounting policies, knowledge of the sector and underlying nature of the projects; and Assessing expert credentials: we assessed the third party experts competence to perform this role by considering their sector experience with reference to previous industry projects and their approach taken.
Provision for trade receivables Trade receivables: (£556.7 million; 2017: £556.6 million) Provision for impairment of receivables: (£83.8 million; 2017: £95.8 million) Refer to page 108 (accounting policy) and page 119 (financial disclosures).	**Subjective estimate** The provision for doubtful debts is a significant risk area as a result of the complexity of the calculation, its subjective nature, and because of its size and the fact that any change in the balance sheet provision would directly impact profit. The provision methodology is based upon forecasting future failure rates using past experience of historical cash collections, and any other external impacting factors such as changes in customer behaviour, to estimate the proportion of the year end receivables that the group expects to receive.	**Our procedures included:** Methodology implementation: assessed whether the calculation incorporated the appropriate information, risks and data including historical cash collections and write offs, to estimate the level of irrecoverable debt, based on our knowledge of the group and the industry; Sector experience: challenged the directors' assumptions over the cash collection profiles based on our knowledge of the market, historical trends, operational performance, historic write offs, economic trends and pricing levels; Sensitivity Analysis: performed sensitivity analysis on the assumptions made, in particular future cash collection rates, and compared the impact on the level of the provision; Assessing transparency: assessed the adequacy of the group's disclosures about the degree of estimation uncertainty involved in calculating the provision.
Group pension obligation Present value of obligation: (£474.1 million; 2017: £497.3 million) Refer to page 65 (Audit Committee Report), page 108 (accounting policy) and page 129 (financial disclosures).	**Subjective valuation** Small changes in the assumptions and estimates used to value the group's pension obligation such as discount rates, inflation price, mortality rates would have a significant effect on the group's net pension deficit.	**Our procedures included:** Benchmarking assumptions: with the support of our own actuarial specialists, we challenged the key assumptions applied, being the discount rate, inflation price and mortality rates. Assessing transparency: we have also considered the adequacy of the group's disclosures in respect of the sensitivity of the deficit to changes in key assumptions
Valuation of parent company's investment in subsidiaries Investment in subsidiaries: (£3,398.1 million; 2017: £3,228.6 million) Refer to page 65 (Audit Committee Report), page 107 (accounting policy) and page 118 (financial disclosures).	**Forecast-based valuation** The valuation of the parent company's investments are stated at fair value. The fair value is calculated using a discounted cash flow model. The judgements related to the future cash flow forecasts and the use of the company's regulatory capital value (RCV) as its terminal value are subjective which results in this balance being a key area of focus for our audit.	**Our procedures included:** Methodology implementation: assessed whether the calculation incorporated the appropriate inputs including reasonable forecasts and assumptions about the future prospects of the subsidiaries; Historical comparisons: we evaluated the director's forecasting ability by comparing previous forecasts to actual results; Benchmarking assumptions: we assessed the valuation method based on recent prices paid for similar companies within the industry, with a focus on the multiple of OFWAT reported RCV used; and Our sector experience: we asses the discount rate used in the discounted cash flow with reference to the WACC used for similar companies.

We continue to perform procedures over derivative financial instruments. However, following a reduction in our assessment of the complexity of the valuations and no audit misstatements in the prior year, we have not assessed this as one of the most significant risks in our current year audit and, therefore, it is not separately identified in our report this year.

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

Materiality for the group financial statements as a whole was set at £11.0 million, determined with reference to a benchmark of group's total assets, of which it represents 0.17% (2017: 0.17%).

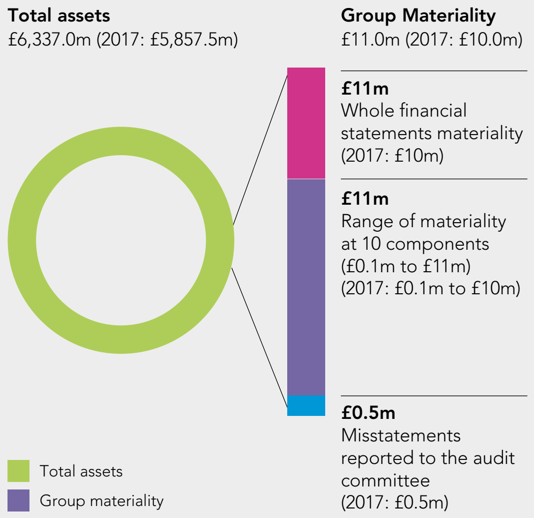
Materiality for the parent company financial statements as a whole was set at £5.9 million (2017: £5.5 million), determined with reference to a benchmark of parent company total assets, of which it represents 0.17% (2017: 0.17%).

We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £0.5 million, in addition to other identified misstatements that warranted reporting on qualitative grounds.

Of the group's 10 (2017: 8) reporting components, we subjected 10 (2017: 8) to full scope audits for group purposes.

The components within the scope of our work accounted for the percentages illustrated opposite.

The Group team approved the component materialities, which ranged from £0.1m to £11m, having regard to the mix of size and risk profile of the Group across the components. The work on all of the components was performed by the Group team.



4. We have nothing to report on going concern

We are required to report to you if we have anything material to add or draw attention to in relation to the directors' statement in note 1 to the financial statements on the use of the going concern basis of accounting with no material uncertainties that may cast significant doubt over the Group and Company's use of that basis for a period of at least twelve months from the date of approval of the financial statements. We have nothing to report in these respects.

5. We have nothing to report on the other information in the Annual Report

The directors are responsible for the other information presented in the Annual Report together with the financial statements. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except as explicitly stated below, any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work we have not identified material misstatements in the other information.

Strategic report and directors' report

Based solely on our work on the other information:

- we have not identified material misstatements in the strategic report and the directors' report;
- in our opinion the information given in those reports for the financial year is consistent with the financial statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

Directors Remuneration Report

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 to be audited has been properly prepared in accordance with the Companies Act 2006, as if those requirements applied to the company.

Disclosures of principal risks and longer-term viability

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

- the directors' confirmation within the long-term viability statement (page 48) that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency and liquidity;
- the Principal Risks disclosures describing these risks and explaining how they are being managed and mitigated; and
- the directors' explanation in the long-term viability statement of how they have assessed the prospects of the Group, over what period they have done so and why they considered that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

Corporate governance disclosures

We are required to report to you if:

- we have identified material inconsistencies between the knowledge we acquired during our financial statements 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 Group's position and performance, business model and strategy; or
- the section of the annual report describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.

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 Guidance 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 part of the Corporate Governance Statement relating to the Company's compliance with the eleven provisions of the UK Corporate Governance Code specified for our review.

We have nothing to report in these respects.

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

Under the Companies Act 2006, we are required to report to you if, in our opinion:

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

We have nothing to report in these respects.

7. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 93, the Directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities

8. The purpose of our audit work and to whom we owe our responsibilities

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

James Ledward
Senior Statutory Auditor

for and on behalf of KPMG LLP
Statutory Auditor Chartered Accountants

3 Assembly Square, Britannia Quay,
Cardiff CF10 4AX
7 June 2018

FINANCIAL STATEMENTS

CONSOLIDATED INCOME STATEMENT FOR THE YEAR ENDED 31 MARCH 2018

Continuing activities	Note	2018 £m	2017 £m
Revenue		**756.7**	743.6
Operating costs:			
Operational expenditure	3	**(319.0)**	(312.6)
Infrastructure renewals expenditure		**(86.0)**	(69.7)
Depreciation and amortisation	3	**(276.3)**	(256.6)
		(681.3)	(638.9)
Operating profit		**75.4**	104.7
Profit on disposal of fixed assets		**1.8**	-
Profit before interest		**77.2**	104.7
Financing expenses:			
Finance costs payable and similar expenses	4a	**(175.9)**	(144.2)
Finance income receivable		**3.9**	3.6
Fair value gains/(losses) on derivative financial instruments	4b	**80.0**	(63.0)
		(92.0)	(203.6)
Loss before taxation		**(14.8)**	(98.9)
Taxation	5	**2.6**	28.9
Loss for the year		**(12.2)**	(70.0)

The company has elected to take the exemption under section 408 of the Companies Act 2006 not to present the parent company's income statement. The profit of the parent company for the year to 31 March 2018 was £0.3m (15 month period to 31 March 2017: £30.2m).

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 MARCH 2018

	Note	2018 £m	2017 £m
Loss for the year		**(12.2)**	(70.0)
Items that will not be reclassified to profit or loss			
Actuarial gain/(loss) recognised in the pension scheme	21	**12.2**	(43.3)
Related deferred tax	6	**(2.8)**	5.9
Revaluation of property, plant and equipment	7	**158.1**	156.8
Related deferred tax	6	**(26.9)**	(15.3)
Total items that will not be reclassified to profit or loss		**140.6**	104.1
Total comprehensive income for the year		**128.4**	34.1

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 MARCH 2018

	Revaluation reserve £m	Retained earnings £m	Total £m
At 1 April 2016	977.9	103.9	**1,081.8**
Loss for the year	-	(70.0)	**(70.0)**
Actuarial loss net of tax	-	(37.4)	**(37.4)**
Revaluation net of tax	141.5	-	**141.5**
Transfer to retained earnings	(50.3)	50.3	**-**
At 31 March 2017	1,069.1	46.8	**1,115.9**
Loss for the year	-	(12.2)	**(12.2)**
Actuarial gain net of tax	-	9.4	**9.4**
Revaluation net of tax	131.2	-	**131.2**
Transfer to retained earnings	(57.5)	57.5	**-**
At 31 March 2018	1,142.8	101.5	**1,244.3**

CONSOLIDATED BALANCE SHEET AS AT 31 MARCH 2018

	Note	2018 £m	2017 £m
Assets			
Non-current assets			
Property, plant and equipment	8	**5,312.1**	5,065.2
Intangible assets	9	**146.3**	119.5
Trade and other receivables	11	**0.9**	-
Financial assets:			
- derivative financial instruments	15	**1.9**	2.2
		5,461.2	5,186.9
Current assets			
Trade and other receivables	11	**577.7**	563.2
Inventories		**3.2**	2.8
Financial assets:			
- derivative financial instruments	15	**6.4**	4.0
Cash and cash equivalents	12	**288.5**	100.6
		875.8	670.6
Total assets		**6,337.0**	5,857.5
Liabilities			
Current liabilities			
Trade and other payables	13	**(564.1)**	(556.5)
Financial liabilities:			
- borrowings	14	**(41.5)**	(39.3)
- derivative financial instruments	15	**(29.2)**	(35.2)
Provisions for other liabilities and charges	17	**(2.4)**	(1.2)
		(637.2)	(632.2)
Net current assets		**238.6**	38.4
Non-current liabilities			
Trade and other payables	13	**(233.9)**	(204.6)
Financial liabilities:			
- borrowings	14	**(3,317.3)**	(2,938.8)
- derivative financial instruments	15	**(376.2)**	(448.0)
Post employment benefits	21	**(80.4)**	(95.2)
Provisions for other liabilities and charges	17	**(6.5)**	(9.6)
		(4,014.3)	(3,696.2)
Net assets before deferred tax		**1,685.5**	1,529.1
Deferred tax - net	6	**(441.2)**	(413.2)
Net assets		**1,244.3**	1,115.9
Equity			
Revaluation reserve		**1,142.8**	1,069.1
Retained earnings		**101.5**	46.8
Reserves		**1,244.3**	1,115.9

The financial statements on pages 101 to 133 were approved by the Board of Directors on 7 June 2018 and were signed on its behalf by:

C A Jones
Chief Executive

P J Bridgewater
Finance and Commercial Director

PARENT COMPANY BALANCE SHEET AS AT 31 MARCH 2018

	Note	2018 £m	2017 £m
Assets			
Non-current assets			
Intercompany loan		21.6	-
Investment in subsidiaries	10	3,398.1	3,228.6
		3,419.7	3,228.6
Current assets			
Cash and cash equivalents	12	8.6	30.1
Intercompany interest receivable		0.2	-
		8.8	30.1
Net assets		3,428.5	3,258.7
Reserves			
Retained earnings		30.5	30.2
Revaluation reserve		3,398.0	3,228.5
Total reserves		3,428.5	3,258.7

PARENT COMPANY STATEMENT OF CHANGES IN RESERVES FOR THE YEAR ENDED 31 MARCH 2018

	Revaluation Reserve £m	Retained earnings £m	Total £m
Balance at incorporation	-	-	-
Profit for the period	-	30.2	30.2
Revaluation	3,228.5	-	3,228.5
Balance at 31 March 2017	3,228.5	30.2	3,258.7
Profit for the year	-	0.3	0.3
Revaluation	169.5	-	169.5
Balance at 31 March 2018	3,398.0	30.5	3,428.5

The parent company was incorporated on 15 December 2015. It acts as a holding company and does not trade.

