Independent auditor's report to the members of Pennon Group plc

Opinion

In our opinion:

- Pennon Group plc's group financial statements and parent company financial statements (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 2020 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006, and, as regards the Group financial statements, Article 4 of the IAS Regulation.

We have audited the financial statements of Pennon Group plc which comprise:

Group	Parent Company
Consolidated Balance sheet as at 31 March 2020	Balance sheet as at 31 March 2020
Consolidated income statement for the year then ended	Statement of changes in equity for the year then ended
Consolidated statement of comprehensive income for the year then ended	Cash flow statement for the year then ended
Consolidated statement of changes in equity for the year then ended	Related notes 1 to 47 to the financial statements, including a summary of significant accounting policies
Consolidated cash flow statement for the year then ended	
Related notes 1 to 47 to the financial statements, including a summary of significant accounting policies	

The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the Parent Company financial statements, as applied in accordance with the provisions 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 under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report below. We are independent of the Group and Parent Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to principal risks, going concern and viability statement

We have nothing to report in respect of the following information in the annual report, in relation to which the ISAs(UK) require us to report to you whether we have anything material to add or draw attention to:

- the disclosures in the annual report set out on pages 58 to 67 that describe the principal risks and explain how they are being managed or mitigated;
- the directors' confirmation set out on page 59 in the annual report that they have carried out a robust assessment of the principal risks facing the entity, including those that would threaten its business model, future performance, solvency or liquidity;
- the directors' statement set out on page 119 in the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them, and their identification of any material uncertainties to the entity's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements
- whether the directors' statement in relation to going concern required under the Listing Rules in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit; or
- the directors' explanation set out on page 68 in the annual report as to how they have assessed the prospects of the entity, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the entity 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.

Overview of our audit approach

Key audit matters	• Revenue recognition, specific to accrued income and IFRIC 12 revenue – Group • Valuation of landfill related provisions – Viridor • Valuation of the provision for doubtful debts – SWW • Valuation of the receivable related to the Interserve claim – Viridor
Audit scope	• We performed an audit of the complete financial information of three components and audit procedures on specific balances for one component. • The components where we performed full or specific audit procedures accounted for 100% of Profit before taxation before non-underlying items, 100% of Revenue and 95% of Total assets.
Materiality	• We set overall group materiality at £14.3 million, which represents 5% of the sum of the profit before taxation before non-underlying items and profit before taxation before non-underlying items from discontinued operations.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included 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 our opinion thereon, and we do not provide a separate opinion on these matters.

Risk

Revenue recognition, specific to accrued income and IFRIC 12 revenue – Group statutory (£636.7 million, PY comparative £632.6 million, discontinued £753.2 million, PY comparative £845.6 million)

Risk direction

Refer to the Audit Committee Report (page 86); Accounting policies (pages 138 to 140); and Note 5 of the Consolidated Financial Statements (page 150)

The Group's material revenue streams relate to the provision of water and sewerage services by South West Water and Pennon Water Services and revenue generated from the renewable energy, recycling and waste management services provided by Viridor. ISAs (UK) presume that there is a risk of fraud relating to revenue recognition. For the Group, given targets associated with financial performance and pressures to meet market expectations, there is an incentive to overstate revenue. This risk over revenue recognition specifically arises in the following judgemental areas, where there is opportunity to overstate revenue:

South West Water and Pennon Water Services Group - statutory (£636.7 million, PY comparative £632.6 million)

Income from measured water services requires an estimation of the amount of unbilled charges at the year end. This is calculated using a combination of system generated information, based on previous customer volume usage, together with management judgement as to the likely impact on usage of factors such as recent weather patterns. The accrued income balance at 31 March 2020 is £83.9 million (2019: £89.8 million) for South West Water and £26.3 million (2019: £28.9 million) for Pennon Water Services.

Viridor – discontinued (£753.2 million, PY comparative £845.6 million)

Calculations of accrued income on waste management contracts and powergen revenue to be received involve estimation by management. The accrued income balance at 31 March 2020 is £51.2 million (2019: £53.3 million).

Accounting for revenue from long term service concession arrangements under IFRIC 12 requires revenue to be recognised on construction, during service delivery and as a capital return on the asset. The determination of the margin allocated during the different phases of each service concession involves management judgement. At 31 March 2020 the Group has recognised contract receivables of £202.4 million (2019: £188.3 million) and other intangible assets of £86.9 million (2019: £90.6 million), related to service concession arrangements (refer to Note 46).

Our response to the risk

Our procedures included:

South West Water and Pennon Water Services

- We obtained an understanding of the process for the supply of measured services, meter reading and related billing in order to assess the completeness of the accrual for revenue at the year end;
- We tested key controls linked to system generated information and around the estimation process for measured revenue;
- We corroborated the key assumptions and estimates made by management in recognising revenue, by obtaining internal and external data on factors that influence demand from customers, such as weather patterns and leaks in infrastructure networks;
- We performed analytical procedures by comparing revenue balances for the year against expectations and obtained support for significant variances; and
- In performing our journal testing, we paid increased attention to entries impacting revenue, focusing on non-system postings and those raised in the last two weeks of the year.

Viridor

- We compared the key assumptions and estimates made by management in recognising accrued revenue in the current year to those applied in the prior year to identify significant changes;
- We analysed revenue trends and evaluated unusual movements to assess the accuracy of the accrued income balance;
- We obtained customer confirmations for a sample of revenue;
- For material items, within accrued income, we reperformed the calculation of the income that had been earned on waste management contracts and powergen revenue to confirm the accuracy of the accrued income recorded by management;
- We tested the application of the IFRIC 12 revenue recognised and assessed the allocation of consideration between the construction and operating services provided;
- We considered whether the revenue recognition policies adopted comply with IFRS, in particular the requirements of IFRIC 12. Specifically, we considered whether the margins used to recognise revenue were appropriate, through testing that costs were allocated to the correct contracts and that revenue recognised, based on those costs, was reasonable and aligned with the individual contract models. We also compared the margins to those generated in prior years and to the latest projections for future years; and
- In performing our journal testing, we paid increased attention to entries impacting revenue, particularly those raised close to the balance sheet date.

We performed full and specific scope audit procedures over this risk area for three components, which covered 100% of the risk amount.

Key observations communicated to the Audit Committee

South West Water and Pennon Water Services

We concluded that the estimation process undertaken by management to calculate the measured income accrual reflected latest operational factors in the key assumptions that the income accrual was appropriately determined.

Viridor

We concluded that accrued income had been recognised appropriately in accordance with IFRS and Viridor's accounting policy, and that IFRIC 12 had been applied appropriately.

Independent auditor's report to the members of Pennon Group plc
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Risk	Our response to the risk	Key observations communicated to the Audit Committee
Valuation of landfill related provisions – Viridor (£201.2 million, PY comparative £209.6 million) **Risk direction** *Refer to the Audit Committee Report (page 86); Accounting policies (page 144); and Notes 32 and 46 of the Consolidated Financial Statements (pages 175 and 190)* Landfill related provisions of £201.2 million (2019: £209.6 million) are disclosed in Notes 32 and 46 and consist of aftercare, restoration and remediation provisions. Calculation of the aftercare provision involves significant judgement in respect of the expected period of aftercare, the level of costs to be incurred and the discount rates to be used. Key areas of estimation for the restoration provision include the expected restoration costs, the void space to be filled and timing of site closure. Judgement over the remedial action required to comply with current environmental legislation, where breaches have been identified, is a key estimate for the remediation provision. We focused on this area given there is a risk that provisions could be misstated due to the complexity of factors to be assessed and assumptions, such as discount rates, applied by management being inappropriate, including the impact of any management bias.	Our procedures included: • We tested the aftercare, restoration and remediation provision models, and verified that the models were arithmetically and logically accurate; • We evaluated the forecast costs in the models, agreeing these to supporting evidence such as budgets and supplier cost quotations and current performance, including prices charged by contractors in the current year for significant sites; • We assessed the material estimates made for evidence of management bias, including agreeing anticipated cost savings to detailed plans and current performance; • We benchmarked the discount and inflation rates applied, using our internal valuation experts to assist in our consideration of whether management's assumptions are within an acceptable range based on comparative market data; • We compared the key assumptions used in the calculation of the provisions, including the discount rates, inflation rates, void space and remaining lives of the sites, to available market information; • We compared the key assumptions used in the current models to those used in the prior year, and sought evidence that changes were appropriate. This included obtaining evidence to support the impact of future planned technological changes; • We performed sensitivity analysis on these key assumptions; and • We tested the appropriateness of journal entries impacting landfill related provisions, particularly those raised close to the balance sheet date. We performed full scope audit procedures over this risk area at Viridor, which covered 100% of the risk amount.	We concluded that management's real risk free rate of 2.175% applied to the most signifcant provision (aftercare) lies outside of an acceptable range (1.80% to 2.16%), but this has an immaterial effect on the provision balance. We concluded that the key assumptions supporting the landfill related provisions reflected management's reasonable best estimates, informed by latest external and internal data, and resulted in appropriately measured and recognised landfill-related provisions.

Risk	Our response to the risk	Key observations communicated to the Audit Committee
Valuation of the provision for doubtful debts – South West Water & Pennon Water Services (£105.5 million, PY comparative £95.5 million) **Risk direction** *Refer to the Audit Committee Report (page 86); Accounting policies (page 142); and included within the total Group balance per Note 22 of the Consolidated Financial Statements (page 164)* Both the South West Water provision of £91.0 million (2019: £86.8 million) and Pennon Water Services provision of £14.5 million (2019: £8.7 million) are calculated using a combination of system generated information on historic debt recovery rates and management's judgement of the future likely recovery rates. Within the current year the provisions were calculated using the normal methodology, and then a further assessment was made to reflect on the risks arising from the ability to collect in future as a result of the economic impact of the COVID-19 pandemic. This resulted in an additional provision of £2.8 million for South West Water and £5.0 million for Pennon Water Services (these amounts are included in the total figures noted above). There is a risk that the assumptions used by management in calculating the bad debt provision may be susceptible to management bias and the valuation of the provision against trade receivables may be misstated. We have therefore focused on this key audit matter. We have shown the risk direction as increasing, reflecting the issues arising from COVID-19 and have also expanded the risk to the PWS component, as the PWS customer base is non household and has been impacted to a greater extent by COVID-19.	Our procedures included: • We performed a walkthrough of the process for calculating the bad debt provision and assessed the design effectiveness of relevant key controls; • We tested the operating effectiveness of the relevant key controls over the integrity of data and the report utilised to generate the ageing and categorisation of debt within South West Water's and Pennon Water Services's billing systems; • We tested historic data on collection rates and evaluated how this data was used in the preparation of the bad debt provision; • We validated the assumptions used by management in determining the amounts provided against the different categories and age of debt, by comparing these assumptions to historic collection rates and by considering the impact of changes in the methods adopted operationally by management to collect debt, and in the external environment; • For South West Water, we utilised collection information over the past three years, to determine a range of the likely ultimate collection of debts existing at the balance sheet date and compared this to the provision recorded by management, including assessing assumptions for evidence of management bias; • We tested management's scenario analysis of the impact of COVID-19 on collection of trade receivables to supporting evidence. This included consideration of information on collections performance in previous recessions, the segmentation of customer base by employment group for household customers and business group for non household customers, together with information on actual collections since the balance sheet date; and • We tested the appropriateness of journal entries and adjustments impacting the doubtful debt provision, particularly those raised close to the balance sheet date. We performed full scope audit procedures over this risk area at South West Water and Pennon Water Services, which covered 100% of the risk amount for these components components and covered 100% of the Group debtors balance shown in Note 22 which excludes receivables relating to Viridor which are shown in Note 46.	We have concluded that the South West Water doubtful debt provision of £91.0 million is within an acceptable range and reflects the recent history of collection of outstanding debts and considerations of the impact on future collections of the economic environment arising from COVID-19. We have also concluded that the Pennon Water Services's provision, including the additional provision relating to COVID-19 of £5.0 million, is appropriate.
Valuation of the receivable related to the Interserve claim – Viridor **Risk direction** *Refer to the Audit Committee Report (page 86); Critical accounting judgements (page 149); and Note 46 of the Consolidated Financial Statements (page 190)* Viridor contracted with Glasgow City Council to construct a Recycling and Renewable Energy Centre in Glasgow. Viridor terminated the contract with the original principal contractor in November 2016 and has overseen the remaining construction. Expenditure to complete construction is expected to exceed the original target and management has accounted for what it believes its contractual rights are. Contract claims as at 31 March 2020 amounted to £72.0 million (2019: £72.0 million). Management recognised a provision against the claims as at 31 March 2020 of £28.3 million (2019: £28.7 million), resulting in a net receivable of £43.7 million (2019: £43.3 million). We focused on this area given there is risk of challenge of the legal position taken and greater judgement involved in assessing the collectability of amounts recorded.	Our procedures included: • We obtained an understanding of the key assumptions and estimates made by management in accounting for thel claim, assessing whether there was evidence of management bias and concluding on whether we concurred with the accounting estimates made by management; • We obtained an update, from management and Group legal, to understand the latest position of the claim as at the year end date; • We inspected the contractual documentation and relevant clauses of the contract for evidence of the entitlement to receive financial compensation; • We inspected the external legal advice/opinion management had obtained in relation to contract positions, quantum of costs and amounts recoverable; • We inspected any available external data, market announcements, financial reports and correspondence between Viridor and Interserve, to assess the recoverability of amounts due from Interserve and whether the reserve recognised reflects an appropriate level of provision; • We inquired of management and assessed other evidence, including board minutes, to test the completeness of amounts recorded in relation to contract claims; and • We read the disclosures made by management in Note 4 'Critical accounting judgements and estimates' in the Annual Report and Accounts, and evaluated the adequacy of these. We performed full scope audit procedures over this risk area in one location, which covered 100% of the risk amount.	We have concluded that the accounting criteria for asset recognition have been met and that the position taken by management, including the recoverability of amounts due from Interserve, is appropriate and is based on supporting legal and financial analysis. We concluded that the disclosures in this key judgement, including the possible range of outcomes, in the Annual Report and Accounts are appropriate.

The key audit matters for the current year are consistent with matters included in our prior year auditor's report, with the exception of the extension of the provision for doubtful debts also to relate to PWS as well as SWW in light of COVID-19.

Independent auditor's report to the members of Pennon Group plc
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An overview of the scope of our audit

Tailoring the scope
Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each entity within the Group. Taken together, this enables us to form an opinion on the consolidated financial statements. We take into account size, risk profile, the organisation of the Group and effectiveness of group-wide controls, changes in the business environment and other factors such as recent Internal audit results when assessing the level of work to be performed at each entity.

In assessing the risk of material misstatement to the Group financial statements, and to ensure we had adequate quantitative coverage of significant accounts in the financial statements, of the six reporting components of the Group, we selected four components covering Pennon Group plc, Viridor, South West Water and Pennon Water Services, which represent the principal business units within the Group.

Of the four components selected, we performed an audit of the complete financial information of three components ("full scope components") which were selected based on their size or risk characteristics. For the remaining one component ("specific scope component"), we performed audit procedures on specific accounts within that component that we considered had the potential for the greatest impact on the significant accounts in the financial statements either because of the size of these accounts or their risk profile.

The reporting components where we performed audit procedures accounted for 100% (2019: 100%) of the Group's Profit before taxation before non-underlying items from both continuing and discontinued operations, 100% (2019: 100%) of the Group's Revenue from continuing and discontinued operations and 95% (2019: 95%) of the Group's Total assets. For the current year, the full scope components contributed 100% (2019: 100%) of the Group's Profit before taxation before non-underlying items from both continuing and discontinued operations, 87% (2019: 88%) of the Group's Revenue from continuing and discontinued operations and 95% (2019: 95%) of the Group's Total assets. The specific scope component contributed 0.4% (2019: -0.6%) of the Group's Profit before taxation before non-underlying items, 13% (2019: 12%) of the Group's Revenue from continuing and discontinued operations and 1% (2019: 1%) of the Group's Total assets. The audit scope of these components may not have included testing of all significant accounts of the component but will have contributed to the coverage of significant accounts tested for the Group.

Of the remaining two components that together represent less than 1% of the Group's profit before taxation before non-underlying items from continuing operations, none is individually greater than 1% of the Group's profit before taxation before non-underlying items from continuing operations. For these components, we performed other procedures, including analytical review procedures, testing of consolidation journals and intercompany eliminations to respond to any potential risks of material misstatement to the Group financial statements.

Involvement with component teams
In establishing our overall approach to the Group audit, we determined the type of work that needed to be undertaken at each of the components by us, as the primary audit engagement team, or by component auditors operating under our instruction. There are three key locations where we perform audit procedures for the Group and its components, being Exeter, Taunton and Bournemouth. The Pennon Group plc and South West Water accounting functions are based in Exeter and the audit teams of these components are led by the Senior Statutory Auditor. Separate teams audit the full scope component, Viridor, in Taunton, and the specific scope component, Pennon Water Services, based in Exeter and Bournemouth. Where the work was performed by component auditors, we determined the appropriate level of involvement to enable us to determine that sufficient audit evidence had been obtained as a basis for our opinion on the Group as a whole.

The primary team interacted regularly with the component teams where appropriate during various stages of the audit, reviewed key audit working papers on risk areas, attended key meetings with local management and were responsible for the scope and direction of the audit process. We maintained continuous and open dialogue with all component audit teams in addition to holding formal meetings to ensure that we were fully aware of their progress and results of their procedures. The Senior Statutory Auditor discussed the planned audit approach with the component teams and any issues arising from their work, attended meetings with local management, attending closing meetings and reviewing key audit working papers on risk areas. This, together with the additional procedures performed at Group level, gave us appropriate evidence for our opinion on the Group financial statements.

Subsequent to the development of COVID-19 pandemic, we revisited our risk assessment and planning to re-assess the risks in this context and held a planning session with Group and component teams. The primary team continued to interact regularly with the component teams during the post year end procedures.

The Senior Statutory Auditor continued to discuss the audit approach with the component teams and any issues arising from their work, attended meetings with local management, attended closing meetings and reviewed key audit working papers on risk areas. All of the above interactions were held remotely using audio-visual technology.

For all components, year-end review of relevant audit work papers was facilitated by the EY's electronic audit file platform, screen sharing or the provision of copies of work papers direct to the Group audit team.

Based upon the above approach we are satisfied that we have been able to perform sufficient and appropriate oversight of our component teams.

Our application of materiality
We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Materiality

The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined overall materiality for the Group to be £14.4 million (2019: £13.4 million), which is 5% (2019: 5%) of the sum of profit before taxation before non-underlying items and profit before taxation before non-underlying items from discontinued operations. We believe that profit before taxation before non-underlying items provides us with an appropriate measure of the underlying performance of the Group. We excluded non-underlying items on the basis that profit before taxation after non-underlying items is not indicative of the underlying performance of the Group. We also note that market and analyst commentary on the performance of the Group uses the same measure. We therefore considered profit before taxation before non-underlying items to be the most relevant performance metric on which to base our materiality calculation.

We determined overall materiality for the Parent Company to be £21.4 million (2019; £19.3 million), which is 1% of Equity. For balances relevant to the Group financial statements we have performed our procedures to a materiality to be in-line with the Group materiality.

Starting basis

Reported profit before taxation
£193.1 million (2019: £260.3 million)

Adjustments

– Profit before taxation on discontinued operations (Refer to Note 46) – £108.4 million (2019: £58.9 million)
– Non-underlying items (Refer to Note 6 decrease basis by £13.9 million (2019: £19.9 million increase)

Materiality

Totals £287.6 million (2019: £280.2 million) profit before taxation before non-underlying items.

Materiality of £14.4 million (5% of profit before taxation before non-underlying items)

Performance materiality

The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality was 75% (2019: 75%) of our planning materiality, namely £10.8 million (2019: £10.5 million). We have set performance materiality at this percentage based on our assessment of the Group's internal control environment and the extent and nature of audit findings identified in the prior period. This basis is consistent with the prior year.

Audit work at component locations for the purpose of obtaining audit coverage over significant financial statement accounts is undertaken based on a percentage of total performance materiality. The performance materiality set for each component is based on the relative scale and risk of the component to the Group as a whole and our assessment of the risk of misstatement at that component. In the current year, the range of performance materiality allocated to components was £3.7 million to £8.1 million (2019: £3.2 million to £9.5 million).

Reporting threshold

An amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £0.7 million (2019: £0.7 million), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

Impact of the COVID-19 pandemic

As a result of the ongoing COVID-19 pandemic, we have revisited our procedures in respect of the Directors' going concern assessment, taking into account the nature of the Group, its business model and related risks. We evaluated the Directors' assessment of the Group's ability to continue as a going concern, including the consistency of the cash flow forecasts, the key assumptions within the scenarios modelled and the available sources of liquidity with the findings from other areas of the audit. We assessed both the impact of additional sensitivities and the availability of mitigating future actions on the going concern assessment. We have also reviewed the disclosures contained within the Annual Report and consolidated financial statements in relation to this issue and consider them to describe adequately the impact of COVID-19 on the Group as at 31 March 2020.

The COVID-19 outbreak and lockdown restrictions occurred late in the Group's financial year and, as such, any audit procedures dependent on physical verification had either been completed, with the exception of stockcounts, and were subject to roll forward procedures or alternative procedures were performed. For stockcounts at the Viridor component, we performed virtual stockcounts. Subsequent to the travel restrictions being put in place, our post year end procedures for the Group and its components were completed remotely. We completed these procedures holding regular discussions with management to discuss the evidence, judgements and accounting. Where evidence comprised reports from systems, we utilised secure software collaboration facilities with management to observe the configuration used and repeat the extraction of reports from systems.

Other information

The other information comprises the information included in the annual report set out on pages 1 to 123, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Independent auditor's report to the members of Pennon Group plc
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In this context, we also have nothing to report in regard to our responsibility to specifically address the following items in the other information and to report as uncorrected material misstatements of the other information where we conclude that those items meet the following conditions:

- **Fair, balanced and understandable set out on page 120** – the statement given by the directors that they consider 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 performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or
- **Audit Committee reporting set out on pages 84 to 87** – the section describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee; or
- **Directors' statement of compliance with the UK Corporate Governance Code set out on page 73** – the parts of the directors' statement required under the Listing Rules relating to the company's compliance with the UK Corporate Governance Code containing provisions specified for review by the auditor in accordance with Listing Rule 9.8.10R(2) do not properly disclose a departure from a relevant provision of the UK Corporate Governance Code.

Opinions on other matters prescribed by 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.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements and those reports have been prepared in accordance with applicable legal requirements;
- the information about internal control and risk management systems in relation to financial reporting processes and about share capital structures, given in compliance with rules 7.2.5 and 7.2.6 in the Disclosure Rules and Transparency Rules sourcebook made by the Financial Conduct Authority (the FCA Rules), is consistent with the financial statements and has been prepared in accordance with applicable legal requirements; and
- information about the company's corporate governance code and practices and about its administrative, management and supervisory bodies and their committees complies with rules 7.2.2, 7.2.3 and 7.2.7 of the FCA Rules.

Matters on which we are required to report by exception
In the light of the knowledge and understanding of the Group and the Parent Company and its environment obtained in the course of the audit, we have not identified material misstatements in:

- the strategic report or the directors' report; or
- the information about internal control and risk management systems in relation to financial reporting processes and about share capital structures, given in compliance with rules 7.2.5 and 7.2.6 of the FCA Rules

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

- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent Company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- a Corporate Governance Statement has not been prepared by the company.

Responsibilities of directors
As explained more fully in the directors' responsibilities statement set out on page 120, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for 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 the directors either intend to liquidate the Group or the Parent Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

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 an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a 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 the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

The objectives of our audit, in respect to fraud, are; to identify and assess the risks of material misstatement of the financial statements due to fraud; to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud, through designing and implementing appropriate responses; and to respond appropriately to fraud or suspected fraud identified during the audit. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management.

Our approach was as follows:

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the group and determined that the most significant are:
  - Companies Act 2006
  - Financial Reporting Council (FRC) and the UK Corporate Governance Code
  - Tax legislation (governed by HM Revenue & Customs)
  - Health and Safety legislation
  - Environment Agency environmental permits
  - Ofwat regulations
  - UK listing rules
- We understood how Pennon Group plc is complying with those frameworks by reading internal policies and codes of conduct and assessing the entity level control environment, including the level of oversight of those charged with governance. We made enquiries of the Group's legal counsel, regulatory team and internal audit of known instances of non-compliance or suspected non-compliance with laws and regulations. We corroborated our enquiries through review of correspondence with regulatory bodies. We designed our audit procedures to identify non-compliance with such laws and regulations identified in the paragraph above. As well as enquiry and attendance at meetings, our procedures involved a review of the reporting to the above committees and a review of board meetings and other committee minutes to identify any non-compliance with laws and regulations. Our procedures also involved journal entry testing, with a focus on journals meeting our defined risk criteria based on our understanding of the business.
- We assessed the susceptibility of the Group's financial statements to material misstatement, including how fraud might occur by making enquiries of senior management, including the Chief Executive Officer, Chief Financial Officer, Head of Internal Audit and Audit Committee Chairman. We planned our audit to identify risks of management override, tested higher risk journal entries and performed audit procedures to address the potential for management bias, particularly over areas involving significant estimation and judgement. Further discussion of our approach to address the identified risks of management override are set out in the key audit matters section of our report.
- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved making enquiries of key management and legal counsel, reviewing key policies, inspecting legal registers and correspondence with regulators and reading key management meeting minutes. We also completed procedures to conclude on the compliance of significant disclosures in the Annual Report and Accounts with the requirements of the relevant accounting standards, UK legislation and the UK Corporate Governance Code.
- We communicated regularly with the component teams and attended key meetings with the component teams, management and legal counsel in order to identify and communicate any instances of non-compliance with laws and regulations.
- The Group operates in the water and waste sectors, which are highly regulated environments. As such the Senior Statutory Auditor reviewed the experience and expertise of the engagement team to ensure that the team had the appropriate competence and capabilities, which included the use of an expert where appropriate.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at https://www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Other matters we are required to address

- We were appointed by the company at its annual general meeting on 31 July 2014 to audit the financial statements for the year ending 31 March 2015 and subsequent financial periods.
- The period of total uninterrupted engagement including previous renewals and reappointments is 6 years, covering the years ended 31 March 2015 to 31 March 2020.
- The non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the Parent Company and we remain independent of the group and the Parent Company in conducting the audit.
- Our audit opinion is consistent with our additional report to the Audit Committee explaining the results of our audit.

Use of our report

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.

Christabel Cowling (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
Leeds

3 June 2020

Notes:

1. The maintenance and integrity of the Pennon Group plc web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.
2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Consolidated income statement
For the year ended 31 March 2020

	Notes	Statutory 2020 £m	Discontinued operations (note 46) 2020 £m	Pro forma Total[2] 2020 £m	Statutory 2019 (restated[1]) £m	Discontinued operations (note 46) 2019 (restated[1]) £m	Pro forma Total 2019[2] £m
Revenue	5	**636.7**	753.2	1,389.9	**632.6**	845.6	1,478.2
Operating costs	7						
Employment costs		**(70.0)**	(130.4)	(200.4)	**(67.2)**	(138.6)	(205.8)
Raw materials and consumables used		**(14.9)**	(87.2)	(102.1)	**(15.0)**	(94.3)	(109.3)
Other operating expenses		**(186.5)**	(337.5)	(524.0)	**(183.1)**	(433.8)	(616.9)
Underlying earnings before interest, tax, depreciation and amortisation	5	**365.3**	198.1	563.4	**367.3**	178.9	546.2
Operating non-underlying items	6	**(7.9)**	3.8	(4.1)	**3.9**	(29.6)	(25.7)
Depreciation and amortisation	7	**(119.8)**	(82.1)	(201.9)	**(117.2)**	(78.0)	(195.2)
Operating profit		**237.6**	119.8	357.4	**254.0**	71.3	325.3
Finance income	8	**4.1**	22.5	26.6	**3.5**	20.0	23.5
Finance costs: Underlying	8	**(66.6)**	(48.7)	(115.3)	**(61.9)**	(44.8)	(106.7)
Finance costs: Non-underlying	6	**18.0**	–	18.0	**5.8**	–	5.8
Finance costs		**(48.6)**	(48.7)	(97.3)	**(56.1)**	(44.8)	(100.9)
Net finance costs	8	**(44.5)**	(26.2)	(70.7)	**(52.6)**	(24.8)	(77.4)
Share of post-tax profit from joint ventures	20	**–**	14.8	14.8	**–**	12.4	12.4
Underlying profit before tax		**183.0**	104.6	287.6	**191.7**	88.5	280.2
Non-underlying operating and finance costs		**10.1**	3.8	13.9	**9.7**	(29.6)	(19.9)
Profit before tax	5	**193.1**	108.4	301.5	**201.4**	58.9	260.3
Taxation charge	9	**(70.6)**	(24.6)	(95.2)	**(32.8)**	(4.9)	(37.7)
			83.8	206.3		54.0	222.6
Profit from continuing operations		**122.5**			**168.6**		
Profit from discontinued operations	46	**83.8**			**54.0**		
Profit for the year		**206.3**			**222.6**		
Attributable to:							
Ordinary shareholders of the parent		**200.4**			**214.3**		
Non-controlling interests		**(1.1)**			**(0.3)**		
Perpetual capital security holders		**7.0**			**8.6**		
Earnings per ordinary share (pence per share)	11						
From continuing operations							
– Basic		**27.7**			**38.2**		
– Diluted		**27.6**			**38.1**		
From continuing and discontinued operations							
– Basic		**47.7**			**51.1**		
– Diluted		**47.5**			**50.9**		

(1) The prior year income statement has been restated to reflect the impact of classifying our waste management activities provided by Viridor as a discontinued operation (see note 46).

(2) Pro forma results represent non-GAAP measures presented to provide sufficient detail to enable certain users of the financial statements to assess the combined results of the continuing and discontinued operations of the Group during the current and prior financial years.

Consolidated statement of comprehensive income
For the year ended 31 March 2020

	Notes	2020 £m	2019 £m
Profit for the year		**206.3**	222.6
Other comprehensive income/(loss)			
Items that will not be reclassified to profit or loss			
Remeasurement of defined benefit obligations	30	**17.7**	(17.2)
Income tax on items that will not be reclassified	9, 31	**0.1**	3.2
Total items that will not be reclassified to profit or loss		**17.8**	(14.0)
Items that may be reclassified subsequently to profit or loss			
Share of other comprehensive income from joint ventures	20	**0.2**	0.5
Cash flow hedges		**(14.3)**	(6.4)
Income tax on items that may be reclassified	9, 31	**3.1**	0.6
Total items that may be reclassified subsequently to profit or loss		**(11.0)**	(5.3)
Other comprehensive income/(loss) for the year net of tax	36	**6.8**	(19.3)
Total comprehensive income for the year		**213.1**	203.3
Total comprehensive income attributable to:			
Ordinary shareholders of the parent		**207.2**	195.0
Non-controlling interests		**(1.1)**	(0.3)
Perpetual capital security holders		**7.0**	8.6

The notes on pages 138 to 190 form part of these financial statements.