The financial statements on pages 104 to 105 were approved by the Board of Directors on 7 June 2018 and were signed on its behalf by:

C A Jones
Chief Executive

P J Bridgewater
Finance and Commercial Director

CONSOLIDATED CASH FLOW STATEMENT FOR THE YEAR ENDED 31 MARCH 2018

	Note	2018 £m	2017 £m
Cash flows from operating activities			
Cash generated from operations	18a	347.5	336.9
Interest paid	18b	(132.9)	(124.6)
Income tax received		0.4	1.1
Net cash generated from operating activities		215.0	213.4
Cash flows from investing activities			
Acquisition of subsidiaries		(0.5)	-
Interest received		3.8	3.8
Purchase of property, plant and equipment		(302.6)	(237.7)
Purchase of intangible assets		(48.5)	(33.5)
Proceeds from sale of plant and equipment		2.5	-
Grants and contributions received		11.4	16.1
Net cash outflow from investing activities		(333.9)	(251.3)
Net cash flow before financing activities		(118.9)	(37.9)
Cash flows from financing activities			
Long term loans received		60.0	70.0
Bond issue		300.0	-
Bond issue costs		(3.5)	-
Repayment of borrowings		(18.2)	(36.9)
Term loan repayments		(21.6)	(20.3)
Finance lease principal payments		(9.8)	(9.3)
Other loan repayments		(0.1)	(0.1)
Net cash flow from financing activities		306.8	3.4
Increase/(decrease) in cash and cash equivalents	19b	187.9	(34.5)
Cash and cash equivalents at 1 April		100.6	135.1
Cash and cash equivalents at 31 March	12	288.5	100.6

PARENT COMPANY CASH FLOW STATEMENT FOR THE YEAR ENDED 31 MARCH 2018

	2018 £m	15 months to 31 March 2017 £m
Cash flow from investing activities		
Dividend received	-	30.2
Investment in subsidiary company	-	(0.1)
Interest received	0.1	-
Long-term loan to subsidiary	(21.6)	-
Net cash flow from investing activity	(21.5)	30.1
Net (decrease)/increase in cash and cash equivalents	(21.5)	30.1
Cash and cash equivalents at beginning of period	30.1	-
Cash and cash equivalents at 31 March	8.6	30.1

1. ACCOUNTING POLICIES, FINANCING RISK MANAGEMENT AND ACCOUNTING ESTIMATES

Accounting policies for the year ended 31 March 2018
Glas Cymru Holdings Cyfyngedig ('the Company') is a private company incorporated, domiciled and registered in Wales in the UK. The registered number is 09917809 and the registered address is Pentwyn Road, Nelson, Treharris, CF46 6LY.

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been applied consistently to both of the years presented.

Basis of preparation
Glas Cymru Holdings Cyfyngedig was incorporated on 15 December 2015 and is limited by guarantee. The Members of Glas Cymru Anghyfyngedig transferred to be Members of Glas Cymru Holdings Cyfyngedig. Accordingly Glas Cymru Holdings Cyfyngedig is now the ultimate parent company of the Glas Group.

The consolidated financial statements of Glas Cymru Holdings Cyfyngedig and the parent company financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adapted by the EU ("Adopted IFRSs"). The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of fixed assets, financial assets and financial liabilities (including derivative financial instruments) at fair value through profit or loss.

The preparation of financial statements to conform with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas including a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed on page 110.

Basis of consolidation
The consolidated financial statements include the financial statements of the Company and its subsidiaries. Intra-group transactions and profits are eliminated on consolidation.

The consolidated financial statements incorporate the results of business combinations using the acquisition method. In the consolidated balance sheet, the acquiree's identifiable assets, liabilities and contingent liabilities are initially recognised at their fair values at the acquisition date. The results of acquired operations are included in the consolidated statement of comprehensive income from the date on which control is obtained. They are de-consolidated from the date on which control ceases.

The parent company financial statements present information about the company as a separate entity and not about its group.

Going concern
As described in the financing risk management section the Group meets its day to day working capital requirement through its bank facilities. The Group's forecasts and projections, taking account of reasonably possible changes in trading performance, show that it should be able to operate within its current facilities. After making enquires, the Directors have a reasonable expectation that the Group has adequate resources to continue operational existence for the foreseeable future. The Group therefore continues to adopt the going concern basis in preparing its financial statements.

Changes in accounting policies and disclosures
The following Adopted IFRSs have been issued but have not been applied in these financial statements.

— IFRS 9 Financial Instruments (effective date 1 January 2018). The standard introduces a revised model for the classification and measurement of financial instruments, a revised approach to hedge accounting and an "expected loss" impairment model. The Group has reviewed the likely impact of adoption and recognises that, while the impairment model is in line with its current approach, additional disclosures will be required to show historical experience and the extent of forward-looking factors. Work is ongoing to assess the potential extent of future expected losses in relation to the measured income accrual but following an initial assessment, the impact is not expected to be material.

— IFRS 15 Revenue from Contracts with Customers (effective date 1 January 2018). The standard deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. Revenue is recognised when a customer obtains control of a good or service and thus has the ability to direct the use and obtain the benefits from the good or service. The standard replaces IAS 18 'Revenue' and IAS 11 'Construction Contracts', and related interpretations. The Group has undertaken an assessment of the impact of IFRS 15 and while the basis of the period of deferral may differ for infrastructure charges, the Directors do not anticipate that it will result in any material change to revenue recognised.

— IFRS 16 Leases (effective date 1 January 2019). The standard revises the treatment of leases in financial statements and largely eliminates the accounting distinction between operating and finance leases. The Group has only a small number of low value, short term operating leases and therefore the impact of adoption is not expected to be material.

Revenue recognition
Revenue represents the income receivable in the ordinary course of business for services provided, excluding value added tax. Where services have been provided but for which no invoice has been raised at the year-end an estimate of the value is included in revenue (see the 'Critical accounting estimates' section for further details). Revenue recognised reflects the value of services provided to customers in the year. Where customers have made payments in advance as at the year end, this is recognised as deferred income.

Segment reporting
Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segment, has been identified as the steering committee that makes strategic decisions.

Investments
The parent company's investments comprise equity holdings in wholly-owned subsidiaries, as set out in note 10. These are stated at fair value with any resultant gain or loss being recognised directly in equity, in the revaluation reserve.

The fair value has been calculated using a discounted cash flow technique, alongside considering observable market transactions, with reference to the Group's weighted average cost of capital.

Property, plant and equipment
The economic value of the Group's water and sewerage business is derived from the Regulatory Capital Value (RCV) set by Ofwat during its five yearly price reviews. The Group considers that a fair value approach to valuing its assets better reflects the underlying value of the assets than historical cost accounting which understates the assets' current value in use.

As at 31 March 2018 the total value of tangible and intangible fixed assets has been revalued to the Group's 'shadow RCV', being the 31 March 2018 RCV published by Ofwat in its PR14 Final determination as adjusted for the impact of any totex over/underspend and the Outcome Delivery Incentive rewards/penalties. The classes of asset impacted are infrastructure assets and operational structures.

The carrying value of assets is reviewed for impairment if circumstances dictate that the carrying value may not be recoverable; asset lives and residual values are reviewed annually.

Property, plant and equipment comprise:

a) Infrastructure assets (being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls); and

b) Other assets (including properties, overground operational structures and equipment, and fixtures and fittings).

Infrastructure assets
Infrastructure assets comprise principally impounding reservoirs and a network of underground water and wastewater systems. For accounting purposes, the water system is segmented into components representing categories of asset classes with similar characteristics and asset lives. The wastewater system is segmented into components representing geographical operating areas, reflecting the way the Group operates its wastewater activities.

Expenditure on infrastructure assets relating to increases in capacity, enhancements or material replacements of network components is treated as additions, which are included at cost. Expenditure incurred in repairing and maintaining the operating capability of individual infrastructure components, 'infrastructure renewals expenditure', is expensed in the year in which the expenditure is incurred.

The depreciation charge for infrastructure assets is determined for each component of the network and is based on each component's cost, estimated residual value and the expected remaining average useful life. The useful average economic lives of the infrastructure components range principally from 60 to 150 years.

Other assets
Other assets are depreciated on a straight-line basis over their estimated useful economic lives, which are as follows:

Freehold buildings	60 years
Operational structures	5 – 80 years
Plant, equipment and computer hardware	3 – 40 years

Assets in the course of construction are not depreciated until commissioned. Land is not depreciated.

Borrowing costs
Borrowing costs are general and specific borrowing costs directly attributable to the acquisition, construction and production of qualifying assets. Qualifying assets are assets that necessarily take a substantial period of time to get ready for their intended use or sale.

Intangible assets
Intangible assets, which comprise principally computer software, systems developments and research and development, are included at cost less accumulated amortisation. Cost reflects purchase price together with any expenditure directly attributable to bringing the asset into use, including directly attributable internal costs. Research expenditure is recognised as an expense as incurred. Costs incurred on development projects are recognised as intangible assets when the relevant recognition criteria are met (as per IAS 38).

The carrying values of intangible assets are reviewed for impairment if circumstances indicate they may not be recoverable. Intangible assets are amortised on a straight line basis over their estimated useful economic lives, which range between 3 and 20 years. These asset lives are reviewed annually.

Leased assets
Certain assets are financed by leasing arrangements which transfer substantially all the risks and rewards of ownership of an asset to the lessee (finance leases). These assets are capitalised and included in 'property, plant and equipment' with the corresponding liability to the lessor included within 'financial liabilities – borrowings'. Leasing payments consist of a capital element and a finance charge; the capital element reduces the obligation to the lessor and the finance charge is recognised over the period of the lease based on its implicit rate so as to give a constant rate of interest on the remaining balance of the liability.

All other leases are regarded as operating leases. Rental costs arising under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

Grants and customer contributions
Grants and customer contributions in respect of expenditure on property, plant and equipment have been offset against these assets.

Grants in respect of revenue expenditure are credited to the income statement over the same period as the related expenditure is incurred.

Capital expenditure programme incentive payments
The Group's agreements with its construction partners involved in delivering capital expenditure programmes incorporate incentive bonuses payable after completion of the programmes. The cost of property, plant and equipment additions includes an accrual for incentive bonuses earned to date, relating to projects substantially completed at the year-end, where the likelihood of making the incentive payment is considered probable. Amounts recoverable from contract partners relating to targets not being achieved are recognised only on completed projects.