Balance sheets
At 31 March 2020

	Notes	Group 2020 £m	Group 2019 £m	Company 2020 £m	Company 2019 £m
Assets					
Non-current assets					
Goodwill	15	**42.3**	385.0	**–**	–
Other intangible assets	16	**1.2**	92.1	**–**	–
Property, plant and equipment	17	**3,171.8**	4,509.4	**0.2**	0.3
Other non-current assets	19	**–**	256.4	**1,223.5**	1,044.6
Deferred tax assets	31	**–**	–	**1.8**	1.2
Derivative financial instruments	23	**4.1**	70.5	**4.1**	3.7
Investments in subsidiary undertakings	20	**–**	–	**845.2**	1,980.8
Investments in joint ventures	20	**–**	51.1	**–**	–
Retirement benefit obligations	30	**6.6**	–	**–**	–
		3,226.0	5,364.5	**2,074.8**	3,030.6
Current assets					
Inventories	21	**4.9**	28.8	**–**	–
Trade and other receivables	22	**185.8**	484.8	**24.7**	21.6
Current tax receivable	27	**1.9**	–	**–**	–
Derivative financial instruments	23	**2.7**	11.8	**2.5**	2.8
Cash and cash deposits	25	**665.9**	569.6	**367.9**	284.8
		861.2	1,095.0	**395.1**	309.2
Assets held for sale	46	**2,675.3**	–	**1,135.6**	–
		3,536.5	1,095.0	**1,530.7**	309.2
Liabilities					
Current liabilities					
Borrowings	28	**(59.9)**	(150.4)	**(290.5)**	(335.7)
Financial liabilities at fair value through profit	24	**(1.5)**	(3.8)	**(0.5)**	(0.4)
Derivative financial instruments	23	**(7.1)**	(11.1)	**(0.9)**	(0.2)
Trade and other payables	26	**(115.3)**	(298.0)	**(19.8)**	(15.8)
Current tax liabilities	27	**–**	(19.1)	**(2.5)**	(3.6)
Provisions	32	**(0.6)**	(28.7)	**–**	–
		(184.4)	(511.1)	**(314.2)**	(355.7)
Liabilities directly associated with assets classified as held for sale	46	**(756.3)**	–	**–**	–
Net current assets/(liabilities)		**2,595.8**	583.9	**1,216.5**	(46.5)
Non-current liabilities					
Borrowings	28	**(3,654.9)**	(3,498.7)	**(1,135.4)**	(989.7)
Other non-current liabilities	29	**(122.9)**	(147.9)	**(8.6)**	(8.6)
Financial liabilities at fair value through profit	24	**(43.1)**	(43.1)	**(1.1)**	(1.4)
Derivative financial instruments	23	**(27.2)**	(9.9)	**(2.8)**	(0.7)
Retirement benefit obligations	30	**–**	(60.8)	**(0.1)**	(3.4)
Deferred tax liabilities	31	**(261.6)**	(305.1)	**–**	–
Provisions	32	**–**	(203.1)	**–**	–
		(4,109.7)	(4,268.6)	**(1,148.0)**	(1,003.8)
Net assets		**1,712.1**	1,679.8	**2,143.3**	1,980.3
Shareholders' equity					
Share capital	33	**171.3**	171.1	**171.3**	171.1
Share premium account	34	**227.0**	223.6	**227.0**	223.6
Capital redemption reserve	35	**144.2**	144.2	**144.2**	144.2
Retained earnings and other reserves	36	**872.8**	843.0	**1,304.1**	1,144.7
Total shareholders' equity		**1,415.3**	1,381.9	**1,846.6**	1,683.6
Non-controlling interests		**0.1**	1.2	**–**	–
Perpetual capital securities	37	**296.7**	296.7	**296.7**	296.7
Total equity		**1,712.1**	1,679.8	**2,143.3**	1,980.3

The profit for the year attributable to ordinary shareholders' equity dealt with in the accounts of the Parent Company is £330.6 million (2019 £194.8 million).

The notes on pages 138 to 190 form part of these financial statements.

The financial statements on pages 132 to 190 were approved by the Board of Directors and authorised for issue on 3 June 2020 and were signed on its behalf by:

Chris Loughlin, Chief Executive Officer Pennon Group plc
Registered Office: Peninsula House, Rydon Lane, Exeter, Devon, England EX2 7HR. Registered in England Number 2366640.

Statements of changes in equity
For the year ended 31 March 2020

	Share capital (note 33) £m	Share premium account (note 34) £m	Capital redemption reserve (note 35) £m	Retained earnings and other reserves (note 36) £m	Non-controlling interests £m	Perpetual capital securities (note 37) £m	Total equity £m
Group							
At 1 April 2018	170.8	218.8	144.2	807.1	1.5	296.7	1,639.1
Profit for the year	–	–	–	214.3	(0.3)	8.6	222.6
Other comprehensive loss for the year	–	–	–	(19.3)	–	–	(19.3)
Total comprehensive income for the year	–	–	–	195.0	(0.3)	8.6	203.3
Transactions with equity shareholders:							
Dividends paid	–	–	–	(162.0)	–	–	(162.0)
Adjustment in respect of share-based payments (net of tax)	–	–	–	4.4	–	–	4.4
Distributions to perpetual capital security holders	–	–	–	–	–	(8.6)	(8.6)
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	–	–	–	(1.5)	–	–	(1.5)
Proceeds from shares issued under the Sharesave Scheme	0.3	4.8	–	–	–	–	5.1
Total transactions with equity shareholders	0.3	4.8	–	(159.1)	–	(8.6)	(162.6)
At 31 March 2019	171.1	223.6	144.2	843.0	1.2	296.7	1,679.8
Opening adjustment on adoption of IFRS 16	–	–	–	(8.0)	–	–	(8.0)
At 1 April 2019 (adjusted for IFRS 16)	171.1	223.6	144.2	835.0	1.2	296.7	1,671.8
Profit for the year	–	–	–	200.4	(1.1)	7.0	206.3
Other comprehensive income for the year	–	–	–	6.8	–	–	6.8
Total comprehensive income for the year	–	–	–	207.2	(1.1)	7.0	213.1
Transactions with equity shareholders:							
Dividends paid	–	–	–	(172.6)	–	–	(172.6)
Adjustment in respect of share-based payments (net of tax)	–	–	–	4.8	–	–	4.8
Distributions to perpetual capital security holders	–	–	–	–	–	(8.6)	(8.6)
Current tax relief on distribution to perpetual capital security holders	–	–	–	–	–	1.6	1.6
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	–	–	–	(1.6)	–	–	(1.6)
Proceeds from shares issued under the Sharesave Scheme	0.2	3.4	–	–	–	–	3.6
Total transactions with equity shareholders	0.2	3.4	–	(169.4)	–	(7.0)	(172.8)
At 31 March 2020	**171.3**	**227.0**	**144.2**	**872.8**	**0.1**	**296.7**	**1,712.1**

The notes on pages 138 to 190 form part of these financial statements.

Statements of changes in equity
For the year ended 31 March 2020
continued

	Share capital (note 33) £m	Share premium account (note 34) £m	Capital redemption reserve (note 35) £m	Retained earnings and other reserves (note 36) £m	Perpetual capital securities (note 37) £m	Total equity £m
Company						
At 1 April 2018	170.8	218.8	144.2	1,111.1	296.7	1,941.6
Profit for the year (note 10)	–	–	–	194.8	8.6	203.4
Other comprehensive income for the year	–	–	–	0.2	–	0.2
Total comprehensive income for the year	–	–	–	195.0	8.6	203.6
Transactions with equity shareholders:						
Dividends paid	–	–	–	(162.0)	–	(162.0)
Distributions to perpetual capital security holders	–	–	–	–	(8.6)	(8.6)
Adjustment in respect of share-based payments (net of tax)	–	–	–	1.5	–	1.5
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	–	–	–	(0.9)	–	(0.9)
Proceeds from shares issued under the Sharesave Scheme	0.3	4.8	–	–	–	5.1
Total transactions with equity shareholders	0.3	4.8	–	(161.4)	(8.6)	(164.9)
At 31 March 2019	171.1	223.6	144.2	1,144.7	296.7	1,980.3
Profit for the year (note 10)	–	–	–	330.6	7.0	337.6
Other comprehensive income for the year	–	–	–	0.5	–	0.5
Total comprehensive income for the year	–	–	–	331.1	7.0	338.1
Transactions with equity shareholders:						
Dividends paid	–	–	–	(172.6)	–	(172.6)
Distributions to perpetual capital security holders	–	–	–	–	(8.6)	(8.6)
Current tax relief on distribution to perpetual capital security holders	–	–	–	–	1.6	1.6
Adjustment in respect of share-based payments (net of tax)	–	–	–	2.0	–	2.0
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	–	–	–	(1.1)	–	(1.1)
Proceeds from shares issued under the Sharesave Scheme	0.2	3.4	–	–	–	3.6
Total transactions with equity shareholders	0.2	3.4	–	(171.7)	(7.0)	(175.1)
At 31 March 2020	**171.3**	**227.0**	**144.2**	**1,304.1**	**296.7**	**2,143.3**

The notes on pages 138 to 190 form part of these financial statements.

Cash flow statements

For the year ended 31 March 2020

		Group		Company	
	Notes	**2020 £m**	2019 £m	**2020 £m**	2019 £m
Cash flows from operating activities					
Cash generated/(outflow) from operations	38	**516.3**	399.8	**(180.3)**	(223.0)
Interest paid	38	**(97.7)**	(83.9)	**(37.4)**	(36.8)
Tax paid		**(52.6)**	(29.2)	**(3.7)**	(22.1)
Net cash generated/(outflow) from operating activities		**366.0**	286.7	**(221.4)**	(281.9)
Cash flows from investing activities					
Interest received		**3.4**	10.3	**45.1**	44.5
Dividends received	44	**6.0**	5.5	**335.6**	196.7
Investment in joint venture		**–**	(54.8)	**–**	–
Loan repayments received from joint ventures		**13.4**	0.5	**–**	–
Deposit of restricted deposits		**(23.3)**	(21.6)	**–**	–
Purchase of property, plant and equipment		**(332.8)**	(356.0)	**–**	–
Purchase of intangible assets		**(0.6)**	–	**–**	–
Proceeds from sale of property, plant and equipment		**10.6**	6.3	**–**	–
Net cash (used in)/received from investing activities		**(323.3)**	(409.8)	**380.7**	241.2
Cash flows from financing activities					
Proceeds from issuance of ordinary shares		**3.6**	5.1	**3.5**	5.1
Proceeds from derivatives early settlement		**87.2**	–	**–**	–
Purchase of ordinary shares by the Pennon Employee Share Trust		**(1.6)**	(1.5)	**–**	–
Proceeds from new borrowing		**268.2**	384.5	**151.7**	334.5
Repayment of borrowings		**(84.8)**	(181.6)	**(51.8)**	(149.6)
Cash inflows from lease financing arrangements		**115.0**	74.9	**–**	–
Lease principal repayments (2019 Finance lease principal repayments)		**(142.8)**	(27.8)	**–**	–
Dividends paid		**(172.6)**	(162.0)	**(172.6)**	(162.0)
Perpetual capital securities periodic return	37	**(8.6)**	(5.8)	**(7.0)**	(5.8)
Net cash received from/(used in) financing activities		**63.6**	85.8	**(76.2)**	22.2
Net increase/(decrease) in cash and cash equivalents		**106.3**	(37.3)	**83.1**	(18.5)
Cash and cash equivalents at beginning of the year	25	**365.7**	403.0	**284.8**	303.3
Cash and cash equivalents at end of the year	25	**472.0**	365.7	**367.9**	284.8

The cash flow statement above includes the entire Group, including cash flows relating to the Viridor business. Disaggregated information relating to the Viridor business is provided in note 46.

The notes on pages 138 to 190 form part of these financial statements.

Notes to the financial statements

1. General information

Pennon Group plc is a company registered in the United Kingdom under the Companies Act 2006. The address of the registered office is given on page 199. Through the year, Pennon Group's business has been operated through two main subsidiaries. South West Water Limited includes the integrated water businesses of South West Water and Bournemouth Water, providing water and wastewater services in Devon, Cornwall and parts of Dorset and Somerset and water only services in parts of Dorset, Hampshire and Wiltshire. Viridor Limited is a recycling and residual waste processing and transformation business. Pennon Group is also the majority shareholder of Pennon Water Services Limited, a company providing water and wastewater retail services to non-household customer accounts across Great Britain. On 18 March 2020 Pennon agreed to sell Viridor Limited for £3.7 billion, subject to a number of conditions. The sale is expected to complete in early summer 2020 (see note 46).

2. Principal accounting policies

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

(a) Basis of preparation

These financial statements have been prepared on the historical cost accounting basis (except for fair value items, principally acquisitions, transfers of assets from customers and certain financial instruments as described in accounting policy notes (b), (v) and (n) respectively) and in accordance with International Financial Reporting Standards (IFRS) and interpretations of the IFRS Interpretations Committee as adopted by the European Union, and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. A summary of the principal accounting policies is set out below, together with an explanation where changes have been made to previous policies on the adoption of new accounting standards and interpretations in the year.

The going concern basis has been adopted in preparing these financial statements. At 31 March 2020 the Group has access to undrawn committed funds and cash and cash deposits totalling £1.6 billion (£1.4 billion after restricted cash). Having considered the Group's strong funding position, the potential use of proceeds from the proposed sale of Viridor and prudent financial projections, which take into account a range of possible impacts, as described in this report, from the COVID-19 pandemic, the Directors have a reasonable expectation that the Group has adequate resource to continue in operational existence for the period of at least 12 months from the date of the approval of the financial statements and that there are no material uncertainties to disclose. For this reason they continue to adopt the going concern basis in preparing the financial statements.

Other than the adoption of IFRS 16, which is explained in note 45, new standards or interpretations which were mandatory for the first time in the year beginning 1 April 2019 did not have a material impact on the net assets or results of the Group.

New standards or interpretations due to be adopted from 1 April 2020 are not expected to have a material impact on the Group's net assets or results. Existing borrowing covenants are not impacted by changes in accounting standards.

(b) Basis of consolidation

The Group financial statements include the results of Pennon Group plc and its subsidiaries and joint ventures.

The results of subsidiaries and joint ventures are included from the date of acquisition or incorporation, and excluded from the date of disposal. The results of subsidiaries are consolidated where the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The results of joint ventures are accounted for on an equity basis.

Intra-group trading, loan balances and transactions are eliminated on consolidation.

The acquisition method of accounting is used to account for the purchase of subsidiaries. The excess of the value transferred to the seller in return for control of the acquired business, together with the fair value of any previously held equity interest in that business over the Group's share of the fair value of the identifiable net assets, is recorded as goodwill.

Assets held for sale and discontinued operations

In accordance with IFRS 5 'Non-current assets held for sale and discontinued operations', non-current assets and disposal groups are classified as held for sale only if available for immediate sale in their present condition and a sale is highly probable and expected to be completed within one year from the date of classification. Such assets are measured at the lower of carrying amount and fair value, less the costs of disposal, and are not depreciated or amortised. Accordingly the net results of the waste management segment (Viridor Group) are presented within discontinued operations in the Group income statement (for which the comparatives have been restated) and the assets and liabilities of these operations are presented separately in the Group Balance Sheet. Further information is provided in note 46.

(c) Revenue recognition

Group revenue is recognised following delivery of performance obligations and an assessment of when control over the product or service is transferred to the customer. Revenue is only recognised when collection of consideration is highly probable.

Revenue is recognised either when the performance obligation in the contract has been performed (point in time recognition) or 'over time' as the performance obligations to the customer are satisfied. For each obligation satisfied over time, the Group applies a revenue recognition method that accurately reflects performance in transferring control of the services to the customer.

Where a contract with a customer includes more than one performance obligation, revenue is allocated to each obligation in proportion to a fair value assessment of the total contract sales value split across the services provided.

At the inception of a contract the total transaction price is estimated, being the fair value to which the Group expects to be entitled under the contract, including any variable consideration. Variable consideration is based on the most likely outcome of the performance obligations.

Revenue excludes value added tax, trade discounts and revenue arising from transactions between Group companies.

2. **Principal accounting policies** continued

Water (domestic and non-household retail)

For most of the services provided to domestic customers, contract terms are implied through statute and regulation in the absence of formal, written contracts. South West Water has a duty under legislation to provide domestic customers with services regardless of payment and is not permitted to disconnect domestic customers for non-payment of bills. Charges are set via the periodic review price-setting process, regulated by Ofwat.

In respect of ongoing, continuous services to customers, such as the provision of drinking water and wastewater services, revenue is recognised over time in line with customer usage of those services.

Customers with an unmeasured supply are billed at the start of the year for the full amount of the annual charge but typically take advantage of a choice of payment arrangements to pay by regular instalments.

Customers with a metered supply are sent up to four bills per year, based either on actual meter readings or estimated usage. For these customers, revenue includes an estimation of the amount of unbilled usage at the period end. Payment options for domestic customers include an annual meter payment plan where customers agree to pay a fixed amount per month which is adjusted to reflect actual consumption at the end of the year.

A range of regulated services is offered to property developers and owners who require connection to the water and sewerage networks or need the networks to be extended or altered. Typically, these customers pay an estimate of the charges in advance as a deposit, which is treated as a contract liability and are billed or refunded the difference between the estimate and actual costs on completion of the work.

Where the performance obligation relates solely to a connection to the network, revenue is recognised at the point of connection when the customer is deemed to obtain control.

Where assets are constructed or provided by the Group or assets transferred to the Group, it is considered that there is an explicit or implied performance obligation to provide an ongoing water and/or wastewater service, with the result that revenue is recognised over a time no longer than the economic life of assets provided by or transferred to the Group.

Pennon Water Services provides specialist retail water and wastewater services to business customers. It raises bills and recognises revenue in accordance with its contracts with customers and in line with the limits established for the non-household periodic price-setting process where applicable.

Energy sales

The Group receives revenue from the sale of electricity from generating assets. These assets include solar, anaerobic digestion, gas from landfill and energy recovery facilities (ERFs). Revenue from the sale of electricity from the Group's generating assets is measured based upon metered output delivered at rates specified under contract terms or prevailing market rates. Revenue is recognised at a 'point in time', being the point of distribution. Typically, invoices are raised monthly with standard payment terms.

Waste management services

In respect of single services with fixed fees, such as the receipt of gate and collection fees, revenue is recognised at the time the service is provided.

The Group also delivers other waste management services for which revenue is recognised 'over time' in accordance with contracts with customers. The nature of contracts and/or performance obligations includes management fees to operate local authority recycling centres and ERFs, multi service contracts including collections and gate fees.

Revenue from other services can be fixed (i.e. management fees) or variable (i.e. gate fees).

Gate fee revenue, derived from the Group's operational assets, is recognised as customer waste is deposited and is based on tonnage received.

In respect of waste collection services, revenue is recognised at the point of collection from customer premises.

In respect of its landfill business, revenue is set to cover total costs, including landfill tax (LFT), and to achieve a desired profit margin. Viridor, as the operator, has a direct obligation to pay LFT, which represents a significant waste disposal cost of production for the business.

A majority of waste management customers are invoiced monthly for services provided within the monthly billing period. Payments are typically due on an end of month following invoice basis. Alternative billing and/or payment terms are agreed in exceptional circumstances.

The Group transfers control of such waste management services prior to invoicing. Receipt of payment following invoice is based solely on the passage of time. A trade receivable is recognised until payment is made and/or refund issued.

Where the Group has entered into service concession arrangements it accounts for these contracts in accordance with IFRIC 12. Consideration is treated as contract assets or other intangible assets, depending upon the right to receive cash from the asset. Consideration is split between construction of assets, operation of the service and provision of finance recognised as interest receivable.

Revenue in respect of construction services is recognised over time and is based on the fair value of work performed, with reference to the total sales value and the stage of completion of those services, as this best reflects the manner in which control passes to the customer. While construction is in progress the consideration is disclosed as a contract asset within non-current financial assets. On entry into operational service, in accordance with IFRIC 12, the contract asset is reclassified as either costs recoverable from construction activities disclosed within other intangible assets when the concession grantor has not provided a contractual guarantee in respect of the recoverable amount regardless of the service use by customers, and/or within other non-current financial assets when the concession grantor contractually guarantees the payment of amounts determined in the contract or the shortfall, if any, between amounts received from users of the public service and amounts specified or determined in the contract. No payments are received during construction.

In respect of operating services, revenue is recognised over time in line with delivery of operational services in accordance with the contract with the local authority.

Once the operational phase commences the Group has a right to receive consideration for the construction and operational services delivered. Invoicing typically occurs monthly and payments are due by the end of the month following date of invoice.

Notes to the financial statements
continued

2. Principal accounting policies continued

Recyclate

The Group transforms waste into recyclate ready for resale. Revenue is measured at the agreed transaction price per tonne of recyclate under the contract with the customer. Revenue recognition occurs when control over the recyclate assets has been transferred to the customer.

In respect of UK sales, the Group's performance obligation is satisfied at the point of collection by the customer. This is the point in time when an invoice is issued and revenue is recognised. Payment terms are typically end of month following invoice date. Overseas sales are predominantly agreed under a letter of credit. Goods are despatched at the point the letter of credit is accepted by the customer's bank. Payment is released when the customer confirms satisfactory receipt of the recyclate. This is the point legal title (i.e. control) passes to the customer and revenue is recognised.

Contract assets and liabilities

A trade receivable is recognised when the Group has an unconditional right to receive consideration in exchange for performance obligations already fulfilled. A contract asset is recognised when the Group has fulfilled some of its performance obligations but has not yet obtained an unconditional right to receive consideration, such as in the construction phase of a service concession agreement, as described above. The amounts for contract assets are disclosed within note 19 (Other non-current assets) and note 22 (Trade and other receivables) as appropriate. A contract liability is recognised when consideration is received in advance of the Group performing its performance obligations to customers, including, when appropriate, transfers of assets from customers (per paragraph (v) below). The value of contract liabilities is disclosed within note 26 (Trade and other payables) and note 29 (Other non-current liabilities) as appropriate.

(d) Segmental reporting

Each of the Group's business segments provides services which are subject to risks and returns which are different from those of the other business segments. The Group's internal organisation and management structure and its system of internal financial reporting are based primarily on business segments. Following the formal agreement to sell Viridor, which represents the waste management business segment, the comparative period segmental information has been restated to remove the waste management business from the continuing operations segmental reporting. The Waste management business was a significant segment of the Group throughout the financial year ended 31 March 2020 as such the results of the waste business have been included in the segmental disclosure as a discontinued operation. Further Information relating to income, expenses, cash flows and net assets of Viridor's waste management business is provided in note 46.

The remaining business segments of the Continuing Group include the water business, comprising the regulated water and wastewater services undertaken by South West Water, and the non-household retail business, comprising the services provided by Pennon Water Services in the non-household water and wastewater retail market which, while regulated, is open to competition. Other segments, including Pennon Group plc, are not reportable segments as they are not reported to Chief Decision makers. Segmental revenue and results include transactions between businesses. Inter-segmental transactions are eliminated on consolidation.

(e) Goodwill

Goodwill arising on consolidation from the acquisition of subsidiary undertakings represents the excess of the purchase consideration over the fair value of net assets acquired, less any subsequent impairment charges.

Goodwill is recognised as an asset and reviewed for impairment at least annually. Any impairment is recognised immediately in the income statement and is not subsequently reversed. For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the cash generating units (CGUs) or group of CGUs, that is expected to benefit from the synergies of the combination. Each unit or group of units to which goodwill is allocated represents the lowest level within the entity at which the goodwill is monitored for internal reporting purposes. Goodwill is allocated and monitored at the reportable operating segment level. Further details are contained in accounting policy (i).

When a subsidiary undertaking is sold, the profit or loss on disposal is determined after including the attributable amount of goodwill.

(f) Other intangible assets

Other intangible assets are recognised in relation to long-term service concessions contracts to the extent that future amounts to be received are not contracted.

Other intangible assets include assets acquired in a business combination and are capitalised at fair value at the date of acquisition. Following initial recognition, finite life intangible assets are amortised on a straight-line basis over their estimated useful lives, with the expense charged to the income statement through operating costs.

(g) Property, plant and equipment

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

Infrastructure assets were included at fair value on transition to IFRS, and subsequent additions are recorded at cost less accumulated depreciation and impairment charges. Expenditure to increase capacity or enhance infrastructure assets is capitalised where it can be reliably measured, and it is probable that incremental future economic benefits will flow to the Group. The cost of day-to-day servicing of infrastructure components is recognised in the income statement as it arises.

Infrastructure assets are depreciated evenly over their useful economic lives, and are principally:

Dams and impounding reservoirs	200 years
Water mains	40 – 120 years
Sewers	40 – 120 years

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

2. **Principal accounting policies** continued

ii) Landfill sites

Landfill sites are included within land and buildings at cost less accumulated depreciation. Cost includes acquisition and development expenses. The cost of a landfill site is depreciated to its residual value over its estimated operational life taking account of the usage of void space.

iii) Landfill restoration

Where the obligation to restore a landfill site is an integral part of its future economic benefits, a non-current asset within property, plant and equipment is recognised. The asset recognised is depreciated based on the usage of void space.

iv) Other assets (including ERFs, property, overground plant and equipment)

Other assets are included at cost less accumulated depreciation.

Freehold land is not depreciated. Other assets are depreciated evenly to their residual value over their estimated economic lives, and are principally:

Land and buildings – freehold buildings	30 – 60 years
Land and buildings – leasehold buildings	Over the estimated economic lives or the finance lease period, whichever is the shorter
Operational properties	40 – 80 years
ERFs (including major refurbishments)	25 – 40 years
Fixed plant	20 – 40 years
Vehicles, mobile plant and computers	3 – 10 years

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

The cost of assets includes directly attributable labour and overhead costs which are incremental to the Group. Borrowing costs directly attributable to the construction of a qualifying asset (an asset necessarily taking a substantial period of time to be prepared for its intended use) are capitalised as part of the asset. Assets transferred from customers are recognised at fair value as set out in accounting policy (v).

The assets' residual values and useful lives are reviewed annually.

Gains and losses on disposal are determined by comparing sale proceeds with carrying amounts. These are included in the income statement.

(h) Leased assets

All are accounted for by recognising a right-of-use asset and a lease liability except for:

- Low value assets; and
- Leases with a duration of 12 months or less.

Contracts previously classified as 'operating leases' under IAS 17 are measured at the present value of contractual payments due to the lessor over the lease term, with the discount rate determined by reference to the rate inherent in the lease unless this is not readily determinable, in which case the Group's incremental borrowing rate on commencement of the lease is used. After initial measurement, lease payments are allocated between the liability and finance cost. The finance cost is charged to profit and loss over the lease period to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The interest element of cash payments in respect of these leases is included within interest payments in determining net cash generated from operating activities. The capital element of the cash payment is included within cash flows from financing activities. Right-of-use assets are amortised on a straight-line basis over the remaining term of the lease or the remaining economic life of the asset if shorter. When the Group revisits its estimate of lease term (because, for example, it reassesses an extension option), it adjusts the carrying amount of the lease liability to reflect the payments to make over the revised term, which is discounted at the same discount rate that applied on lease commencement. In these circumstances an equivalent adjustment is made to the carrying value of the right-of-use asset, with the revised carrying amount being amortised over the remaining (revised) lease term.

Measurement and recognition of assets and liabilities previously accounted for as 'finance leases' under IAS 17 continue to apply following the adoption of IFRS 16. Assets continue to be included as property, plant and equipment as right-of-use assets at the lower of their fair value at commencement or the present value of the minimum lease payments, and are depreciated over their estimated economic lives or the finance lease period, whichever is the shorter. The corresponding liability is recorded as borrowings. The interest element of the rental costs is charged against profits using the actuarial method over the period of the lease.

The Group regularly uses sale and lease back transactions to finance its capital programme. A sale and leaseback transaction is where the Group sells an asset and immediately reacquires the use of the asset by entering into a lease with the buyer. Each transaction is assessed as to whether it meets the criteria within IFRS 15 'Revenue from contracts with customers' for a sale to have occurred. As a result, a lease liability is recognised, the associated property, plant and equipment asset is derecognised, and a right-of-use asset is recognised at the proportion of the carrying value relating to the right retained. Any gain or loss arising relates to the rights transferred to the buyer.

The impact of the adoption of IFRS 16 'Leases' on 1 April 2020 is set out in note 45.

IFRS 16 policy applied from 1 April 2020

The impact of the adoption of IFRS 16 'Leases' on 1 April 2020 is discussed in paragraph (a) above and note 45.

Notes to the financial statements
continued

2. Principal accounting policies continued

(i) Impairment of non-financial assets

Assets with an indefinite useful life are not subject to amortisation and are tested annually for impairment, or whenever events or changes in circumstance indicate that the carrying amount may not be recoverable.

Assets subject to amortisation or depreciation are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised for the amount by which an asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value, less costs to sell, and value-in-use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (CGUs). Value-in-use represents the present value of projected future cash flows expected to be derived from a CGU, discounted using a pre-tax discount rate which reflects an assessment of the market cost of capital of the CGU. Impairments are charged to the income statement in the year in which they arise.

Non-financial assets other than goodwill that have been impaired are reviewed for possible reversal of the impairment at each reporting date.

Where a previously impaired asset or CGU's recoverable amount is in excess of its carrying amount, previous impairments are reversed to the carrying value that would have expected to be recognised had the original impairment not occurred.

(j) Investment in subsidiary undertakings

Investments in subsidiary undertakings are initially recorded at cost, being the fair value of the consideration paid. Subsequently investments are reviewed for impairment on an individual basis annually or if events or changes in circumstances indicate that the carrying value may not be fully recoverable.

(k) Investment in joint ventures

Joint ventures are entities over which the Group exercises joint control. Investments in joint ventures are accounted for using the equity method of accounting. Any excess of the cost of acquisition over the Group's share of the fair values of the identifiable net assets of the joint venture at the date of acquisition is recognised as goodwill and is included in the carrying value of the investment in the joint venture.