Trade receivables
Trade receivables are recognised initially at fair value and measured subsequently at amortised cost less provision for impairment. They are first assessed individually for impairment, or collectively where the receivables are not significant individually. Where there is no objective evidence of impairment for an individual receivable, it is included in a group of receivables with similar credit risk characteristics and these are assessed collectively for impairment based on their ageing. Movements in the provision for impairment are recorded in the income statement.

Cash and cash equivalents
Cash and cash equivalents include highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of change in value. Such investments are normally those with less than three months' maturity from the date of acquisition and typically include cash in hand and deposits with banks or other financial institutions.

Pension costs
1) Defined benefit scheme
The Group operates a defined benefit scheme, the DCWW Pension Scheme, which was closed to future accrual from 1 April 2017 for all members except for 18 ESPS section members. The scheme is funded by employer contributions as well as employee contributions from the remaining active members. Contribution rates are based on the advice of a professionally qualified actuary and actuarial valuations of the scheme are carried out at least every three years.

The liability recognised in the balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets. The defined benefit obligation is calculated annually by an independent actuary using the projected unit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligation. In countries where there is no deep market in such bonds, the market rates on government bonds are used.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise.

Past-service costs are recognised immediately in the income statement.

2) Defined contribution scheme
The Group operates a defined contribution scheme, the DCWW Group Personal Pension Plan, which all employees are eligible to join. Obligations for contributions to the scheme are recognised as an expense in the income statement in the period in which they arise.

Financial liabilities
Debt is measured initially at fair value, being net proceeds after deduction of directly attributable issue costs, with subsequent measurement at amortised cost. Debt issue costs are recognised in the income statement over the expected term of such instruments at a constant rate on the carrying amount.

Trade payables are obligations to pay for goods and services acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year, or in the normal operating cycle of the business.

Derivative instruments utilised by the Group are interest rate swaps, inflation swaps and power hedges. Derivative instruments are used for hedging purposes to alter the risk profile of existing underlying exposures within the Group.

Derivatives are recognised initially and subsequently re-measured at fair value. During the year to 31 March 2018, none of the Group's derivatives qualified for hedge accounting under IAS 39 (2017: none). These instruments are carried at fair value with changes in fair value being recognised immediately in the income statement.

Deferred taxation
Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax has been recognised in relation to rolled over gains except for where reinvestment has been made in certain operational assets which the group plans to use until the end of their useful economic life. The group anticipates that these assets will then be scrapped for negligible proceeds, or proceeds less than their tax base, and therefore no chargeable gain is expected to arise in the future.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised.

Provisions
Provisions for restructuring costs and uninsured losses are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been estimated reliably. Restructuring provisions comprise employee severance and pension fund top-up costs. Where the Group receives claims that are either not covered by insurance or where there is an element of the claim for which insurance cover is not available, a provision is made for the expected future liabilities. Provisions are not recognised for future operating losses.

Where there is a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligation is small.

Taxation
Current taxation is corporation tax in the United Kingdom based on the taxable profit for the period and is provided at amounts expected to be paid or recovered using tax rates and laws that have been enacted or substantively enacted at the balance sheet date.

FINANCING RISK MANAGEMENT OBJECTIVES AND POLICIES

Treasury activities are managed within a formal set of treasury policies and objectives, which is reviewed regularly and approved by the Board. The policies specifically prohibit any transactions of a speculative nature and the use of complex financial instruments. Certain detailed policies for managing interest rate, currency and inflation risk and that for managing liquidity risk are approved by the Board and may be changed only with the consent of Dŵr Cymru Cyfyngedig's Security Trustee. The risk is mitigated further by limiting exposure to any one counterparty. The Group uses financial instruments to raise finance and manage operational risk; these instruments principally include listed bonds, finance leases, bank loan facilities and derivatives.

Credit risk
The Group has a prudent policy for investing cash and short term bank deposits set by the bond documentation within the Common Terms Agreement. Deposits can be placed with our Account Bank for overnight risk only or for up to one year with counterparties that have a minimum short-term rating of A1/P1/F1 from Standard & Poor's, Moody's and Fitch Ratings respectively. Deposits of over one year should be placed with counterparties that have a minimum long-term rating of AA-/Aa3/AA-.

In practice, in the current economic environment the Group has adopted a more prudent approach to cash management and timed deposits are placed for a maximum of 35 days with banks subject to minimum long-term rating criteria of A-/A3/A-. Bond and commercial paper purchases of up to one year can be placed with certain AAA-rated supranationals only. The maximum cash investment with a single counterparty was £73m (2017: £69m).

Interest rate risk
The Group hedges at least 85% of its total outstanding financial liabilities, including finance leases, into either index-linked or fixed rate obligations. For this purpose floating rate interest liabilities are hedged through a combination of derivative instruments and cash balances. The regulatory framework under which revenues and the regulatory asset value are indexed also exposes the Group to inflation risk. Therefore, subject to market constraints and Board approval, the Group may seek to raise new debt through index-linked instruments or enter into appropriate hedging transactions.

The Group analyses its interest rate exposure on a dynamic basis. Various scenarios are simulated taking into consideration refinancing, renewal of existing positions, alternative financing and hedging. Of total borrowings of £3,359m as at 31 March 2018 (2017: £2,978m) none related to floating rate debt (2017: none). The Group therefore considers overall interest rate exposure at the balance sheet date to be minimal.

As at 31 March 2018, 100% (2017: 100%) of the Group's gross debt was at fixed or index-linked ('RPI') rates of interest after taking into account interest rate and RPI swaps. The hedges established to manage interest rate risks are economic in nature, but do not satisfy the specific requirements of IAS 39 in order to be treated as hedges for accounting purposes. Accordingly, all movements in the fair value of derivative financial instruments are reflected in the income statement. This has resulted in a net liability of £397m in the balance sheet at 31 March 2018 (2017: £477m) but, assuming that the swaps are held to maturity, this will ultimately reduce to £nil.

Power price hedges
The group enters into contracts which fix the price of a proportion of future power purchases in order to reduce the impact of power price variances. These contracts qualify as financial instruments and are included in the financial statements.

Refinancing risk
Refinancing risk is managed by maintaining a balance between the continuity of funding and flexibility through the use of borrowings across a range of instruments, types and maturities. The Group's policy is to ensure that the maturity profile does not impose an excessive strain on its ability to repay loans. Under this policy, no more than 20% of the principal of Group borrowings of £3,309m (2017: £2,923m) can fall due in any 24 month period.

Liquidity risk
The Group maintains committed banking facilities in order to provide flexibility in the management of its liquidity.

Under the Common Terms Agreement which governs obligations to bondholders and other financial creditors, the Group is required to have cash available to fund operations for 12 months. As at 31 March 2018, the Group had committed undrawn borrowing facilities of £420m (2017: £460m) and cash and cash equivalents (excluding debt service payments account) of £294m (2017: £95m).

The undrawn facilities comprise £170 million revolving credit facilities which are available until 2020 and a European Investment Bank loan facility of £250m, available until January 2019. There is also a £10m overdraft facility renewable on an annual basis.

As at 31 March 2018 there was also a special liquidity facility of £135 million (2017: £135 million); this is required in order to meet certain interest and other obligations that cannot be funded through operating cash flow in the event of a standstill being declared by the security trustee, following an event of default under the Group's debt financing covenants. The facility is renewable on an annual basis.

Capital risk
The Group's objective when managing capital is to safeguard its ability to continue as a going concern. Given the regulatory environment in which the Group operates, the Group monitors capital on the basis of the gearing ratio. This is calculated as net debt (as defined in the Group's borrowing covenants) as a proportion of its Regulatory Capital Value (RCV) as linked to movements in the Retail Prices Index and determined by Ofwat. As at 31 March 2018 this regulatory gearing was 57% (2017: 56%).

In respect of the risks detailed above, further quantitative disclosures are provided in note 16.

CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements conforming to IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates.

Provision for impairment of trade receivables
Individual impairment losses on customer debts are calculated based on an individual assessment of expected cash flows. Collective impairment losses on receivables with similar credit risk are calculated using a statistical model. The key assumption in the model is the probability of a failure to recover amounts when they fall into arrears. The probability of failing to recover a debt is determined by past experience, adjusted for changes in external factors. The accuracy of the impairment calculation would therefore be affected by unexpected changes to the economic situation, and to changes in customer behaviour. To the extent that the failure to recover debts in arrears alters by 1%, the provision for impairment would increase or decrease by £0.9m (2017: £1.0m).

Pension benefits
The present value of the pension obligations is dependent on the actuarial calculation, which includes a number of assumptions. These assumptions include the discount rate, price inflation and mortality rates, which are used to calculate the present value of the estimated future cash outflows that will be required to meet the pension obligations. In determining the discount rate to use, the Group considers market yields of high quality corporate bonds, denominated in sterling, that have times to maturity approximating the terms of the pension liability. Were this discount rate to reduce or increase by 0.1%, the carrying value of the pension obligations as at 31 March 2018 would increase or reduce by £8.9m (2017: £9.9m).

Measured income accrual
Revenue includes an accrual for unbilled charges at the year-end. The accrual is estimated using a defined methodology based upon the weighted average water consumption by tariff, which is calculated using historical billing information adjusted for changes in external factors, such as weather. The total accrual as at 31 March 2018 was £70.8m (2017: £68.8m). A 1% change in actual consumption from that estimated would have the effect of increasing or decreasing the accrual by £0.5m (2017: £0.5m).

Fair value estimation
In accordance with IFRS 13 Fair Value Measurement trading and treasury derivatives of the Group are categorised into different levels:

Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (prices) or indirectly (derived from prices).

Level 3: inputs for the asset or liability not based on observable market data.

All of the Group's trading and treasury derivatives are categorised at Level 2 and as at 31 March 2018 were valued as follows:

Assets: trading derivatives £4.8m, treasury derivatives £3.5m. (March 2017: trading derivatives £2.6m, treasury derivatives £3.6m).

Liabilities: trading derivatives £0.3m treasury derivatives £405.1m. (March 2017: trading derivatives £3.3m, treasury derivatives £479.9 m).

Trading derivatives relate to power price hedges. Treasury derivatives relate to interest rate swap contracts and are recorded on the balance sheet at fair value. These have all been assessed as Level 2.

The power price hedging contracts have been fair valued using rates that are quoted in an active market. Interest rate swaps are fair valued using forward interest rates extracted from observable yield curves. The effects of discounting are generally insignificant for Level 2 derivatives.

Level 2 debt investments are valued using a discounted cash flow approach, which discounts the contractual cash flows using discount rates derived from observable market prices of other quoted debt instruments of the counterparties.

There were no transfers between Levels 1 and 2 during the year.

Capitalisation
There is a high degree of judgement involved in determining whether costs, both initial and subsequent expenditure, including employee and other internal expenditure on both infrastructure and non-infrastructure assets meet the relevant criteria for capitalisation (directly attributable to the asset, provide probable economic benefit and can be measured reliably) and therefore are included in the valuation of property, plant and equipment, or alternatively should be expensed immediately.