The carrying value of the Group's investment is adjusted for the Group's share of post-acquisition profits or losses recognised in the income statement and statement of comprehensive income. Losses of a joint venture in excess of the Group's interest are not recognised unless the Group has a legal or constructive obligation to fund those losses.

(l) Inventories

Inventories are stated at the lower of cost and net realisable value. The cost of finished goods and work in progress includes raw materials and the cost of bringing stocks to their present location and condition. It excludes borrowing costs. Net realisable value is the estimated selling price less cost to sell. The costs of items of inventory are determined using weighted average costs.

(m) Cash and cash deposits

Cash and cash deposits comprise cash in hand and short-term deposits held at banks. Bank overdrafts are shown within current borrowings.

(n) Financial instruments

Financial instruments are recognised and measured in accordance with IFRS 9. The Group classifies its financial instruments in the following categories:

i) Debt instruments at amortised cost

All loans and borrowings are initially recognised at fair value, net of transaction costs incurred. Following initial recognition, interest-bearing loans and borrowings are subsequently stated at amortised cost using the effective interest method. Gains and losses are recognised in the income statement when instruments are derecognised or impaired. Premia, discounts and other costs and fees are recognised in the income statement through amortisation.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

ii) Trade receivables

Trade receivables do not carry any interest receivable and are recognised initially at fair value and subsequently at amortised cost using the effective interest method, less provision for expected credit losses (ECLs). In accordance with the terms and conditions of IFRS 9, since 1 April 2019, each Group entity performs an impairment analysis at each reporting date to measure the ECLs. Each entity does not track changes in credit risk but instead recognises a loss allowance based on lifetime ECLs at each reporting date. Each subsidiary has established a provision matrix that is based on its historical credit loss experience, adjusted for forward-looking factors specific to the receivables and the economic environment.

2. **Principal accounting policies** continued

iii) Trade payables

Trade payables are not interest-bearing and are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

iv) Financial assets arising from service concession arrangements

Where the provision of waste management services is performed through a contract with a public sector entity, which controls a significant residual interest in asset infrastructure at the end of the contract, then consideration is treated as contract receivables, split between profit on the construction of assets, operation of the service and the provision of finance which is recognised in notional interest within finance income.

v) Derivative financial instruments and hedging activities

The Group uses derivative financial instruments, principally interest rate swaps, foreign exchange forward contracts and cross-currency interest rate swaps to hedge risks associated with interest rate and exchange rate fluctuations. Derivative instruments are initially recognised at fair value on the date the derivative contract is entered into and subsequently remeasured at fair value for the reported balance sheet.

The Group designates certain hedging derivatives as either:

- A hedge of a highly probable forecast transaction or change in the cash flows of a recognised asset or liability (a cash flow hedge); or
- A hedge of the exposure to change in the fair value of a recognised asset or liability (a fair value hedge).

The gain or loss on remeasurement is recognised in the income statement except for cash flow hedges which meet the conditions for hedge accounting, when the portion of the gain or loss on the hedging instrument which is determined to be an effective hedge is recognised directly in equity, and the ineffective portion in the income statement. The gains or losses deferred in equity in this way are subsequently recognised in the income statement in the same period in which the hedged underlying transaction or firm commitment is recognised in the income statement.

In order to qualify for hedge accounting, the Group is required to document in advance the relationship between the item being hedged and the hedging instrument. The Group is also required to document and demonstrate an assessment of the relationship between the hedged item and the hedging instrument which shows that the hedge will be highly effective on an ongoing basis. This effectiveness testing is reperformed at the end of each reporting period to ensure that the hedge remains highly effective.

The full fair value of a hedging derivative is apportioned on a straight-line basis between non-current and current assets and liabilities based on the remaining maturity of the hedging derivative.

Derivative financial instruments deemed held for trading, which are not subject to hedge accounting, are classified as a current asset or liability with any change in fair value recognised immediately in the income statement.

The Group uses cross-currency swaps for some of its foreign currency denominated private placement borrowings. The swaps either have the effect of (i) converting variable rate foreign currency borrowings into fixed rate sterling borrowings, (ii) converting fixed rate foreign currency borrowings into fixed rate sterling borrowings, or (iii) converting fixed rate foreign currency borrowings into floating rate sterling borrowings.

In January 2020, the IASB's interest rate benchmark reform amendments IFRS 7 'Financial Instrument (FI) disclosures' and to IFRS 9 'FI recognition and measurement' were endorsed by the EU. The amendments modify hedge accounting requirements to allow hedge accounting to continue for affected hedges during the period of uncertainty before the hedged items or hedging instruments are affected when current interest rate benchmarks are amended due to the ongoing interest rate benchmark reforms.

The amendments are relevant to the Group given that it applies hedge accounting to its benchmark interest rate exposures.

The application of the amendments impacts the Group's accounting policies in the following ways:

The Group has floating rate debt, linked to the UK's benchmark rate GBP London Inter-Bank Offered Rate (GBP LIBOR), which it fixes through cash flow hedges using interest rate swaps. The amendments permit continuation of hedge accounting even though there is uncertainty about the timing and amount of the hedged cash flows due to the interest rate benchmark reforms.

The Group uses cross-currency interest rate swaps to hedge the foreign currency risk, where applicable, within its financial instruments. The amendments permit continuation of hedge accounting even though there is uncertainty about the replacement of the floating interest rates included in its cross-currency interest rate swaps.

The Group will retain the cumulative gain or loss in the hedging reserve for designated cash flow hedges that are subject to interest rate benchmark reforms even though there is uncertainty arising from the reform with respect to the timing and amount of the cash flows of the hedged items. If the hedged future cash flows are no longer expected to occur due to reasons other than interest rate benchmark reform, the cumulative gain or loss will be immediately reclassified to profit or loss.

The Group has chosen to early adopt the amendments to IFRS 7 and IFRS 9 for the reporting period ended 31 March 2020, which are mandatory for annual reporting periods commencing after 1 January 2020.

vi) Financial instruments at fair value through profit

Financial instruments at fair value through profit reflect the fair value movement of the hedged risk on a hedged item through a fair value hedging relationship. The fair values of these financial instruments are initially recognised on the date the hedging relationship is entered into and thereafter remeasured at each subsequent balance sheet date. The gain or loss on remeasurement for the period is recognised in the income statement

vii) Receivables due from subsidiary undertakings

Amounts owed by subsidiaries are classified and recorded at amortised cost and reduced by allowances for ECLs. Estimated future credit losses are first recorded on initial recognition of a receivable and are based on estimated probability of default. Individual balances are written off when management deems them not to be collectible.

Notes to the financial statements
continued

2. Principal accounting policies continued

(o) Taxation including deferred tax

The tax charge for the year comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised in the statement of comprehensive income or directly in equity. In this case, the tax is also recognised in the statement of comprehensive income or directly in equity as appropriate.

Current tax is calculated on the basis of tax laws enacted or substantively enacted at the balance sheet date. Management periodically evaluates tax items subject to interpretation and establishes provisions on individual tax items, where in the judgement of management, the position is uncertain. The Group includes a number of companies, including the parent company, which are part of a tax group for certain aspects of the tax legislation. One of these aspects relates to group relief whereby current tax liabilities can be offset by current tax losses arising in other companies within the same tax group. Payments for group relief are included within the current tax disclosures.

Deferred tax is provided in full on temporary differences between the carrying amount of assets and liabilities in the financial statements and the tax base, except where they arise 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 tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which the assets can be realised. Deferred tax is determined using the tax rates enacted or substantively enacted at the balance sheet date, and expected to apply when the deferred tax liability is settled or the deferred tax asset is realised.

(p) Provisions

Provisions are made where there is a present legal or constructive obligation as a result of a past event and it is probable that there will be an outflow of economic benefits to settle this obligation and a reliable estimate of this amount can be made. Where the effect of the time value of money is material the current amount of a provision is the present value of the expenditures expected to be required to settle obligations. The unwinding of the discount to present value is included as notional interest within finance costs.

The Group's policies on specific provisions are:

i) Landfill restoration costs

Provisions for the cost of restoring landfill sites are made when the obligation arises. Where the obligation recognised as a provision is an integral part of a landfill site's future economic benefit, an asset in property, plant and equipment is recognised. Provisions are otherwise charged against profits based on the usage of void space.

ii) Environmental control and aftercare costs

Environmental control and aftercare costs are incurred during the operational life of each landfill site and for a considerable period thereafter. Provision for all such costs is made over the operational life of the site and charged to the income statement on the basis of the usage of void space at the site. Further provisions required after the operational life of a site are recognised immediately in the income statement.

iii) Underperforming contracts

Where the unavoidable costs of meeting a contract's obligations exceed the economic benefits derived from that contract, the unavoidable costs, less revenue anticipated under the terms of the contract, are recognised as a provision and charged to the income statement. An impairment loss on any assets dedicated to that contract is also recognised as described in accounting policy (i).

(q) Share capital and treasury shares

Ordinary shares are classified as equity.

Where the Company purchases the Company's equity share capital (treasury shares) the consideration paid, including any directly attributable costs, is deducted from equity until the shares are cancelled or reissued. Where such shares are subsequently reissued, any consideration received, net of any directly attributable transaction costs, is included in equity.

The Group balance sheet includes the shares held by the Pennon Group plc Employee Benefit Trust, relating to employee share-based payments, which have not vested at the balance sheet date. These are shown as a deduction from shareholders' equity until such time as they vest. The Trust, which is registered in the United Kingdom, was formed on 18 December 2019 to supersede the Pennon Employee Share Trust which was registered in Guernsey.

(r) Dividend distributions

Dividend distributions are recognised as a liability in the financial statements in the period in which the dividends are approved by the Company's shareholders. Interim dividends are recognised when paid; final dividends when approved by shareholders at the Annual General Meeting.

(s) Employee benefits

i) Retirement benefit obligations

The Group operates defined benefit and defined contribution pension schemes.

Defined benefit pension schemes

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 year less the fair value of plan assets. If the value of a plan's assets exceeds the present value of its obligations, the resulting surplus is only recognised if the Group has an unconditional right to that surplus.

The defined benefit obligation is calculated by independent actuaries who advise on the selection of Directors' best estimates of assumptions, using the projected unit credit 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, and that have terms to maturity approximating to the terms of the related pension obligation. The increase in liabilities of the Group's defined benefit pension schemes, expected to arise from employee service in the year, is charged against operating profit.

Changes in benefits granted by the employer are recognised immediately as a past service cost in the income statement.

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

2. Principal accounting policies continued

Defined contribution scheme

Costs of the defined contribution pension scheme are charged to the income statement in the year in which they arise. The Group has no further payment obligations once the contributions have been paid.

ii) Share-based payment

The Group operates a number of equity-settled, share-based payment plans for employees. The fair value of the employee services required in exchange for the grant is recognised as an expense over the vesting period of the grant.

Fair values are calculated using an appropriate pricing model. Non-market-based vesting conditions are adjusted for assumptions as to the number of shares which are expected to vest.

(t) Pre-contract and development costs

Pre-contract and development costs, including bid costs are expensed as incurred, except where it is probable that the contract will be awarded or the development completed, in which case they are recognised as an asset which is amortised to the income statement over the life of the contract. These costs are included within other receivables as shown in note 19.

(u) Fair values

The fair value of interest rate swaps is based on the market price to transfer the asset or liability at the balance sheet date in an ordinary transaction between market participants. The fair values of short-term deposits, loans and overdrafts with a maturity of less than one year are assumed to approximate to their book values. In the case of non-current bank loans and other loans, the fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate available to the Group for similar financial instruments.

(v) Transfers of assets from customers

Where an item of property, plant and equipment that must be used to connect customers to the network is received from a customer, or where cash is received from a customer for the acquisition or construction of such an item, that asset is recorded and measured on initial recognition at its fair value. The credit created by the recognition of the asset is recognised as a contract liability on the balance sheet. The contract liability reduces, and revenue is recognised in the income statement, as performance obligations are satisfied. The period over which the credit is recognised depends upon the nature of the service provided, as determined by the agreement with the customer. Where the service provided is solely a connection to the network, the credit is recognised at the point of connection. If the agreement does not specify a period, revenue is recognised over a period no longer than the economic life of the transferred asset used to provide the ongoing service.

The fair value of assets on transfer from customers is determined using a cost valuation approach allowing for depreciation.

(w) Foreign exchange

Transactions denominated in foreign currencies are translated at the exchange rate at the date of the transaction. Monetary assets and liabilities denominated in a foreign currency are translated at the closing balance sheet rate. The resulting gain or loss is recognised in the income statement.

(x) Perpetual capital securities

Perpetual capital securities are issued securities that qualify for recognition as equity. Accordingly, any periodic returns are accounted for as dividends and recognised directly in equity and as a liability at the time the Company becomes obligated to pay the periodic return. This reflects the nature of the periodic returns and repayment of principal being only made at the Company's discretion. Any associated tax impacts are recognised directly in equity.

(y) Non-underlying items

Non-underlying items are those that in the Directors' view should be separately disclosed by virtue of their size, nature or incidence to enable a full understanding of the Group's financial performance.

3. Financial risk management

(a) Financial risk factors

The Group's activities expose it to a variety of financial risks: liquidity risk; market risk (interest rate and foreign currency risk); and credit risk.

The Group's treasury function seeks to ensure that sufficient funding is available to meet foreseeable needs and to maintain reasonable headroom for contingencies, and manages inflation and interest rate risk.

The principal financial risks faced by the Group relate to liquidity, interest rate and credit counterparty risk.

These risks and treasury operations are managed by the Chief Financial Officer in accordance with policies established by the Board. Major transactions are individually approved by the Board. Treasury activities are reported to the Board and are subject to review by internal audit.

Financial instruments are used to raise finance, manage risk, optimise the use of surplus funds and manage overall interest rate performance. The Group does not engage in speculative activity.

i) Liquidity risk

The Group actively maintains a mixture of long-term and short-term committed facilities which are designed to ensure the Group has sufficient available funds for operations and planned expansions equivalent to at least one year's forecast requirements at all times. Details of undrawn committed facilities and short-term facilities are provided in note 28.

Refinancing risk is managed under a Group policy that requires that no more than 20% of Group net borrowings should mature in any financial year.

The Group and water business have entered into covenants with lenders. While terms vary, these typically provide for limits on gearing (primarily based on the water business's regulatory capital value and Viridor Limited's EBITDA plus interest receivable on service concession arrangements) and interest cover. Existing covenants are not impacted by subsequent changes to accounting standards.

Notes to the financial statements
continued

3. Financial risk management continued

Contractual undiscounted cash flows, including interest payments, at the balance sheet date were:

	Due within 1 year £m	Due between 1 and 2 years £m	Due between 2 and 5 years £m	Over 5 years £m	Total £m
Group					
31 March 2020					
Non-derivative financial liabilities					
Borrowings excluding lease liabilities	**40.7**	**244.4**	**511.9**	**1,479.3**	**2,276.3**
Interest payments on borrowings	**59.1**	**56.3**	**135.8**	**618.2**	**869.4**
Lease liabilities including interest	**39.5**	**94.4**	**150.9**	**1,750.6**	**2,035.4**
Trade and other payables	**115.3**	**–**	**–**	**–**	**115.3**
Guarantees	**197.1**	**–**	**–**	**–**	**197.1**
Derivative financial liabilities					
Derivative contracts – net payments/(receipts)	**7.0**	**7.3**	**20.3**	**0.7**	**35.3**
31 March 2019					
Non-derivative financial liabilities					
Borrowings excluding finance lease liabilities	86.8	41.1	672.8	1,288.0	2,088.7
Interest payments on borrowings	60.5	59.4	156.4	681.0	957.3
Lease liabilities including interest	92.2	55.5	242.1	2,153.9	2,543.7
Trade and other payables	298.0	–	–	–	298.0
Guarantees	201.7	–	–	–	201.7
Derivative financial liabilities					
Derivative contracts – net payments/(receipts)	3.8	(3.7)	(12.0)	(65.1)	(77.0)
Company					
31 March 2020					
Non-derivative financial liabilities					
Borrowings excluding intercompany borrowings	**6.1**	**204.4**	**393.1**	**537.9**	**1,141.5**
Interest payments on borrowings	**33.1**	**30.9**	**61.3**	**64.8**	**190.1**
Trade and other payables	**19.8**	**–**	**–**	**–**	**19.8**
Guarantees	**658.0**	**–**	**–**	**–**	**658.0**
Derivative financial liabilities					
Derivative contracts – net payments	**0.6**	**0.7**	**1.5**	**0.3**	**3.1**
31 March 2019					
Non-derivative financial liabilities					
Borrowings excluding intercompany borrowings	51.8	6.1	551.7	431.9	1,041.5
Interest payments on borrowings	33.6	32.8	77.9	81.5	225.8
Trade and other payables	15.8	–	–	–	15.8
Guarantees	763.2	–	–	–	763.2
Derivative financial liabilities					
Derivative contracts – net payments	0.2	0.2	0.3	–	0.7

No liability is expected to arise in respect of the guarantees noted above. Guarantees are analysed in note 42.

ii) Market risk

Of the Group's interest-bearing liabilities at the year end 55% (2019 63%) were at fixed rates after the impact of financial derivatives in order to manage the risk of fluctuating interest rates impacting the financial performance of the Group. While this level is below our policy of maintaining at least 60% of interest-bearing liabilities at fixed rates, it reflects considerations regarding Pennon's debt levels following the Group's announcement of the strategic review and the subsequent announcement of the proposed sale of Viridor. 19% (2019 18%) of the Group's net borrowings are RPI index-linked. The interest rate for index-linked debt is based upon an RPI measure, which is also used in determining the amount of income from customers in South West Water. Overall around 76% of the Group's debt is fixed or index-linked, the Group uses a combination of fixed rate, index-linked borrowings and fixed rate interest swaps as cash flow hedges of future variable interest payments to achieve this. The notional principal amounts of the interest rate swaps are used to determine settlement under those swaps and are not therefore an exposure for the Group. These instruments are analysed in note 23.

The Group is primarily exposed to the UK's benchmark interest rate, GBP LIBOR, within its hedge accounting relationships, which are subject to interest rate benchmark reform. The Group also has a small amount of Euro denominated debt on which the foreign currency risk has been managed through cross currency swaps.

The Group has closely monitored the market and the output from the various industry working groups managing the transition to new benchmark interest rates. The Financial Conduct Authority (FCA) has made clear that, at the end of 2021, it will no longer seek to persuade, or compel, the banks to submit to LIBOR.

During 2019/20 the Group has converted a LIBOR revolving credit facility (RCF) to a Sterling Overnight Index Average (SONIA) linked RCF, this was to address the documentary changes and allow the Group to test the changes in the Treasury management system. Further work continues to ensure the Group is well placed to amend the debt portfolio and it is expected that later this year our relationship banks will no longer provide LIBOR-linked products.

3. **Financial risk management** continued

Below are the details of the hedging instruments and hedged items in scope of the amendments to IFRS 7 and 9 due to interest rate benchmark reform, by hedge type. The terms of the hedged items listed match those of the corresponding hedging instruments.

Hedge type	Instrument type	Maturing between	Nominal £m	Hedged item
Fair value hedges	Pay six-month UK benchmark rate (GBP LIBOR), receive sterling fixed cross currency swap	2020 – 2026	16	Fixed-rate Euro denominated financial instrument of the same maturity and nominal as the swap
Cash flow hedges	Receive three-month UK benchmark rate (GBP LIBOR), pay GBP fixed interest rate swap	2020 – 2027	958	UK benchmark rate (GBP LIBOR) issued financial instruments of the same nominals as the swaps
	Receive six-month UK benchmark rate (GBP LIBOR), pay GBP fixed interest rate swap	2020 – 2025	150	UK benchmark rate (GBP LIBOR) issued financial instruments of the same nominals as the swaps
	Receive six-month EURIBOR, pay GBP fixed cross currency swap	2021	26.4	Euro denominated financial instruments issued of the same maturity and nominals as the swaps

The Group will continue to apply the amendments to IFRS 9 until the uncertainty arising from the interest rate benchmark reforms with respect to the timing and the amount of the underlying cash flows that the Group is exposed ends. The Group has assumed that this uncertainty will not end until alternative language has been agreed with the counterparties and is dependent on the outcome of the introduction of fallback provisions and the clauses negotiated with lenders.

The Group has no significant interest-bearing assets upon which the net return fluctuates from market risk. Deposit interest receivable is expected to fluctuate in line with interest payable on floating rate borrowings. Consequently the Group's income and cash generated from operations (note 38) are independent of changes in market interest rates.

For 2020 if interest rates on variable net borrowings had been on average 0.5% higher/lower with all other variables held constant, post-tax profit for the year and equity would have increased/decreased by £2.4 million (2019 £2.4 million), for the equity sensitivity fair value, with derivative impacts excluded.

For 2020 if RPI on index-linked borrowings had been on average 0.5% higher/lower with all other variables held constant, post-tax profit for the year and equity would have decreased/increased by £2.0 million (2019 £2.0 million).

Foreign currency risk occurs at transactional and translation level from borrowings and transactions in foreign currencies. These risks are managed through forward contracts, which provide certainty over foreign currency risk.

iii) Credit risk

Credit counterparty risk arises from cash and cash deposits, derivative financial instruments and exposure to customers, including outstanding receivables. Further information on the credit risk relating to trade and other receivables is given in notes 19 and 22.

Counterparty risk arises from the investment of surplus funds and from the use of derivative financial instruments. The Board has agreed a policy for managing such risk which is controlled through credit limits, counterparty approvals, and rigorous monitoring procedures.

The Group has no other significant concentration of credit risk. The Group's surplus funds are managed by the Group's treasury function and are usually placed in short-term fixed interest deposits or the overnight money markets. Deposit counterparties must meet Board approved minimum criteria based on their short-term credit ratings and therefore of good credit quality.

(b) Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to minimise the cost of capital.

The Group's policy is to have a minimum of 12 months pre-funding of projected capital expenditure. At 31 March 2020 the Group had cash and facilities, including restricted funds, of £1.6 billion, meeting this objective.

In order to maintain or adjust the capital structure, the Group seeks to maintain a balance of returns to shareholders through dividends and an appropriate capital structure of debt and equity for each business segment and the Group.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net borrowings divided by total capital. Net borrowings are analysed in note 39 and calculated as total borrowings less cash and cash deposits. Total capital is calculated as total shareholders' equity plus net borrowings.

The gearing ratios at the balance sheet date were:

	2020 £m	2019 £m
Net borrowings (note 39)	**3,048.9**	3,079.5
Total equity	**1,712.1**	1,679.8
Total capital	**4,761.0**	4,759.3
Gearing ratio	**64.0%**	64.7%

The water segment is also monitored on the basis of the ratio of its net borrowings to regulatory capital value. Ofwat's notional gearing target for the K7 (2020-25) regulatory period is set at 60.0%.

	Water business	
	2020 £m	2019 £m
Regulatory capital value	**3,572.5**	3,504.7
Net borrowings	**2,307.2**	2,062.6
Net borrowings/regulatory capital value	**64.6%**	58.9%

The Group has entered into covenants with lenders and, while terms vary, these typically provide for limits on gearing and interest cover. The Group has been in compliance with its covenants during the year.

Notes to the financial statements
continued

3. Financial risk management continued

(c) Determination of fair values

The Group uses the following hierarchy for determining the fair value of financial instruments by valuation technique:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1)
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2)
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

The Group's financial instruments are valued principally using level 2 measures as analysed in note 23.

The fair value of financial instruments not traded in an active market (for example over-the-counter derivatives) is determined by using valuation techniques. A variety of methods and assumptions are used based on market conditions existing at each balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows.

The carrying values, less expected credit losses, of trade receivables and payables are assumed to approximate to their fair values.

4. Critical accounting judgements and estimates

The Group's principal accounting policies are set out in note 2. Management is required to exercise significant judgement and make use of estimates and assumptions in the application of these policies. Estimates are based on factors including historical experience and expectations of future events that management believe to be reasonable. However, given the judgemental nature of such estimates, actual results could be different from the assumptions used.

Estimates impacting continuing operations

Provision for doubtful debts

The Group has a material level of exposure to collection of trade receivables. Provisions in respect of these balances are calculated with reference to historical credit loss experience, adjusted for forward-looking factors which by their nature are subject to uncertainty. Analysis of actual recovery compared with provisioning levels have not, to date, resulted in material variances.

Under its regular review procedures at the balance sheet date, the Group applies a simplified approach in calculating ECLs for trade receivables and contract assets. Therefore, the Group does not track changes in credit risk but instead recognises a loss allowance based on lifetime ECLs at each reporting date. Each subsidiary has established a provision matrix that is informed by its historical credit loss experience, adjusted for forward-looking factors specific to the receivables and the economic environment.

In light of the broad economic challenges arising from the COVID-19 pandemic, part of the assessment of ECLs has been focused on the potential impact from the pandemic. Considerations in this assessment have included the type of customers, whether they conduct essential business operations, are linked to central or regional government and past experience of behaviours in challenging economic times. The precise quantum of the impact of the pandemic on both the Group's business and household customers is subject to significant estimate at the current time.

The actual level of debt collected may differ from the estimated levels of recovery. As at 31 March 2020 the Continuing Group's current trade receivables were £241.9 million, against which £106.1 million had been provided for ECLs (note 22). The provision for ECLs includes a non-underlying charge of £7.9 million in relation to the impact of COVID-19. At 31 March 2020, the Disposal Group's current trade receivables were £96.8 million, against which £2.9 million had been provided for ECLs. £1.1 million of the Disposal Group's provision represents a non-underlying charge in respect of COVID-19. As at 31 March 2019, the Group's current trade receivables were £360.2 million against which £99.0 million had been provided for ECLs.

Retirement benefit obligations

The Group operates defined benefit pension schemes for which actuarial valuations are carried out as determined by the trustees at intervals of not more than three years. The most recent triennial valuation of the main scheme was as at 31 March 2019 and has recently been concluded, the outcome of which is summarised in note 30.

The pension cost and liabilities under IAS 19 are assessed in accordance with Directors' best estimates using the advice of an independent qualified actuary and assumptions in the latest actuarial valuation. The assumptions are based on member data supplied to the actuary and market observations for interest rates and inflation, supplemented by discussions between the actuary and management. The mortality assumption uses a scheme-specific calculation based on CMI 2019 actuarial tables with an allowance for future longevity improvement. The principal assumptions used to measure schemes' liabilities, sensitivities to changes in those assumptions and future funding obligations are set out in note 30.

Taxation

As at 31 March 2020, the Continuing Group is reporting a current tax receivable of £1.9 million, reduced from £19.1 million in 2018/19, which includes £1.2 million receivable related to prior year tax items. The balance at 31 March 2020 excludes a current tax liability of £1.0 million in respect of the Disposal Group and this amount is included within liabilities associated with assets classified as held for sale.

Judgements impacting continuing operations

Non-underlying items

In establishing which items are disclosed separately as non-underlying, to enable a full understanding of the Group's financial performance, the Directors exercise their judgement in assessing the size, nature or incidence of specific items. See note 6 for further details.

4. Critical accounting judgements and estimates continued

Estimates impacting measurement of assets and liabilities held for sale

Environmental and landfill restoration provisions

Environmental control and aftercare costs are incurred during the operational life of each landfill site and for a considerable period thereafter. The period of aftercare post-closure and the level of costs expected are uncertain and can vary significantly from site to site. Key factors are the type of waste, the speed at which it decomposes, the volume of leachate requiring treatment and regulatory requirements specific to the site. The amounts expected to be incurred are based on landfill site operating lives, taking account of the anticipated decline in landfill activity.

The provisions are based on latest assumptions reflecting recent historic data and future cost estimates.

The aftercare provision is particularly sensitive to the estimated volumes of leachate and their associated cost, together with the discount rate used to establish the provision.

The provisions are recognised in the financial statements at the net present value of the estimated future expenditure required to settle the Group's obligations. A discount rate is applied to recognise the time value of money and is unwound over the life of the provision. This is included in the income statement as a financial item within finance costs.

Viridor assume an aftercare period of 60 years in calculating provision values. This is considered reasonable by management, is comparable to peers in the waste business and is consistent with Environment Agency bond periods.

The impact of a 0.1% change in discount rate is estimated to be in the region of £2.5 million.

As at 31 March 2020, the Group's environmental and landfill restoration provisions were £201.2 million (2019 £209.6 million) (note 32), which has now been transferred to liabilities associated with assets classified as held for sale (note 46).

Where a restoration provision is an integral part of a landfill site's future economic benefits, an asset is recognised and depreciated in accordance with the Group's depreciation policy. As at 31 March 2020 these assets had a net book value of £27.3 million (2019 £30.8 million) (note 17), which has now been transferred to liabilities associated with assets classified as held for sale (note 46).

Service concession arrangements

Consideration from public sector entities for the operation of waste management service concessions is treated as contract receivables or other intangible assets, depending upon the right to receive cash from the asset. At the balance sheet date the Group recognised contract receivables of £202.4 million (2019 £188.3 million) and other intangible assets of £86.9 million (2019 £90.6 million) in relation to its service concession arrangements, which have been transferred to assets classified as held for sale (note 46).

Consideration relating to contract receivables is split between profit on the construction of assets, operation of the service and provision of finance recognised as interest receivable. Management's judgement is used in the allocation between these three elements, this assessment reflects external market conditions according to the type of service provided and project specific cash flow expectations, including the recovery of costs from the original contractor on our Glasgow concession.

Retirement benefit obligations

The Group operates defined benefit pension schemes for which actuarial valuations are carried out as determined by the trustees at intervals of not more than three years. The most recent triennial valuation of the main scheme was as at 31 March 2019 and has recently been concluded, the outcome of which is summarised in note 30.

The pension cost and liabilities under IAS 19 are assessed in accordance with Directors' best estimates using the advice of an independent qualified actuary and assumptions in the latest actuarial valuation. The assumptions are based on member data supplied to the actuary and market observations for interest rates and inflation, supplemented by discussions between the actuary and management. The mortality assumption uses a scheme-specific calculation based on CMI 2019 actuarial tables with an allowance for future longevity improvement. The principal assumptions used to measure schemes' liabilities, sensitivities to changes in those assumptions and future funding obligations are set out in note 30.

Taxation

The Group continues to have a small number of ongoing uncertain tax items primarily relating to the interpretation of tax legislation regarding different tax aspects of its ERFs. This is part of the normal course of business and the Group has paid in full the tax HMRC interpret as due, and therefore would benefit by a cash refund of up to £24.0 million (2018/19 £26.2 million) should these tax items be concluded in the Group's favour. The Group is continuing to work towards resolution of these matters with HMRC. The amount of the cash refund reduces over time as the uncertain tax items mainly relate to timing issues of when the tax is due.