2. SEGMENTAL INFORMATION

The Directors consider that there is only one operating segment, being the operation of water and sewerage business (and peripheral commercial activities) in the UK. As the Group has only domestic activities there is also only one geographical segment; therefore, the disclosures for this segment have also already been given in these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

3. LOSS BEFORE TAXATION

The following items have been included in arriving at the loss before taxation:

Group	2018 £m	2017 £m
Operating expenditure		
Power	**42.7**	41.0
Chemicals	**9.6**	9.3
Materials and equipment	**5.5**	5.5
Vehicles and plant	**8.5**	7.8
Office expenses	**9.8**	10.3
Property costs	**4.0**	3.5
Insurance	**4.1**	5.7
Sewerage contractors	**19.8**	18.5
Laboratories and analytical services	**0.8**	0.7
Collection commissions	**4.2**	3.6
IT contracts	**11.1**	16.2
Bought-in services and other costs	**38.9**	35.3
Employee costs (note 20)	**150.4**	134.4
Staff costs capitalised	**(53.8)**	(48.3)
Research and development credit	**(1.4)**	-
Trade receivables impairment	**22.1**	23.3
Rates	**26.9**	30.5
Natural Resources Wales/Environment Agency charges	**15.3**	14.8
Fees payable to auditors	**0.5**	0.5
Total operational expenditure	**319.0**	312.6
Infrastructure renewals expenditure	**86.0**	69.7
Depreciation and amortisation		
Depreciation of property plant and equipment	**259.8**	241.4
Release of deferred income	**(5.2)**	(4.5)
Amortisation of intangible assets	**21.7**	19.7
Total depreciation and amortisation	**276.3**	256.6
Total operating costs	**681.3**	638.9

NOTES TO THE FINANCIAL STATEMENTS

SERVICES PROVIDED BY THE GROUP'S AUDITORS

During the year, the Group obtained the following services from its statutory auditors:

Group	2018	2017
Audit fees	**£000**	£000
Audit of parent company and consolidated financial statements	**20**	20
Audit of subsidiary companies	**139**	120
Total audit fees	**159**	140
Audit-related assurance services		
Review of interim financial statements	**22**	22
Regulatory audit services pursuant to legislation	**48**	39
Regulatory price review assurance work	**-**	14
Scheme of charges assurance work	**26**	25
Investor report reviews	**6**	6
Environment Agency levy assurance work	**3**	3
Bond issuance assurance work	**38**	-
Wholesale charges assurance work	**-**	22
Total audit and audit-related assurance services	**302**	271
Other services		
Pensions advice	**80**	37
Tax advisory services	**-**	17
Assurance on market opening	**-**	25
Assurance on commercial activities	**58**	85
Legal services advice including payroll, reward and data analytics services regarding Gender Pay Gap reporting and a voluntary equal pay audit	**65**	30
Total other services	**203**	194
Total cost of services provided by the Group's auditors	**505**	465

Audit fees for the year ended 31 March 2018 reflect additional audit work required following the acquisition of Welsh Water Organic Energy Limited and Welsh Water Organic Energy (Cardiff) Limited (see note 22).

Regulatory audit services include audit work in respect of regulatory requirements: the Annual Performance Report, Cost Assessment tables and Principal Statement.

The Board has adopted a formal policy with respect to services received from external auditors. The external auditors will not be used for internal audit services and all non-audit work will be subject to prior competitive tendering or approval by the Audit Committee.

NOTES TO THE FINANCIAL STATEMENTS

4. FINANCING COSTS

a) Finance cost before fair value gains/(losses) on derivative financial instruments

Group	2018 £m	2017 £m
Interest payable on bonds	**(86.7)**	(88.4)
Indexation on index-linked bonds	**(45.7)**	(24.8)
Indexation on index-linked loan	**(9.6)**	(5.7)
Interest payable on finance leases (including swaps to RPI)	**(20.8)**	(18.5)
Other loan interest	**(20.0)**	(12.6)
Other interest payable and finance costs	**(7.0)**	(1.9)
Net interest charge on pension scheme liabilities	**(2.5)**	(1.8)
Capitalisation of borrowing costs under IAS 23 (2018: 6.1%; 2017: 5.2%)	**16.4**	9.5
	(175.9)	(144.2)
Finance income	**3.9**	3.6
Net finance cost before fair value adjustments	**(172.0)**	(140.6)

b) Fair value gains/(losses) on derivative financial instruments

Derivative financial instruments are held for economic hedging purposes although they do not qualify as accounting hedges under IAS 39. Consequently, the Group's interest rate and index-linked swaps are fair valued at each balance sheet date with the net loss or gain disclosed in the income statement. Over the life of these swaps, if held to maturity, these fair value adjustments will reverse and reduce to zero. (See note 15 in respect of derivative financial instruments held on the balance sheet).

Group	2018 £m	2017 £m
Fair value gains/(losses) on interest rate swaps	**3.6**	(2.6)
Fair value gains/(losses) on index-linked swaps	**71.2**	(69.0)
Fair value gains on trading derivatives	**5.2**	8.6
Total fair value gains/(losses) on derivative financial instruments	**80.0**	(63.0)

Interest rate swap movements are caused by fluctuations in long-term interest rates, while the index-linked swap movements result from fluctuations in the value of index-linked gilts.

5. TAXATION

Analysis of credit in the year

Group	2018 £m	2017 £m
Current tax		
Current tax on loss for the year	**0.4**	1.0
Current tax on research and development credit	**(0.3)**	-
Adjustment in respect of prior years	**0.9**	(0.1)
Total current tax	**1.0**	0.9
Deferred tax		
Origination and reversal of timing differences	**2.3**	17.5
Adjustment in respect of prior year	**(0.7)**	(1.9)
Effect of tax rate change	**-**	12.4
Total deferred tax (note 6)	**1.6**	28.0
Taxation credit	**2.6**	28.9

The current tax credit of £0.4m (2017: £1.0m) has arisen from the surrender of tax losses relating to energy efficient capital expenditure.

Operating expenditure includes a tax credit of £1.4m (2017: £nil) relating to R&D expenditure. The tax credit is taxable and the corresponding charge of £0.3m is shown above.

Tax trading losses carried forward as at 31 March 2018 are £nil (2017: £189m) and have decreased as a result of disclaiming capital allowances in relation to a prior period.

Adjustments in respect of prior years relate to revisions to deferred tax balances in respect of capital expenditure, and adjustments to tax credits for energy efficient capital expenditure and the remediation of contaminated land.

Deferred taxes have benefitted from a £11.8m credit in the year ended 31 March 2017 following reductions made to the future rates of corporation taxes. The rate used to calculate deferred taxes fell from 18% to 17% for that year. The Government has not announced any further reductions to corporation tax rates and therefore no further credits arising from rate changes are expected in future periods.

The effective rate of tax for the year is lower (2017: higher) than the standard rate of corporation tax in the UK of 19% (2017: 20%). The differences are explained below:

Group	2018 £m	2017 £m
Loss before tax	**(14.8)**	(98.9)
Loss before tax multiplied by the corporation tax rate in the UK of 19% (2017: 20%)	**(2.8)**	(19.8)
Effect of:		
Adjustments in respect of prior years	**(0.1)**	1.9
Other permanent differences	**1.0**	0.7
Effect of pension payments in excess of service charge	**(0.7)**	(1.0)
Effect of tax rate change on closing deferred tax from 18% to 17%	**-**	(12.4)
Difference in standard rate of corporation tax (19%) and rate used for deferred tax (17%)	**-**	1.7
Total taxation credit	**(2.6)**	(28.9)

NOTES TO THE FINANCIAL STATEMENTS

6. DEFERRED TAX

Deferred tax is calculated in full on temporary differences under the liability method using a tax rate of 17% (2017: 17%).

The movement in the deferred tax provision is as shown below:

Group	2018 £m	2017 £m
At 1 April	**413.2**	431.8
Credit to Income Statement	**(1.6)**	(28.0)
Charge/(credit) to the Statement of Comprehensive Income	**2.8**	(5.9)
Charge to Revaluation Reserve	**26.9**	15.3
At 31 March	**441.2**	413.2

Analysis of amounts charged/(credited) to the Statement of Comprehensive Income and Revaluation Reserve:

Group	2018 £m	2017 £m
Defined benefit pension schemes	**2.1**	(7.8)
Reallocation of tax from income statement - pension payment in excess of service charge	**0.7**	1.0
Reduction in corporation tax rate - pension scheme	**-**	0.9
Charged/(credited) to the Statement of Comprehensive Income	**2.8**	(5.9)
Revaluation of fixed assets	**26.9**	28.2
Reduction in corporation tax rate - revaluation of fixed assets	**-**	(12.9)
Charged to the Revaluation Reserve	**26.9**	15.3

Group	2018 £m	2017 £m
Effect of:		
Tax allowances in excess of depreciation	**281.0**	316.0
Deferred tax on revaluation of fixed assets	**234.1**	218.9
Capital gains rolled over	**2.7**	2.7
Deferred tax on tax losses carried forward	**(1.4)**	(32.1)
Deferred tax on losses on derivative financial instruments	**(60.7)**	(75.1)
Pensions	**(12.9)**	(15.7)
Other tax differences	**(1.6)**	(1.5)
Net provision for deferred tax	**441.2**	413.2

Deferred tax assets have been recognised in respect of all tax losses and other temporary differences giving rise to deferred tax assets because it is probable that these assets will be recovered. Under the current tax regime, trading tax losses carried forward will be available to offset trading profits in future periods.

The parent company has no deferred tax balance (2017: nil).

7. REVALUATION RESERVE

Revaluation reserve movement	2018 £m	2017 £m
Revaluation reserve as at 1 April	**1,069.1**	977.9
Revaluation of assets to RCV	**158.1**	156.8
Depreciation charge on revalued assets	**(69.3)**	(61.3)
	88.8	95.5
Deferred tax on revaluation	**(26.9)**	(15.3)
Deferred tax on depreciation charge	**11.8**	11.0
	(15.1)	(4.3)
Revaluation reserve as at 31 March	**1,142.8**	1,069.1

8. PROPERTY, PLANT AND EQUIPMENT

Group — 2018	Freehold land & buildings £m	Infrastructure assets £m	Operational structures £m	Plant, equipment, computer hardware £m	Total £m
Cost or valuation					
At 1 April 2017	41.7	2,236.5	3,866.1	264.1	6,408.4
Revaluation	-	21.5	-	-	21.5
Additions net of grants and contributions	-	104.3	239.4	5.7	349.4
Disposal	-	-	-	(6.6)	(6.6)
At 31 March 2018	**41.7**	**2,362.3**	**4,105.5**	**263.2**	**6,772.7**
Accumulated depreciation					
At 1 April 2017	20.6	-	1059.2	263.4	1,343.2
Revaluation	-	(48.6)	(88.0)	-	(136.6)
Charge for the year	0.7	48.6	206.5	4.1	259.9
Released on disposal	-	-	-	(5.9)	(5.9)
At 31 March 2018	**21.3**	**-**	**1,177.7**	**261.6**	**1,460.6**
Net book value					
At 31 March 2018	**20.4**	**2,362.3**	**2,927.8**	**1.6**	**5,312.1**
At 31 March 2018 (historic cost basis)	**20.4**	**1,730.8**	**2,182.3**	**1.6**	**3,935.1**

The net book value of property, plant and equipment includes £278.5m in respect of assets in the course of construction (2017: £207.6m).

£55.4m of borrowing costs were capitalised in accordance with IAS 23 (2017: £42.9m) of which £14.1m were additions in the year (2017: £8.4m).