Judgements impacting assets and liabilities held for resale

Glasgow Recycling and Renewable Energy Centre (GRREC)

Total spend to bring the project into full operation was on the project since commencement has been £273.0 million, comprising the original target of £155.0 million, a further £21.0 million invested to provide additional throughput capacity and £97.0 million to address remediation and non-conformities. Viridor is contractually entitled to recover the incremental remediation and non-conformities spend, including from the original contractor, Interserve Construction Limited, under certain circumstances. The Group believes these circumstances have been met for a substantial element which is recoverable from Interserve. While Interserve disputes the amount due, dialogue with Interserve is ongoing, alongside the Group continuing to legally pursue the matter.

The associated contract with Glasgow City Council is accounted for in accordance with IFRIC 12 service concession arrangements and the spend on the project of £273.0 million has contributed £117.0 million to a financial asset, £84.0 million to an intangible asset and an amount contractually due from Interserve of £72.0 million (accounted for in accordance with IFRS 9). In line with IFRS 9, the Group has recorded credit related provisions recognising that Interserve's financial condition has been under stress. The Group has considered all relevant available public information concerning Interserve and at 31 March 2020 recognises a provision of £28.3 million, resulting in a net receivable due of £43.7 million (2019 £43.3 million). Due to uncertainty and the level of judgement associated with the provision related to the specific recovery from Interserve, it is possible the final outcome may differ from the net receivable recognised, with the boundaries for the possible outcome being zero and £72.0 million.

Non-underlying items

In establishing which items are disclosed separately as non-underlying, to enable a full understanding of the Group's financial performance, the Directors exercise their judgement in assessing the size, nature or incidence of specific items. See note 6 for further details.

Other estimates

During the year, management reassessed the critical estimates and resolved that the level of estimation for revenue recognition of accrued revenue relating to water, waste and sale of electricity was no longer considered critical as the estimates are largely calculated on a systematic basis and have not, to date, resulted in a material adjustment within the following 12-month period. However, management consider the total level of estimation of accrued revenue relating to water, waste and sale of electricity to be material and highlight this as a material other estimate.

Notes to the financial statements
continued

5. Segmental information

Operating segments are reported in a manner consistent with internal reporting provided to the Chief Operating Decision-Maker (CODM), which has been identified as the Pennon Group plc Board. The earnings measures below are used by the Board in making decisions.

The water business comprises the regulated water and wastewater services undertaken by South West Water. The non-household retail business comprises the services provided by Pennon Water Services in the non-household water and wastewater retail market which, while regulated, is open to competition. Segment assets include goodwill and other intangible assets, property, plant and equipment, inventories, trade and other receivables and cash and cash deposits. Segment liabilities comprise operating liabilities and borrowings and exclude taxation. The other segment liabilities include the Company's financing arrangements and Group taxation liabilities. Capital expenditure comprises additions to property, plant and equipment, including additions resulting from acquisitions through business combinations.

Following the Group entering into a formal sale agreement on 18 March 2020 to dispose of Viridor, the waste management business has been accounted for as a discontinued operation. In accordance with IFRS 5 'Non-current assets held for sale and discontinued operations', the net results of the waste management segment are presented within discontinued operations in the Group income statement (for which comparatives have been restated) and the assets and liabilities of these operations are presented separately as assets held for sale in the Group balance sheet. The waste management business has been a significant reporting segment during the year ended 31 March 2020 and will continue to be reported separately to the CODM until the expected completion of the disposal transaction in the summer of 2020 following approval by the Group's shareholders.

	2020 £m	2019 (restated) £m
Revenue from continuing operations		
Water	**570.3**	581.0
Non-household retail	**173.5**	173.7
Other	**10.1**	10.5
Less intra-segment trading[1]	**(117.2)**	(132.6)
	636.7	632.6
Revenue from discontinued operations		
Waste management	**757.8**	852.7
Other	**9.4**	10.9
Less intra-segment trading[1]	**(14.0)**	(18.0)
	753.2	845.6
Pro forma total revenue	**1,389.9**	1,478.2
Operating profit before depreciation, amortisation and non-underlying items (EBITDA) from continuing operations		
Water	**364.2**	367.1
Non-household retail	**1.9**	1.0
Other	**(0.8)**	(0.8)
	365.3	367.3
EBITDA from discontinued operations – Waste management	**198.1**	178.9
	563.4	546.2
Operating profit before non-underlying items from continuing operations		
Water	**245.4**	251.1
Non-household retail	**1.2**	0.3
Other	**(1.1)**	(1.3)
	245.5	250.1
Operating profit from discontinued operations – Waste management	**116.0**	100.9
	361.5	351.0
Profit before tax and non-underlying items from continuing operations		
Water	**174.0**	180.6
Non-household retail	**(0.4)**	(1.6)
Other	**9.4**	12.7
	183.0	191.7
Profit before tax from discontinued operations – Waste management	**104.6**	88.5
	287.6	280.2
Profit before tax from continuing operations		
Water	**189.0**	184.6
Non-household retail	**(5.4)**	(1.6)
Other	**9.5**	18.4
	193.1	201.4
Profit before tax from discontinued operations – Waste management	**108.4**	58.9
	301.5	260.3

(1) Intra-segment transactions between and to different segments is under normal market-based commercial terms and conditions. Intra-segment revenue of the other segment is at cost.

5. Segmental information continued

	Water £m	Non-household retail £m	Other £m	Total Continuing Group (pre-eliminations) £m	Disposal Group (pre-eliminations) £m	Eliminations £m	Group £m
Balance sheet							
31 March 2020							
Assets (excluding investments in joint ventures)	3,654.6	54.6	1,928.0	5,637.2	2,618.4	(1,553.2)	6,702.4
Investments in joint ventures	–	–	–	–	60.1	–	60.1
Total assets	3,654.6	54.6	1,928.0	5,637.2	2,678.5	(1,553.2)	6,762.5
Liabilities	(2,854.6)	(54.2)	(1,727.6)	(4,636.4)	(1,967.2)	1,553.2	(5,050.4)
Net assets	800.0	0.4	200.4	1,000.8	711.3	–	1,712.1
31 March 2019							
Assets (excluding investments in joint ventures)	3,690.2	64.6	1,659.0	5,413.8	2,464.8	(1,470.2)	6,408.4
Investments in joint ventures	–	–	–	–	51.1	–	51.1
Total assets	3,690.2	64.6	1,659.0	5,413.8	2,515.9	(1,470.2)	6,459.5
Liabilities	(2,762.2)	(58.7)	(1,685.8)	(4,506.7)	(1,743.2)	1,470.2	(4,779.7)
Net assets	928.0	5.9	(26.8)	907.1	772.7	–	1,679.8

Segment liabilities of the water and waste management segments comprise of operating liabilities and borrowings. The other segment includes company only assets and liabilities as well as Group taxation liabilities and should be considered in conjunction with the eliminations column. Note 46 provides details of this Disposal Group which excludes intercompany receivables of £3.2 million and intercompany payables of £1,210.9 million which will be settled on completion as part of the sale being completed on a debt free basis.

	Notes	Water £m	Non-household retail £m	Other and eliminations £m	Total from continuing operations £m	Discontinued operations Waste management £m	Group £m
Other information							
31 March 2020							
Amortisation of other intangible assets	7	0.4	0.2	–	0.6	4.1	4.7
Capital expenditure	17	161.1	–	0.1	161.2	165.7	326.9
Depreciation	7	118.3	0.5	0.4	119.2	78.0	197.2
Finance income	8	2.3	–	1.8	4.1	22.5	26.6
Finance costs (before non-underlying items)	8	73.4	0.3	(7.1)	66.6	48.7	115.3
31 March 2019							
Amortisation of other intangible assets	7	0.5	0.2	–	0.7	4.5	5.2
Capital expenditure	17	154.0	–	0.1	154.1	233.1	387.2
Depreciation	7	115.5	0.6	0.4	116.5	73.5	190.0
Finance income	8	2.3	–	1.2	3.5	20.0	23.5
Finance costs (before non-underlying items)	8	72.8	1.9	(12.8)	61.9	44.8	106.7

Finance income and costs above reflect the segment in which the amounts arise and exclude inter-company transactions.

The grouping of revenue streams by how they are affected by economic factors, as required by IFRS 15, is as follows:

	Water	Non-household retail	Other		Waste management (WM)					
Year ended 31 March 2020	UK total £m	UK total £m	UK total £m	Total from continuing operations £m	UK £m	Rest of EU £m	China £m	Rest of world £m	Total from discontinued operations WM £m	Total £m
Segment revenue	570.3	173.5	10.1	753.9	741.3	11.8	3.8	10.3	767.2	1,521.1
Inter-segment revenue	(106.4)	(0.9)	(9.9)	(117.2)	(14.0)	–	–	–	(14.0)	(131.2)
Revenue from external customers	463.9	172.6	0.2	636.7	727.3	11.8	3.8	10.3	753.2	1,389.9
Significant service lines										
Water	463.9	–	–	463.9	–	–	–	–	–	463.9
Non-household retail	–	172.6	–	172.6	–	–	–	–	–	172.6
Waste management services	–	–	–	–	567.2	–	–	–	567.2	567.2
Energy	–	–	–	–	109.2	–	–	–	109.2	109.2
Recyclate	–	–	–	–	50.9	11.8	3.8	10.3	76.8	76.8
Other	–	–	0.2	0.2	–	–	–	–	–	0.2
	463.9	172.6	0.2	636.7	727.3	11.8	3.8	10.3	753.2	1,389.9

Notes to the financial statements
continued

5. Segmental information continued

Year ended 31 March 2019	Water UK total £m	Non-household retail UK total £m	Other UK total £m	Total from continuing operations £m	Waste management (WM) UK £m	Rest of EU £m	China £m	Rest of world £m	Total from discontinued operations WM £m	Total £m
Segment revenue	581.0	173.7	21.4	776.1	802.3	13.8	25.6	11.0	852.7	1,628.8
Inter-segment revenue	(124.9)	(4.0)	(21.4)	(150.3)	(0.3)	–	–	–	(0.3)	(150.6)
Revenue from external customers	456.1	169.7	–	625.8	802.0	13.8	25.6	11.0	852.4	1,478.2
Significant service lines										
Water	456.1	–	–	456.1	–	–	–	–	–	456.1
Non-household retail	–	169.7	–	169.7	–	–	–	–	–	169.7
Waste management services	–	–	–	–	655.8	–	–	–	655.8	655.8
Energy	–	–	–	–	88.9	–	–	–	88.9	88.9
Recyclate	–	–	–	–	57.3	13.8	25.6	11.0	107.7	107.7
	456.1	169.7	–	625.8	802.0	13.8	25.6	11.0	852.4	1,478.2

The Group's country of domicile is the United Kingdom and this is the country in which it generates the majority of its revenue. The Group's non-current assets are all located in the United Kingdom.

6. Non-underlying items

Non-underlying items are those that in the Directors' view should be separately disclosed by virtue of their size, nature or incidence to enable a full understanding of the Group's financial performance in the year and business trends over time. The presentation of results is consistent with internal performance monitoring.

	Notes	**Continuing operations 2020 £m**	**Discontinued operations 2020 £m**	**Pro forma Total 2020 £m**	Continuing operations 2019 £m	Discontinued operations 2019 £m	Pro forma Total 2019 £m
Operating costs							
Pension past service credit[1]		**–**	**4.9**	**4.9**	–	–	–
COVID-19 provision for expected credit losses[2]		**(7.9)**	**(1.1)**	**(9.0)**	–	–	–
Pension past service cost (GMP equalisation impact)[3]		**–**	**–**	**–**	(2.1)	(0.9)	(3.0)
Provision for receivable (due from Interserve in respect of Glasgow Recycling and Renewable Energy Centre)[4]		**–**	**–**	**–**	6.0	(28.7)	(22.7)
Earnings before interest, tax, depreciation and amortisation		**(7.9)**	**3.8**	**(4.1)**	3.9	(29.6)	(25.7)
Remeasurement of fair value movement in derivatives[5]	8	**18.0**	**–**	**18.0**	5.8	–	5.8
Net tax credit arising on non-underlying items above		**(1.9)**	**(0.7)**	**(2.6)**	(0.7)	5.7	5.0
Deferred tax change in rate[6]	9	**(30.3)**	**(10.3)**	**(40.6)**	–	–	–
Net non-underlying (charge)/credit		**(22.1)**	**(7.2)**	**(29.3)**	9.0	(23.9)	(14.9)

(1) Upon cessation of the Greater Manchester contract, Viridor employees delivering this contract transferred to the new contract provider. Accordingly, defined benefit pension commitments for these employees are in the process of being transferred. The past service credit of £4.9 million (2019 £nil) reflects curtailment and other gains resulting from transferring employees moving from an active to deferred status in these schemes.

(2) In response to the COVID-19 pandemic a detailed expected credit loss review has been undertaken. Economic and credit conditions are worsening, however the UK Government continues to implement economic measures to support the wider economy. As a result of the review a Group provision of £9.0 million has been recognised. The charge is considered non-underlying due to its size and nature.

(3) On 26 October 2018, the High Court of Justice of England and Wales issued a judgment in a claim regarding the rights of female members of certain pension schemes to equality of treatment in relation to pension benefits (GMP equalisation). The judgment concluded that the claimant is under a duty to amend the schemes in order to equalise benefits for men and women in relation to guaranteed minimum pension benefit. The issues determined by the judgment arise in relation to many other occupational pension schemes.
The Group estimates, with advice from the Group's corporate actuary, that scheme liabilities will increase by an estimated £3.0 million as a result of the judgment. This cost was recognised as a past service cost in the income statement for the year ended 31 March 2019. These charges are considered non-underlying due to size and non-recurring nature.

(4) The financial statements recognise a gross receivable of £72.0 million from Interserve Construction Limited in relation to rectifications and completion costs for GRREC. During the financial year ended 31 March 2019, Interserve Plc (holding company of Interserve Construction Limited) entered into administration. The operating company, Interserve Construction Limited with whom we contracted, is currently continuing to trade. As a result of the lack of certainty around the future of Interserve's business, and in accordance with IFRS 9, we have sought to make an appropriate market-based credit assessment using the latest public information available. Consequently, a provision of £22.7 million was recognised in 2018/19 against the receivable, resulting in a total cumulative provision at 31 March 2019 of £28.7 million. The charge is considered non-underlying due to its size and non-recurring nature. The financial stability of Interserve Construction Limited is judged to be outside the control of Pennon Group.

(5) In the year a gain of £18.0 million has been recognised relating to non-cash derivative fair value movements associated with derivatives that are not designated as being party to an accounting hedge relationship (2019 credit of £5.8 million). In the year these instruments were early settled, as the instruments no longer met the Group's accounting hedging requirements, and this has locked in the mark to market gain. These movements are non-underlying due to the nature of the item being market dependent and potentially can be significant in value (size).

(6) Following the Chancellor's Budget on 11 March 2020, the UK headline corporation tax rate will remain at 19%. It was previously set to reduce to 17% from 1 April 2020 and that change has now been cancelled. All deferred tax assets and liabilities have therefore been recalculated to crystallise at 19%, resulting in a non-underlying deferred tax change in the year of £40.6 million. The change was substantively enacted on 17 March 2020. This charge is considered non-underlying due to it arising from a material legislative change, and its treatment is consistent with that applied in relation to previous changes in the corporation tax rate.