Group — 2017	Freehold land & buildings £m	Infrastructure assets £m	Operational structures £m	Plant, equipment, computer hardware £m	Total £m
Cost or valuation					
At 1 April 2016	41.6	2,090.1	3,681.9	262.4	6,076.0
Revaluation	-	24.3	-	-	24.3
Additions net of grants and contributions	0.1	122.1	184.2	2.1	308.5
Disposals	-	-	-	(0.4)	(0.4)
At 31 March 2017	41.7	2,236.5	3,866.1	264.1	6,408.4
Accumulated depreciation					
At 1 April 2016	19.8	-	955.2	259.7	1,234.7
Revaluation	-	(43.8)	(88.7)	-	(132.5)
Charge for the year	0.8	43.8	192.7	4.1	241.4
Released on disposal	-	-	-	(0.4)	(0.4)
At 31 March 2017	20.6	-	1,059.2	263.4	1,343.2
Net book value					
At 31 March 2017	21.1	2,236.5	2,806.9	0.7	5,065.2
At 31 March 2017 (historic cost basis)	21.1	1,662.8	2,092.4	0.7	3,777.0

Assets held under finance leases

Included within the above are assets held under finance leases as analysed below:

Group — 2018	Infrastructure assets £m	Operational structures £m	Total £m
At 31 March 2018			
Valuation	669.9	117.7	787.6
Accumulated depreciation	-	(77.7)	(77.7)
Net book value	**669.9**	**40.0**	**709.9**

Group — 2017	Infrastructure assets £m	Operational structures £m	Total £m
At 31 March 2017			
Valuation	670.5	117.7	788.2
Accumulated depreciation	-	(73.6)	(73.6)
Net book value	670.5	44.1	714.6

The parent company owns no property, plant or equipment.

9. INTANGIBLE ASSETS

Group — 2018	Cost £m	Amortisation £m	Net book value £m
At 1 April 2017	274.8	(155.3)	119.5
Additions/(charge for the year)	48.5	(21.7)	26.8
At 31 March 2018	**323.3**	**(177.0)**	**146.3**

Intangible assets principally comprise computer software and related system developments.

Group — 2017	Cost £m	Amortisation £m	Net book value £m
At 1 April 2016	241.3	(135.6)	105.7
Additions/(charge for the year)	33.5	(19.7)	13.8
At 31 March 2017	274.8	(155.3)	119.5

The net book value of intangible assets includes £36.7m in respect of assets in the course of construction (2017: £20.0m). The net book value of intangible assets includes £5.6m of borrowing costs capitalised in accordance with IAS 23 (2017: £3.6m), of which £2.3m were additions in the year (2017: £1.1m).

The parent company owns no intangible assets.

10. INVESTMENTS

Group
Equity of less than 10% is held in the following unlisted company:

	Principal activities	Country of incorporation	Holding
Water Research Centre (1989) plc	Water research	England and Wales	B" Ordinary Shares of £1

Parent Company
The parent company has a £1 investment in Glas Cymru (Securities) Cyfyngedig (100% holding) and a £100,000 investment in Welsh Water Holdings Limited (100%). It also has indirect investments in the following subsidiary undertakings:

	Principal activities	Tax Residency	Country of incorporation	Holding
Dŵr Cymru (Holdings) Limited	Holding company	UK resident	England and Wales	100%
Dŵr Cymru Cyfyngedig	Water and sewerage	UK resident	England and Wales	100%
Dŵr Cymru (Financing) Limited	Raising finance	UK resident	Cayman Islands	100%
Cambrian Utilities Limited	Retail services in the competitive market	UK resident	England and Wales	100%
Welsh Water Infrastructure Limited	Competitive business activity in the water sector and other associated sectors	UK resident	England and Wales	100%
Welsh Water Organic Energy Limited	Food waste processing, treatment and recycling	UK resident	England and Wales	100%
Welsh Water Organic Energy (Cardiff) Limited	Operation and maintenance of an anaerobic digestion food waste facility	UK resident	England and Wales	100%

The registered office of all the above companies is Pentwyn Road, Nelson, Treharris, Mid Glamorgan CF46 6LY.

The Company has revalued its investments in subsidiary undertakings to fair value; the carrying value is revalued annually and subject to an impairment review.

Further information on the Group's structure is available in the Annual Report on page 53.

Investment in subsidiaries	2018 £m	2017 £m
At beginning of period	**3,228.6**	0.1
Revaluation	**169.5**	3,228.5
At 31 March	**3,398.1**	3,228.6

The parent company's investments in subsidiary companies are initially recognised at cost and subsequently revalued to fair value using a discounted cash flow method. The fair value of investments comprises mainly the fair value of the regulated water and sewerage company, Dŵr Cymru Cyfyngedig. A present value has been determined using a discount rate based on the regulator's allowed weighted average cost of capital and a terminal value being the projected regulatory capital value. Revaluation amounts are recognised in other comprehensive income.

11. TRADE AND OTHER RECEIVABLES

Group	2018 £m	2017 £m
Current		
Trade receivables	**556.7**	556.6
Provision for impairment of receivables	**(83.8)**	(95.8)
Trade receivables - net	**472.9**	460.8
Prepayments and accrued income	**88.1**	90.2
Other receivables	**16.7**	12.2
	577.7	563.2
Non-current		
Other receivables	**0.9**	-
Total trade and other receivables	**578.6**	563.2

As at 31 March 2018, based on a review of historical collection rates it was considered that £83.8m (2017: £95.8m) of trade receivables were impaired and these have therefore been provided for. The impaired receivables relate mainly to the measured and unmeasured supply of water and sewerage services. Trade receivables aged greater than one month are past due; the net column shows amounts deemed not to be impaired.

The ageing of receivables was as follows:

Current year Trade receivables	Total £m	Provided for £m	Net £m
Billed in advance	**369.8**	-	**369.8**
Under one month	**25.8**	(2.7)	**23.1**
Between one and six months	**35.5**	(3.3)	**32.2**
Between six months and one year	**26.5**	(3.2)	**23.3**
Between one and two years	**42.5**	(30.9)	**11.6**
Between two and three years	**30.5**	(23.1)	**7.4**
Over three years	**26.1**	(20.6)	**5.5**
	556.7	**(83.8)**	**472.9**

Prior year **Trade receivables**	**Total** **£m**	**Provided for** **£m**	**Net** **£m**
Billed in advance	370.2	-	370.2
Under one month	25.4	(9.1)	16.3
Between one and six months	33.5	(13.1)	20.4
Between six months and one year	33.3	(5.8)	27.5
Between one and two years	39.3	(24.0)	15.3
Between two and three years	34.4	(23.3)	11.1
Over three years	20.5	(20.5)	-
	556.6	(95.8)	460.8

The maximum exposure to credit risks at the reporting date is the carrying value of each class of receivable mentioned above. The Group holds around 4,100 charging orders as collateral against £9m of debt.

Movements in the provision for impairment of trade receivables are as follows:

	2018 **£m**	**2017** **£m**
At 1 April	**95.8**	85.3
Charge to Income Statement	**20.8**	22.8
Receivables written off during the year as uncollectable	**(32.8)**	(12.3)
At 31 March	**83.8**	95.8

The creation and release of provision for impaired receivables have been included in operational expenditure.

The other classes of trade and other receivables do not contain impaired assets. All trade and other receivables are denominated in sterling.

During the year the Group has written off £32.8m of debt which had been provided for in full (2017: £12.3m).

The total charge to the income statement of £22.1m (2017: £23.3m) includes the bad debt element of collection charges under arrangements with third parties who collect debt on the Group's behalf (2018: £1.3m, 2017: £0.5m).

12. CASH AND CASH EQUIVALENTS

	Group **2018** **£m**	**Group** **2017** **£m**	**Company** **2018** **£m**	**Group** **2017** **£m**
Cash at bank and in hand	**10.0**	36.6	**-**	-
Short-term deposits	**278.5**	64.0	**8.6**	30.1
	288.5	100.6	**8.6**	30.1

The effective interest rate on short-term deposits as at 31 March 2018 was 0.5% (2017: 0.2%) and these deposits had an average maturity of 22 days (2017: 16 days). With the exception of €76,000, all cash and cash equivalents are held in sterling.

NOTES TO THE FINANCIAL STATEMENTS

13. TRADE AND OTHER PAYABLES

Group **Current**	**2018** **£m**	**2017** **£m**
Trade payables	**45.7**	44.6
Capital payables	**60.3**	65.8
Social security and other taxes	**3.4**	4.3
Accruals and deferred income	**454.7**	441.8
	564.1	556.5

Group **Non-current**	**2018** **£m**	**2017** **£m**
Deferred income	**233.9**	204.6

14. FINANCIAL LIABILITIES — BORROWINGS

Group **Current**	**2018** **£m**	**2017** **£m**
Overdrawn funds	**5.1**	5.9
Interest accruals	**2.4**	0.9
Bonds	**0.3**	0.3
Term loans	**21.7**	21.7
Finance lease obligations	**12.0**	10.5
	41.5	39.3

Group **Non-current**	**2018** **£m**	**2017** **£m**
Interest accruals	**48.8**	48.2
Bonds	**2,356.1**	2,014.0
Term loans	**488.5**	440.6
Finance lease obligations	**423.9**	436.0
	3,317.3	2,938.8

The parent company has no borrowings.

A security package was granted by Dŵr Cymru Cyfyngedig (DCC), as part of the Group's bond programme for the benefit of holders of senior bonds, finance lessors and other senior financial creditors.

The obligations of DCC are guaranteed by the Company, Glas Cymru (Securities) Cyfyngedig and Dŵr Cymru (Holdings) Limited. The main elements of the security package are:

i) a first fixed and floating security over all of DCC's assets and undertaking, to the extent permitted by the Water Industry Act, other applicable law and its licence; and

ii) a fixed and floating security given by the guarantors referred to above which are accrued on each of these companies' assets including, in the case of Dŵr Cymru (Holdings) Limited, a first fixed charge over its shares in DCC.

The Group's Class A Bonds of £1,008m (2017: £989m) benefit from a guarantee from Assured Guaranty (London) Ltd. Assured Guaranty's credit rating is graded as Baa2 and A by Moody's and Standard and Poor's respectively, and is not rated by Fitch. The credit rating of the Class A bonds has therefore defaulted to the higher underlying rating of these bonds, of A2/A/A from Moody's, Standard and Poor's and Fitch respectively. The underlying rating reflects the standalone credit quality of these bonds without the benefit of the guarantee from Assured Guaranty, and is the same as the credit ratings of the Group's Class B bonds of £1,350m (2017: £1,023m).

15. DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments are held for economic hedging purposes. However, they do not qualify as accounting hedges under IAS 39 and movements in their fair value are taken to the Income Statement (see note 4b). The fair values of all derivative financial instruments held by the Group are the result of mark-to-market pricing by the issuing counterparties and as such fall within Level 2 of the fair value hierarchy set out in IFRS 7.

Fair values	**Assets**	**Liabilities**
Group — 2018	**£m**	**£m**
Current		
Index-linked swaps	**3.5**	**(20.2)**
Interest rate swaps	**-**	**(9.0)**
Power hedging swaps	**2.9**	**-**
	6.4	**(29.2)**
Non-current		
Index-linked swaps	**-**	**(295.0)**
Interest rate swaps	**-**	**(80.9)**
Power hedging swaps	**1.9**	**(0.3)**
	1.9	**(376.2)**
Total	**8.3**	**(405.4)**

Fair values	**Assets**	**Liabilities**
Group — 2017	**£m**	**£m**
Current		
Index-linked swaps	3.6	(25.8)
Interest rate swaps	-	(9.2)
Power hedging swaps	0.4	(0.2)
	4.0	(35.2)
Non-current		
Index-linked swaps	-	(360.5)
Interest rate swaps	-	(84.4)
Power hedging swaps	2.2	(3.1)
	2.2	(448.0)
Total	6.2	(483.2)

In accordance with IAS 39, 'Financial instruments: Recognition and Measurement', the Group has reviewed all contracts for embedded derivatives that are required to be accounted for separately if they do not meet certain requirements set out in the standard. The Group has no such embedded derivatives as per IAS 39.

The parent company has no derivative financial instruments or embedded derivatives.

Interest rate swaps
At 31 March 2018 an interest rate swap fixes the interest rate on £192m (2017: £192m) of floating liabilities held by the Group. The maturity date of the swap is 31 March 2031 and the fixed interest rate is 5.67% per annum, payable quarterly.

Index-linked swaps
Finance lease swaps
The index-linked swaps have the effect of index-linking the interest rate on £381m (2017: £381m) of finance lease liabilities by reference to the Retail Prices Index ("RPI").

The notional amount of index-linked swaps allocated to finance leases as at 31 March 2018 was £399m (2017: £400m), representing the average balance on the finance leases subject to floating interest rates for the year to 31 March 2018. The notional amount amortises over the life of the swaps to match the average floating rate balances of the leases.

The principal terms of the index linked swaps are as follows:

Notional amount	£399m amortising (2017: £400m amortising)
Average swap maturity	18 years (2017: 18 years)
Average interest rate	1.40% fixed plus RPI (2017: 1.35% fixed plus RPI)

Bond swap
The index-linked swap have the effect of index-linking the interest rate on £100m of fixed rate bonds by reference to the RPI.

The principal terms are as follows:

Indexed notional amount	£140m (2017: £135m)
Swap maturity	39 years (2017: 40 years)
Interest rate	1.35% indexed by RPI (2017: 1.35% indexed by RPI)

16. FINANCING RISK MANAGEMENT

The policies of the Group in respect of financing risk management are included in the accounting policies note on page 106. The numerical financial instrument disclosures as required by IFRS 7 are set out below.

a) Interest rate risk
The effective interest rates at the balance sheet dates were as follows:

	2018	**2017**
Assets:		
Cash and cash equivalents	**0.5%**	0.2%
Liabilities:		
Bonds	**4.1%**	4.3%
Term loans	**0.6%**	0.5%
Other unsecured loans	**5.0%**	5.0%
Finance lease obligations	**0.6%**	0.7%

Trade and other receivables and payables are non interest-bearing.

The effective interest rates ignore the effect of the interest rate and index-linked swaps set out in note 15. They also exclude the indexation charge applicable to the index-linked bonds.

b) Liquidity risk

Group — 2018	Within 1 year £m	1 - 2 years £m	2 - 5 years £m	> 5 years £m	Total £m
Assets:					
Cash and cash equivalents	288.5	-	-	-	288.5
Trade and other receivables	577.7	-	-	-	577.7
	866.2	-	-	-	866.2
Liabilities:					
Cash and cash equivalents	5.1	-	-	-	5.1
Bonds	0.7	0.7	327.1	2,035.4	2,363.9
Term loans	21.6	29.1	155.0	304.0	509.7
Other unsecured loans	0.1	0.1	0.3	-	0.5
Finance lease obligations	12.0	13.5	32.8	377.6	435.9
Trade and other payables	564.1	5.2	15.6	213.1	798.0
Future interest payable	121.0	124.1	368.2	1,042.4	1,655.7
	724.6	172.7	899.0	3,972.5	5,768.8

Group — 2017	Within 1 year £m	1 - 2 years £m	2 - 5 years £m	> 5 years £m	Total £m
Assets:					
Cash and cash equivalents	100.6	-	-	-	100.6
Trade and other receivables	563.3	-	-	-	563.3
	663.9	-	-	-	663.9
Liabilities:					
Cash and cash equivalents	5.9	-	-	-	5.9
Bonds	0.7	0.7	327.1	1,690.2	2,018.7
Term loans	21.6	21.6	163.0	255.5	461.7
Other unsecured loans	0.1	0.1	0.4	-	0.6
Finance lease obligations	10.5	11.9	45.5	378.6	446.5
Trade and other payables	556.5	1.8	4.9	197.9	761.1
Future interest payable	112.9	113.5	335.6	917.5	1,479.5
	708.2	149.6	876.5	3,439.7	5,174.0

The minimum lease payments under finance leases fall due as follows:

	2018 £m	2017 £m
Gross finance lease liabilities		
Within one year	15.9	19.6
Between two and five years	82.1	99.2
After five years	438.3	439.6
	536.3	558.4
Future interest	(100.4)	(111.9)
Net finance lease liabilities	435.9	446.5
Net finance lease liabilities are repayable as follows:		
Within one year (note 14)	12.0	10.5
Between two and five years	46.3	57.4
After five years	377.6	378.6
Total over one year (note 14)	423.9	436.0

c) Fair values

The fair values of the Group's derivative financial instruments are set out in note 15. The following table summarises the fair value and book value of the Group's bonds.

	2018 Book value £m	2018 Fair value £m	2017 Book value £m	2017 Fair value £m
Bonds	2,363.9	3,171.2	2,018.7	2,934.4

The fair values of all other financial instruments are equal to the book values. On 17 January 2018 the Group announced a benchmark – sized GBP Class B bond transaction. The bond proceeds of £300m were settled on 24 January 2018 with a maturity date of 31 March 2036 and a fixed coupon of 2.5%.

d) Borrowing facilities

As at 31 March 2018, the Group had available undrawn committed borrowing facilities of £420m expiring as set out below, in respect of which all conditions precedent had been met (2017: £460m).

	2018 £m	2017 £m
Expiring in less than 1 year:		
- term loan facility	250	60
Expiring in more than 1 year:		
- revolving credit facilities	170	150
- term loan facility	-	250
	170	400
	420	460

The term loan facility of £60m with KfW-IPEX Bank was drawn on 5 May 2017. The loan will start to amortise from May 2020 and will be repayable in six-monthly instalments until November 2025.

The undrawn facilities comprise £170m revolving credit facilities which are available until 2020 and a European Investment Bank loan facility of £250m, available until January 2019. There is also a £10m overdraft facility renewable on an annual basis.

As at 31 March 2018 there was also a special liquidity facility of £135m (2017: £135m); this is required in order to meet certain interest and other obligations that cannot be funded through operating cash flow in the event of a standstill being declared by the security trustee, following an event of default under the Group's debt financing covenants. The facility is renewable on an annual basis.

All of the above facilities are at floating rates of interest.

e) Capital risk management

Gearing ratios	2018 £m	2017 £m
Total borrowings	(3,359)	(2,978)
Less: cash and cash equivalents	289	101
Net debt	(3,070)	(2,877)
Regulatory capital value (RCV)	5,468	5,217
Total capital	2,398	2,340
Less: unamortised bond costs and swap indexation	(48)	(39)
Total capital per bond covenants	2,350	2,301
Gearing ratio	57%	56%

As set out on page 86, the Group monitors its capital structure based on a regulatory gearing ratio which compares its net debt to the Ofwat-determined RCV.

Under the Common Terms agreement regulatory gearing is calculated as the level of net debt in the whole business securitisation relative to the regulatory capital value.

17. PROVISIONS

Group — 2018	Restructuring provision	Uninsured loss provision	Other provisions	Total
	£m	£m	£m	£m
At 1 April 2017	4.0	4.3	2.5	10.8
Charged to Income Statement	-	1.2	-	1.2
Unused amounts reversed	-	-	(0.1)	(0.1)
Utilised in year	(1.6)	(1.3)	(0.1)	(3.0)
At 31 March 2018	**2.4**	**4.2**	**2.3**	**8.9**
Split as:				
Amounts to be utilised within one year	1.0	1.3	0.1	2.4
Amounts to be utilised after more than one year	1.4	2.9	2.2	6.5
At 31 March 2018	**2.4**	**4.2**	**2.3**	**8.9**

Group — 2017	Restructuring provision	Uninsured loss provision	Other provisions	Total
	£m	£m	£m	£m
At 1 April 2016	5.9	3.9	4.7	14.5
Charged to Income Statement	-	1.7	(0.2)	1.5
Utilised in year	(1.9)	(1.3)	(2.0)	(5.2)
At 31 March 2017	4.0	4.3	2.5	10.8
Split as:				
Amounts to be utilised within one year	1.0	-	0.2	1.2
Amounts to be utilised after more than one year	3.0	4.3	2.3	9.6
At 31 March 2017	4.0	4.3	2.5	10.8

The parent company had no provisions at 31 March 2018 (2017: none).

Restructuring provision
This provides for the cost of restructuring associated with a reduction in the headcount by around 360, pursuant to the restructuring plan for the five-year period 2015-2020 as a whole.

Uninsured loss provision
This provision is in respect of uninsured losses and instances where insurance does not cover a deductible amount. The utilisation period of these liabilities is uncertain due to the nature of claims, but is estimated to be within five years.

Other provisions
Other provisions are made for certain other obligations which arise during the ordinary course of the Group's business.

18. NET CASH INFLOW FROM OPERATING ACTIVITIES

a) Cash generated from operations
Reconciliation of operating profit to cash generated from operations:

Group	2018	2017
	£m	£m
Operating profit	**75.4**	104.7
Adjustments for:		
Depreciation and amortisation	**276.3**	256.6
Changes in working capital:		
Increase in trade and other receivables	**(14.6)**	(20.4)
Increase in inventories	**(0.4)**	(0.7)
Increase in trade and other payables	**17.7**	6.3
Pension contributions above service cost	**(5.0)**	(6.2)
Decrease in provisions	**(1.9)**	(3.4)
	(4.2)	(24.4)
Cash generated from operations	**347.5**	336.9

Pension contributions above service cost represent DCWW Pension Scheme deficit recovery costs paid in accordance with the Recovery Plan agreed between the Company and the Scheme's Trustees.

b) Interest paid

Group	2018	2017
	£m	£m
Interest payable per income statement	**175.9**	144.2
Less non-cash items:		
Indexation on index-linked bonds	**(45.7)**	(24.8)
Indexation on index-linked debt	**(9.6)**	(5.7)
Amortisation of bond issue costs	**(0.3)**	(0.3)
Interest charge on pension scheme liabilities	**(2.5)**	(1.8)
Amortisation of bond issue premium	**0.7**	0.6
Effect of capitalisation under IAS 23	**16.4**	9.5
(Increase)/decrease in accruals	**(2.0)**	2.9
	(43.0)	(19.6)
Interest paid	**132.9**	124.6

19. ANALYSIS AND RECONCILIATION OF NET (DEBT)/FUNDS

Net (debt)/funds is defined as the value of cash and cash equivalents less net accrued interest and total borrowings.

a) Net (debt)/funds at the balance sheet date may be analysed as:

	Group		Company	
	2018 £m	2017 £m	2018 £m	2017 £m
Cash and cash equivalents	**288.5**	100.6	8.6	30.1
Debt due after one year	**(2,844.6)**	(2,454.6)	-	-
Debt due within one year	**(27.1)**	(27.9)	-	-
Finance leases	**(435.9)**	(446.5)	-	-
Accrued interest	**(51.2)**	(49.1)	0.2	-
	(3,358.8)	(2,978.1)	0.2	-
Net (debt)/funds	**(3,070.3)**	(2,877.5)	8.8	30.1

b) The movement in net (debt)/funds during the year may be summarised as:

	Group		Company	
	2018 £m	2017 £m	2018 £m	2017 £m
Net (debt)/funds at start of year	**(2,877.5)**	(2,808.1)	**30.1**	-
Movement in net cash	**187.9**	(34.5)	**(21.5)**	30.1
Movement in debt arising from cash flows	**(326.9)**	(3.4)	**-**	-
Movement in net (debt)/funds arising from cash flows	**(139.0)**	(37.9)	**(21.5)**	30.1
Movement in accrued interest	**(1.6)**	(1.0)	**0.2**	-
Indexation of index-linked debt	**(55.3)**	(30.5)	**-**	-
Other non-cash movements	**(0.1)**	-	**-**	-
Movement in net (debt)/funds during the year	**(192.8)**	(69.4)	**(21.3)**	30.1
Net (debt)/funds at end of year	**(3,070.3)**	(2,877.5)	**8.8**	30.1

NOTES TO THE FINANCIAL STATEMENTS

20. EMPLOYEES AND DIRECTORS

Staff costs for the Group during the year

	2018 £m	2017 £m
Wages and salaries	**124.7**	110.8
Social security costs	**13.0**	10.8
Other pension costs	**12.7**	12.8
	150.4	134.4

Of the above, £53.8m (2017: £48.3m) has been capitalised, being the investment cost of employees' work on the capital programme.

	2018	2017
Average monthly number of people employed by the Group (including Executive Directors)	**Number**	Number
Regulated water and sewerage activities	**3,387**	3,091

For further information see the Remuneration Report on page 75.

No remuneration was paid or is payable by the parent company. The directors are employed by other companies in the Group and consider their duties to this company incidental to their other activities within the Group. The parent company had no employees during the period other than the directors.

21. PENSION COMMITMENTS

The Group operates a funded defined benefit pension scheme (based on final pensionable salary and pensionable service), the DCWW Pension Scheme. The assets of the scheme are held in a separate trustee-administered fund.

The DCWW Pension Scheme was closed to new members from 31 December 2005 and closed for future accruals from 1 April 2017. A new defined contribution scheme, the Dŵr Cymru Defined Contribution Scheme, was introduced from 1 January 2006.

Defined benefit scheme
A full actuarial valuation of the scheme was undertaken as at 31 March 2016 by Joanne Eynon of Quantum Advisory, an independent, professionally qualified actuary, using the projected unit method. This valuation has been updated as at 31 March 2018 and the principal assumptions made by the actuaries were:

	2018	2017
Discount rate	**2.8%**	2.8%
Inflation assumption	**3.1%**	3.2%
Rate of increase in pensionable salaries	**3.1%**	3.2%
Rate of increase in pensions in payment	**3.0%**	3.1%
Post retirement mortality (life expectancy)		
- Current pensioners aged 65 - males	**87.1 years**	87.0 years
- Current pensioners aged 65 - females	**89.1 years**	89.0 years
- Future pensioners aged 65 (currently aged 45) - males	**88.4 years**	88.3 years
- Future pensioners aged 65 (currently aged 45) - females	**90.6 years**	90.5 years

The mortality assumptions are the S2PxA base tables with future improvements in line with the CM1 2016 projection model with a long term trend rate of 1% p.a.

Changes in the defined benefit obligation are as follows:

	2018 £m	2017 £m
At 1 April	**497.3**	413.1
Current service cost	**0.3**	4.8
Interest expense	**13.5**	14.5
Remeasurement: (gain)/loss from change in financial assumptions	**(8.7)**	90.3
Benefits paid	**(28.3)**	(25.4)
At 31 March	**474.1**	497.3

Changes in the fair value plan assets are as follows:

	2018 £m	2017 £m
At 1 April	**404.9**	358.6
Interest income	**11.0**	12.7
Expenses	**-**	(0.4)
Experience gains	**3.5**	47.0
Contributions	**6.9**	12.4
Benefits paid	**(28.3)**	(25.4)
At 31 March	**398.0**	404.9

Experience gains and losses are differences between the actual events as they have turned out and the assumptions that they were made as at the date of the earlier actuarial valuation and changes in the actuarial assumption during the year.

	2018 £m	2017 £m
Present value of funded obligations	**(474.1)**	(497.3)
Fair value of plan assets	**398.0**	404.9
	(76.1)	(92.4)
EFRBS unfunded liability	**(4.3)**	(2.8)
Net defined benefit liability recognised in the balance sheet	**(80.4)**	(95.2)

The contributions paid in the year to 31 March 2018 include special contributions of £6.7m (2017: £7.2m). The special contributions expected to be paid in line with the extant schedule of contributions during the financial year ending 31 March 2019 amount to £6.7m (2017: £6.7m).

	Change in assumption	Movement in liabilities
Discount rate	0.10%	£8.9m
Price inflation	0.10%	£8.7m
Life expectancy	1 year	£12.5m

The above sensitivity analysis is based on isolated changes in each assumption whilst holding all over assumption constant. In practice, this is unlikely to occur, and there is likely to be some level of correlation between the movements in different assumptions.

EFRBS

During 2011, the Company put arrangements in place via an Employer-Financed Retirement Benefit Scheme (EFRBS) for four 'capped' Executive Members of the scheme. The accrual of benefits under this agreement is conditional on remaining a member of the DCWW Pension Scheme. At 31 March 2018, there were three Executive Members with entitlements under this arrangement, one of whom has commenced the receipt of his benefits.

22. BUSINESS COMBINATIONS

On 19 December 2017, the Group acquired 100% of the share capital of Kelda Organic Energy Limited for £150,000. On the same date, the Group also acquired 100% of the share capital of Kelda Organic Energy (Cardiff) Limited for £350,000. These companies' names were changed, on 8 January 2018, to Welsh Water Organic Energy Limited and Welsh Water Organic Energy (Cardiff) Limited respectively. WWOE operates a Public Private Partnership Concession Contract with the City of Cardiff Council and the Vale of Glamorgan Council for food and green waste treatment and recycling and WWOE(C) operates and maintains an anaerobic digestion food waste facility and a green waste composting facility in Cardiff.

As a result of these acquisitions, the Group is expected to secure electricity production for its Cardiff Wastewater Treatment Works, increase collaboration with Cardiff Council and explore new avenues in energy production.
An intangible asset of £316,011 arising from the acquisition is attributable to the value of the contract with the Councils.

The following tables summarise the considerations paid for WWOE and WWOE(C), the fair value of assets acquired and liabilities assumed at the acquisition date:

Consideration at 19 December 2017	**WWOE** £000	**WWOE(C)** £000
Cash	150	350
Total consideration	150	350

Fair value of recognised amounts of identifiable assets acquired and liabilities assumed	**WWOE** £000	**WWOE(C)** £000
Cash and equivalents	-	-
Property, plant and equipment	17,138	170
Trade and other receivables	174	496
Trade and other payables	(544)	(109)
Intercompany loan	(17,438)	-
Deferred tax assets	122	175
Total identifiable net (liabilities)/assets	(548)	732
Intangible asset	698	(382)
Total	150	350

Welsh Water Organic Energy Limited
Acquisition-related costs of £703,000 have been charged to operating expenses in the consolidated income statement for the year ended 31 March 2018.

The fair value of trade and other receivables is £174,000 and includes trade receivables with a fair value of £160,000. The gross contractual amount for trade receivables due is £160,000, of which £nil is expected to be uncollectable.

The revenue included in the consolidated statement of comprehensive income since 19 December 2017 contributed by WWOE was £360,000. WWOE also contributed a loss before tax of £67,000 over the same period.

Had WWOE been consolidated from 1 April 2017, the consolidated statement of income would show pro-forma revenue of £3,218,000 and a loss before tax of £871,000.

Welsh Water Organic Energy Cardiff
Acquisition-related costs of £301,000 have been charged to operating expenses in the consolidated income statement for the year ended 31 March 2018.

The fair value of trade and other receivables is £697,953 and includes trade receivables with a fair value of £52,684. The gross contractual amount for trade receivables due is £52,684, of which £nil is expected to be uncollectable.

The revenue included in the consolidated statement of comprehensive income since 19 December 2017 contributed by WWOE(C) was £157,823. WWOE(C) also contributed a loss before tax of £529,199 over the same period.

Had WWOE(C) been consolidated from 1 April 2017, the consolidated statement of income would show pro-forma revenue of £520,740 and a loss before tax of £1,907,817.

23. CAPITAL AND OTHER FINANCIAL COMMITMENTS

The Group's business plan at 31 March 2018 shows net capital expenditure and infrastructure renewals expenditure of £478m (2017: £406m) during the next financial year. While only a portion of this amount has been formally contracted for, the Group is effectively committed to a majority of the total as part of the capital investment programme approved by its regulator, Ofwat.

24. RELATED PARTY TRANSACTIONS

In accordance with the exemption afforded by IAS 24 there is no disclosure in the consolidated financial statements of transactions with entities that are part of the Glas Cymru Holdings Cyfyngedig Group.

The parent company issued an intercompany loan to Welsh Water Holdings Limited, a wholly-owned subsidiary, during the year, the balance of which stood at £21,553,702 as at 31 March 2018 (no repayments were made during the year). Interest is chargeable at a fixed rate of 5% and £286,194 was charged during the year.

During the period ended 31 March 2017 the parent company received dividends totalling £30.2m from its wholly-owned subsidiary, Glas Cymru Anghyfyngedig.

25. STATUS OF THE COMPANY

The Company is limited by guarantee and does not have any share capital. In the event of the Company being wound up, the liability of the Members is limited to £1 each.

26. ELAN VALLEY TRUST FUND

In 1984 Welsh Water Authority entered into a conditional sale and purchase agreement with Severn Trent Water Authority for the sale of the aqueduct and associated works by which the bulk supply to Severn Trent reservoirs is conveyed.

The sum of £31.7m, representing the consideration for the conditional sale, was invested in a trust fund. The principal function of the fund was to provide an income to Welsh Water Authority, whilst preserving the capital value of the fund in real terms. Welsh Water Authority's interest in this fund was vested in Dŵr Cymru Cyfyngedig under the provisions of the Water Act 1989.

The assets of the fund are not included in these financial statements. As at 31 March 2018 the market value of the trust fund was £115m (2017: £118m).

Interest receivable includes £2.8m (2017 £2.7m) in respect of distributions from the Elan Valley Trust Fund.

27. CONTINGENT LIABILITIES

There were no contingent liabilities other than those arising from in ordinary course of the Group's business and in respect of these no material losses are anticipated.

28. IMMEDIATE AND ULTIMATE HOLDING COMPANY AND CONTROLLING PARTY

The immediate and ultimate holding company and controlling party is Glas Cymru Holdings Cyfyngedig, a company registered in England and Wales on 15 December 2015, company number 09917809, registered office Pentwyn Road, Nelson Treharris CF46 6LY. The largest and smallest group with in which the results of the company are consolidated is that headed by Glas Cymru Holdings Cyfyngedig.

APPENDICES

GLOSSARY

Abstraction	The removal of water from any source.
AMP	The water industry operates on five-yearly cycles called 'Asset Management Plans'. AMP6 will run from 2015-2020.
Anaerobic digestion	A process by which organic material is broken down by bacteria and other micro-organisms to generate renewable energy.
Assets	These include infrastructure such as water mains and sewers, dams and reservoirs, water and sewage treatment works, pumping stations, company laboratories, depots and workshops.
AVPS	Annual Variable Pay Scheme – a performance related element of emoluments.
Bacteriological failures	The drinking water supplied to customers is sampled and analysed against a range of chemical and bacteriological parameters. If a sample shows a bacteriological parameter that exceeds the limit specified in the regulations, it is deemed a bacteriological failure.
Catchment	An area of land through which water drains into a body of water (such as a river or reservoir).
Combined sewer	Combined sewer for sewage and rain water runoff.
CSO	Combined Sewer Overflows act as relief valves which prevent the overloading of sewers which could otherwise lead to flooding of properties and sewage treatment works.
Company limited by guarantee	A private company that does not have shareholders or share capital.
CPNI	Centre for the Protection of National Infrastructure.
CCWater	Consumer Council for Water – see page 42.
Credit rating	Credit ratings provide an assessment of the credit quality of a company which can affect the cost of borrowing.
Customer Payment Account	The Customer Payment Account (as defined by the Common Terms Agreement) is the allocation of Customer Reserves used specifically for rebates to customers.
Customer Reserves	Customer Reserves is the difference between the RCV and net debt and is therefore a measure of the value created by the business for customers. Some of that value can be used for investment in the business and rebates to customers. We aim to maintain net debt at around 60% of the RCV with retained Customer Reserves as the remaining 40%.
Discharge permits	Legal agreements issued by the environmental regulator relating to the amount, quality and frequency of wastewater that can be returned to the environment.
DWI	Drinking Water Inspectorate – see page 42.
Drinking Water Safety Plan	This is a proactive method of assessing risk to drinking water quality, which better protects public health.
Drought plan	Statutory plan produced by a water company that details the actions to be taken to manage the supply of water in a drought.
Effluent	Water that flows from a sewage treatment plant after it has been treated.
Environment Agency (EA)	An executive, non-departmental Government body that has a statutory duty to protect and enhance the environment in England – see page 42.

Financeability	The ability of appointed water companies to finance their functions through debt, equity or retained earnings.
Gearing	Net debt expressed as a percentage of regulatory capital value.
Glas Cymru	Glas Cymru is the generic name used to refer to the Group holding company. Glas Cymru Cyfyngedig was formed in 2000 to own, finance, and manage Dŵr Cymru Welsh Water. During 2015/16 Glas Cymru Cyfyngedig was reregistered as Glas Cymru Anghyfngedig and Glas Cymru Holdings Cyfyngedig was created to be the holding company for the Glas Cymru Group.
Groundwater	Water that can be found in the saturated zone of the soil.
Group	Glas Cymru and all its subsidiaries.
ICT	Information and communications technology.
Leakage	Water lost between the treatment works and the customer's home or business.
Let's Stop the Block	Behavioural change campaign being undertaken by Welsh Water which asks customers to help reduce the number of sewer blockages.
LVPS	Long-term Variable Pay Scheme. A performance related element of emoluments.
'Look-up' Compliance	This is where a wastewater treatment works fails to meet the consented parameters set by the NRW or EA for less than 95% of the time.
Mean Zonal Compliance (MZC)	Mean Zonal Compliance is a measure of compliance in all the water quality zones for 39 key chemical and bacteriological parameters derived from the statutory monitoring programme of samples taken from customers' taps.
Megalitres	One megalitre is equal to 1,000 cubic metres or one million litres. A standard Olympic-size swimming pool contains 2.5 megalitres of water.
Natural Resources Wales (NRW)	Welsh Government sponsored body whose purpose it is to ensure that the natural resources of Wales are sustainably maintained, enhanced and used.
Non-Executive Directors	Members of Glas Cymru's Board. Non-Executive Directors are not responsible for the day-to-day running but challenge management and oversee the running of the Group.
ODI	Outcome Delivery Incentive – This is the mechanism for rewards and penalties which underpins the performance measures set out in our Final Determination Ofwat PR14 business plan.
Ofwat	The economic regulator of the water sector in England and Wales.
Operating costs	Total operating expenditure of the business, net of any operating income, primarily any profits or losses on the disposal of fixed assets.
Pollution Incidents	An accidental or deliberate release of contaminants such as oils, fuels and chemicals that can be harmful to human health and the environment.
Private Sewer Transfer (PST)	In 2011-12, the UK Government transferred ownership of most of the private sewers in England and Wales to the 10 water and sewerage companies, to form part of the public sewer network.
Pumping station	Used to pump water or sewerage from one place to another.
Quality and Environment Committee (QEC)	Board level Committee in Glas Cymru which addresses performance and operational risk issues across the company.
RainScape	Glas Cymru's approach to managing surface water and overloaded sewers (sustainable urban drainage systems).
Real terms	This means the change in a financial number after removing the effect of inflation.

Regulatory Capital Value (RCV)	The asset value of Dŵr Cymru, determined by Ofwat, on which our investment returns (or Regulatory Returns) is allowed to be made. This is, in effect, a proxy for the economic value in use of the appointed business of Dŵr Cymru Cyfyngedig.
Reservoir	A natural or artificial lake where water is collected and stored until needed.
Rising main	A pumped pipeline that carries wastewater.
Scorecard	A statistical record used by Welsh Water to measure achievement or progress towards a particular goal.
Security and Emergency Measures Directive (SEMD)	Issued by Welsh Government and DEFRA to the water sector to provide guidance on how to respond to major incidents.
Service Incentive Mechanism (SIM)	This is an Ofwat measure designed to improve the level of customer service that water companies provide.
Service reservoir	This is a tank containing drinking water that is usually sited within or near to a water distribution system.
Serviceability	The capability of a system of assets to deliver an expected level of service to consumers and to the environment now and into the future.
Sewer	An underground pipe that takes household and non-household wastewater and surface water away from properties for treatment and disposal.
Sewer flooding	Occurs when wastewater escapes from sewer pipes through a manhole cover or a drain, or by backing up through toilets.
Safety Takes Every Person (STEP)	Behavioural safety training which emphasises that each individual has responsibility for Health and Safety issues.
SSSI	Site of Special Scientific Interest
Storm tank	A tank into which, in wet weather, stormwater and wastewater is stored until the wastewater treatment works can treat it.
Supply/demand balance	The balance of the volume of water available.
Surface water	Run-off from rainwater that falls onto customers' properties (such as roofs, paths and driveways).
Surface water drainage	The removal of rainwater, snow or melted ice from exterior areas of a property (such as roofs and driveways) often to a surface water sewer or combined sewer.
Sustainable Urban Drainage (SUDS)	A sustainable drainage system is designed to reduce the potential impact of new and existing developments with respect to surface water drainage discharges.
Totex	An Ofwat abbreviation for total expenditure. The total sum of capital expenditure and operational expenditure.
Trunk main	A main through which water is fed into a water distribution system. A trunk main will often run from a water treatment works to a service reservoir.
Wastewater	Waste matter from household or non-household properties that is carried away from properties in sewers or drains.
Wastewater treatment works (WWTW)	Wastewater treatment works are designed to remove biological or chemical waste products from water before it is returned to water sources.
Water main	A large pipe that carries treated water to households.
Water Resource Management Plan (WRMP)	This outlines how a water company will maintain a sustainable balance between water supplies and demand over the next 25 years.
Water treatment works (WTW)	Water treatment plants produce drinking water for public consumption or industrial water for manufacturing or other business operations.

MEASURES OF SUCCESS: DEFINITIONS

A1a	**Safety of Drinking Water (% compliance)**	Provide safe drinking water that meets the Drinking Water Inspectorate's standards. The percentage of the sample tests that are compliant with the standards. We take over 250,000 samples tests per year at our water treatment works, service reservoirs and at customer taps.
A1b	**Safety of Drinking Water (Mean Zonal Compliance)**	Mean Zonal Compliance is published annually in the Drinking Water Inspectorate (DWI) report. The MZC covers 39 different parameters such as Iron, Lead and Aluminium, which are tested to establish the quality of water as received by customers. MZC is calculated as the average of the compliance levels for each parameter in each of our 87 water quality zones, which range in size from 27 population to almost 100,000 population. (The maximum allowable population is any one water quality zone is 100,000 allowable within the DWI regulations).
A2	**Customer acceptability**	The number of contacts received from customers in the year regarding the appearance, taste or odour of drinking water, expressed as a rate per 1,000 customers.
A3	**Reliability of Supply**	The average number of minutes that customers are without water within our supply area (includes both planned and unplanned interruptions)
B1	**Abstraction for water for use**	The percentage compliance with our abstraction licences, as issued by Regulators.
B2	**Treating wastewater**	For each of our wastewater treatment works there is a permit which regulates the quality of wastewater the company is allowed to discharge into rivers and coastal waters, which is regulated by the NRW. The measure is the % compliance against the discharge permits.
B3a	**Preventing pollutions (cat 1,2&3)**	Reduce the number of pollution incidents (caused by blockages or collapsed sewers). Pollution incidents are categorised as category 1, 2 or 3 incident and reported by Natural Resources Wales and the Environment Agency. Category 1 – the most severe and have a major or serious impact on the environment, people or property. Category 2 – significant impact or effect on the environment, people or property. Category 3 – minor or minimal impact on the environment, people or property.
B3b	**Preventing pollutions (cat 3 only)**	As above but only category 3 pollution incidents (minor or minimal impact on the environment, people or property).
C1	**Responding to climate change**	Reduce the amount of rainwater entering our sewers. The measure is the volume of surface water removed from the system, expressed as the number of equivalent properties.

C2	**Carbon footprint**	To generate more renewable energy and therefore to offset our carbon emissions and the cost of imported energy (GWh hours per year).
D1	**SIM**	Service incentive mechanism (SIM) is a measure introduced by the Regulator Ofwat to monitor and report customer service information across all water & wastewater companies as a comparative measure.
D2	**At Risk Customer Service**	The number of customers who are on our register of "at risk". They are deemed to be "at risk" because their service has repeatedly fallen short in one of the following five areas: discolouration of water, interruptions to supply, low pressure, odour from wastewater assets and sewer flooding.
D3	**Properties flooded in the year**	The number of properties suffering internal sewer flooding per year.
D4a	**Business Customer Satisfaction % satisfied**	Business customer satisfaction as measured by either satisfied or very satisfied in the six monthly survey undertaken.
D4b	**Non Household Customer Satisfaction**	Business customer satisfaction as measured by the average customer score out of a total of 5 then converted to a percentage.
D5	**Earning the Trust of Customers**	Customer trust as measured in an annual survey we undertake.
E1	**Affordable Bills**	The company will continue to make bills more affordable by maintaining falling bills in real terms, beating inflation by around 1% a year.
E2	**Help for Disadvantaged customers**	Help more customers who genuinely struggle to pay their bills by providing assistance through a range of social tariffs and our Customer Assistance Fund.
F1	**Asset Serviceability**	Maintain our assets. Serviceability includes a basket of sub-measures used by Ofwat to monitor the effectiveness of our asset management and the maintenance of our assets.
F2	**Leakage**	Reduce our leakage levels – megalitres per day (Ml/d).
F3	**Asset Resilience**	Improve the resilience score of our most strategic assets. Improve the percentage of strategic assets that are resilient against a set of criteria. Strategic assets are those where failure would have a major impact on service to customers or on the environment.
G1	**RIDDOR Incidents**	This is the total number of injuries reported each year to the Health and Safety Executive under the Reporting of Injuries, Diseases and Dangerous Occurrences Regulations 2013 (RIDDOR). It includes injuries that occur across the wholesale and retail businesses, as well as those involving our main contractors and capital partners.
G2	**Competence in Role**	We have a "Progression in Role" framework and have established clear role profiles that define key criteria which we use to measure individuals' knowledge, skills and competence to undertake their respective roles. Our objective is that by 2020 (and ongoing beyond that) 95% of the outlined key roles will be deemed competent (with the remainder being new starters in training).
H1	**Financing Efficiency (credit rating)**	The rating ascribed by the three main rating agencies: S&P, Moody's and Fitch.

Glas Cymru Holdings Cyfyngedig
Company Number: 09917809