7. Operating costs

	Notes	2020 £m	2019 (restated) £m
Employment costs before non-underlying items	13	**70.0**	67.2
Raw materials and consumables		**14.9**	15.0
Other operating expenses before non-underlying items include:			
Profit on disposal of property, plant and equipment		**(0.4)**	(1.6)
Operating lease rentals payable		**–**	3.1
Short-term/low value asset lease expense		**1.2**	–
Research and development expenditure		**0.1**	0.2
Trade receivables impairment	22	**11.4**	2.9
Depreciation of property, plant and equipment:			
– Owned assets		**73.2**	77.0
– Under leases (2019 finance leases only)		**46.0**	39.5
Amortisation of other intangible assets	16	**0.6**	0.7

Operating costs include a charge of £7.9 million relating to non-underlying items, as detailed in note 6.

The costs above are exclusive of amounts relating to discontinued operations.

Fees payable to the Company's auditor in the year were:

	2020 £000	2019 £000
Fees payable to the Company's auditor and its associates for the audit of parent company and consolidated financial statements	**143**	102
Fees payable to the Company's auditor and its associates for other services:		
The audit of Company's subsidiaries	**784**	621
Audit-related assurance services	**50**	50
Other non-audit services	**85**	118
Total fees	**1,062**	891
Fees payable to the Company's auditor in respect of Pennon Group pension schemes:		
Audit	**52**	50

Expenses reimbursed to the auditor in relation to the audit of the Group were £39,000 (2019 £63,000).

A description of the work of the Audit Committee is set out in its report on pages 84 to 87 which includes an explanation of how the auditor's objectivity and independence are safeguarded when non-audit services are provided by the auditor's firm.

8. Net finance costs

		2020			2019 (restated)		
	Notes	Finance cost £m	Finance income £m	Total £m	Finance cost £m	Finance income £m	Total £m
Cost of servicing debt							
Bank borrowing and overdrafts		**(28.1)**	**–**	**(28.1)**	(23.1)	–	(23.1)
Interest element of lease payments (2019 interest element of finance lease payments)		**(35.6)**	**–**	**(35.6)**	(35.4)	–	(35.4)
Other finance costs		**(2.7)**		**(2.7)**	(2.4)	–	(2.4)
Interest receivable		**–**	**4.1**	**4.1**	–	3.5	3.5
		(66.4)	**4.1**	**(62.3)**	(60.9)	3.5	(57.4)
Notional interest							
Retirement benefit obligations	30	**(0.2)**	**–**	**(0.2)**	(1.0)	–	(1.0)
Net finance cost before non-underlying items		**(66.6)**	**4.1**	**(62.5)**	(61.9)	3.5	(58.4)
Non-underlying items							
Fair value remeasurement of non-designated derivative financial instruments providing commercial hedges	6	**18.0**	**–**	**18.0**	5.8	–	5.8
Net finance cost after non-underlying items		**(48.6)**	**4.1**	**(44.5)**	(56.1)	3.5	(52.6)

In addition to the above, finance costs of £2 million have been capitalised on qualifying assets included in property, plant and equipment (2019 restated £2.9 million).

Excluded from the amounts above are net finance costs relating to discontinued operations of £26.2 million (2019 £24.8 million), consisting of finance income of £22.5 million (2019 £20.0 million) and finance costs of £48.7 million (2019 £44.8 million).

Notes to the financial statements
continued

9. Taxation

	Notes	Before non-underlying items 2020 £m	Non-underlying items (note 6) 2020 £m	Total 2020 £m	Before non-underlying items 2019 £m	Non-underlying items (note 6) 2019 £m	Total 2019 £m
Analysis of charge in year							
Current tax charge/(credit)		**18.8**	**15.3**	**34.1**	29.4	(5.5)	23.9
Deferred tax – other		**33.2**	**(12.7)**	**20.5**	13.3	0.5	13.8
Deferred tax arising on change of rate of corporation tax		**–**	**40.6**	**40.6**	–	–	–
Total deferred tax charge		**33.2**	**27.9**	**61.1**	13.3	0.5	13.8
Tax charge/(credit) for year		**52.0**	**43.2**	**95.2**	42.7	(5.0)	37.7

	Notes	Continuing operations 2020 £m	Discontinued operations 2020 £m	Pro forma Total 2020 £m	Continuing operations 2019 £m	Discontinued operations 2019 £m	Pro forma Total 2019 £m
Analysis of charge in year							
Current tax charge/(credit)		**43.8**	**(9.7)**	**34.1**	29.6	(5.7)	23.9
Deferred tax – other		**(3.5)**	**24.0**	**20.5**	3.2	10.6	13.8
Deferred tax arising on change of rate of corporation tax		**30.3**	**10.3**	**40.6**	–	–	–
Total deferred tax charge		**26.8**	**34.3**	**61.1**	3.2	10.6	13.8
Tax charge for year		**70.6**	**24.6**	**95.2**	32.8	4.9	37.7

UK corporation tax is calculated at 19% (2019 19%) of the estimated assessable profit for the year.

UK corporation tax for the pro forma total group, including discontinued operations is stated after a credit relating to prior year current tax of £9.2 million (2019 credit of £3.0 million) and a prior year deferred tax charge of £6.5 million (2019 credit of £9.9 million).

The tax for the year differs from the theoretical amount which would arise using the standard rate of corporation tax in the UK of 19% (2019 19%) as follows:

	Continuing operations 2020 £m	Pro forma Total 2020 £m	Continuing operations 2019 £m	Pro forma Total 2019 £m
Reconciliation of total tax charge				
Profit before tax for continuing operations	**193.1**	**301.5**	201.4	260.3
Profit multiplied by the standard rate of UK corporation tax of 19% (2019 19%)	**36.7**	**57.3**	38.3	49.5
Effects of:				
Expenses not deductible for tax purposes	**0.4**	**1.0**	0.4	1.7
Joint venture profits not taxed	**–**	**(2.8)**	–	(2.4)
Adjustments to tax charge in respect of prior years	**3.2**	**(2.7)**	(6.6)	(12.9)
Change in UK tax rates	**30.3**	**40.6**	–	–
Depreciation charged on non-qualifying assets	**0.3**	**1.9**	1.9	3.7
Other	**(0.3)**	**(0.1)**	(1.2)	(1.9)
Tax charge for year	**70.6**	**95.2**	32.8	37.7

9. **Taxation** continued

	Continuing operations 2020 £m	Pro forma Total 2020 £m	Continuing operations 2019 £m	Pro forma Total 2019 £m
Reconciliation of current tax charge				
Profit before tax	**193.1**	**301.5**	201.4	260.3
Profit multiplied by the standard rate of UK corporation tax of 19% (2019 19%)	**36.7**	**57.3**	38.3	49.5
Effects of:				
Relief for capital allowances in place of depreciation	**(21.8)**	**(52.4)**	(22.1)	(54.2)
Disallowance of depreciation charged in the accounts	**19.5**	**32.1**	18.8	31.0
Other timing differences	**9.3**	**7.9**	(2.9)	0.2
Expenses not deductible for tax purposes	**0.4**	**1.1**	0.4	1.7
Joint venture profits not taxed	**–**	**(2.8)**	–	(2.4)
Adjustments to tax charge in respect of prior years	**(0.3)**	**(9.2)**	(4.3)	(3.0)
Depreciation charged on non-qualifying assets	**0.3**	**1.9**	1.9	3.7
Relief for capitalised interest and foreign exchange gains/losses	**(0.3)**	**(1.8)**	(0.5)	(2.6)
Current tax charge for year	**43.8**	**34.1**	29.6	23.9

The pro forma Group's current tax charge is lower than the UK headline rate of 19%, primarily due to the availability of capital allowances. Capital allowances provide tax relief when a business incurs expenditure on qualifying capital items such as plant and machinery used by the business. As an infrastructure business, these allowances help the Group to plan major investment and consequently to maintain lower customers bills, as corporation tax relief is given against the investments made.

The headline UK tax rate will now be held at 19% (rather than reducing to 17% as previously enacted) following the Chancellor's Budget on 11 March 2020. The change to remain at 19% was substantively enacted on 17 March 2020.

Joint venture profits are not subject to any additional tax within the Group as these are included on a post-tax basis already, as the joint venture entity is subject to UK tax itself.

In addition to the amounts recognised in the income statement, the following tax charges and credits were recognised:

	Continuing operations 2020 £m	Pro forma Total 2020 £m	Continuing operations 2019 £m	Pro forma Total 2019 £m
Amounts recognised directly in other comprehensive income				
Deferred tax credit on defined benefit pension schemes	**(1.5)**	**(0.1)**	(1.3)	(3.2)
Deferred tax credit on cash flow hedges	**(3.1)**	**(3.1)**	(0.1)	(0.6)
Amounts recognised directly in equity				
Deferred tax credit on share-based payments	**(0.8)**	**(1.4)**	(0.4)	(0.5)
Current tax credit on perpetual capital securities periodic return	**(1.6)**	**(1.6)**	–	–

10. **Profit of the parent company**

	2020 £m	2019 £m
Profit attributable to ordinary shareholders' equity dealt within the accounts of the parent company	**330.6**	194.8

As permitted by Section 408 of the Companies Act 2006, no income statement or statement of comprehensive income is presented for the Company.

Notes to the financial statements
continued

11. Earnings per share

Basic earnings per share are calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year, excluding those held in the employee share trust (note 36), which are treated as cancelled.

For diluted earnings per share, the weighted average number of ordinary shares in issue is adjusted to include all dilutive potential ordinary shares. The Group has two types of dilutive potential ordinary shares – those share options granted to employees where the exercise price is less than the average market price of the Company's ordinary shares during the year; and the contingently issuable shares under the Group's Performance and Co-investment Plan, the long-term incentive plan and the deferred shares element of the Annual Incentive Bonus Plan, based on performance criteria for the vesting of the awards.

The weighted average number of shares and earnings used in the calculations were:

	2020	2019
Number of shares (millions)		
For basic earnings per share	**420.2**	419.6
Effect of dilutive potential ordinary shares from share options	**1.9**	1.3
For diluted earnings per share	**422.1**	420.9

Basic and diluted earnings per ordinary share

Earnings per ordinary share before non-underlying items, deferred tax and adjusted to annualise depreciation and amortisation in the Disposal Group are presented as the Directors believe that this measure provides a more useful year on year comparison of business trends and performance. Deferred tax is excluded as the Directors believe it reflects a distortive effect of changes in corporation tax rates and the level of long-term capital investment. Following the announcement on 18 March of the proposed sale of Viridor, the assets and liabilities of the Disposal Group have been transferred to assets held for sale and in accordance with IFRS 5, the property, plant and equipment and intangible assets have not been depreciated or amortised from that date. The Directors believe that to aid comparison of earnings year on year, it is appropriate to reflect a full year's depreciation and amortisation consistent with all other revenues and costs recognised for the full year in the Disposal Group. Earnings per share have been calculated as follows:

	2020			2019		
	Profit after tax	Earnings per share		Profit after tax	Earnings per share	
Continuing and discontinued operations	£m	Basic p	Diluted p	£m	Basic p	Diluted p
Statutory earnings attributable to ordinary shareholders of the parent	**200.4**	**47.7**	**47.5**	214.3	51.1	50.9
Deferred tax charge before non-underlying items	**33.2**	**7.9**	**7.8**	13.3	3.1	3.1
Non-underlying items (net of tax)	**29.3**	**6.9**	**6.9**	14.9	3.6	3.6
Non-controlling interests' share of non-underlying items	**(1.0)**	**(0.2)**	**(0.2)**	–	–	–
Full year depreciation charge in the Disposal Group	**(2.6)**	**(0.6)**	**(0.6)**	–	–	–
Adjusted earnings	**259.3**	**61.7**	**61.4**	242.5	57.8	57.6

	2020			2019		
	Profit after tax	Earnings per share		Profit after tax	Earnings per share	
Continuing operations	£m	Basic p	Diluted p	£m	Basic p	Diluted p
Statutory earnings attributable to ordinary shareholders of the parent	**116.6**	**27.7**	**27.6**	160.3	38.2	38.1
Deferred tax charge before non-underlying items	**10.1**	**2.4**	**2.4**	2.5	0.6	0.6
Non-underlying items (net of tax)	**22.1**	**5.3**	**5.2**	(9.0)	(2.1)	(2.2)
Non-controlling interests' share of non-underlying items	**(1.0)**	**(0.2)**	**(0.2)**	–	–	–
Full year depreciation charge in the Disposal Group	**–**	**–**	**–**	–	–	–
Adjusted earnings	**147.8**	**35.2**	**35.0**	153.8	36.7	36.5

	2020			2019		
	Profit after tax	Earnings per share		Profit after tax	Earnings per share	
Discontinuing operations	£m	Basic p	Diluted p	£m	Basic p	Diluted p
Statutory earnings attributable to ordinary shareholders of the parent	**83.8**	**20.0**	**19.9**	54.0	12.9	12.8
Deferred tax charge before non-underlying items	**23.1**	**5.4**	**5.4**	10.8	2.5	2.6
Non-underlying items (net of tax)	**7.2**	**1.7**	**1.7**	23.9	5.7	5.7
Non-controlling interests' share of non-underlying items	**–**	**–**	**–**	–	–	–
Full year depreciation charge in the Disposal Group	**(2.6)**	**(0.6)**	**(0.6)**	–	–	–
Adjusted earnings	**111.5**	**26.5**	**26.4**	88.7	21.1	21.1

12. Dividends

	2020 £m	2019 £m
Amounts recognised as distributions to ordinary equity holders in the year		
Interim dividend paid for the year ended 31 March 2019 12.84p (2018 11.97p) per share	**54.0**	50.2
Final dividend paid for the year ended 31 March 2019 28.22p (2018 26.62p) per share	**118.6**	111.8
	172.6	162.0
Proposed dividends		
Proposed interim dividend for the year ended 31 March 2020: 13.66p per share	**57.5**	54.0
Proposed final dividend for the year ended 31 March 2020: 30.11p per share	**126.8**	118.7
	184.3	172.7

The proposed interim and final dividends have not been included as liabilities in these financial statements.

The proposed interim dividend for 2020 was paid on 3 April 2020 and the proposed final dividend is subject to approval by shareholders at the AGM.

13. Employment costs

	Notes	Continuing operations 2020 £m	Discontinued operations 2020 £m	Total 2020 £m	Continuing operations 2019 £m	Discontinued operations 2019 £m	Total 2019 £m
Wages and salaries		**67.2**	**113.7**	**180.9**	63.7	120.6	184.3
Social security costs		**7.1**	**11.5**	**18.6**	6.6	12.5	19.1
Pension costs – before non-underlying items	30	**8.5**	**13.7**	**22.2**	8.6	13.3	21.9
Pension (credit)/costs – non-underlying items	6	**–**	**(4.9)**	**(4.9)**	2.1	0.9	3.0
Share-based payments	33	**2.9**	**0.9**	**3.8**	2.5	1.1	3.6
Total employment costs		**85.7**	**134.9**	**220.6**	83.5	148.4	231.9
Charged:							
Employment costs (excluding non-underlying items) – consolidated income statement		**70.0**	**135.3**	**205.3**	67.2	138.6	205.8
Employment costs (non-underlying items) – consolidated income statement		**–**	**(4.9)**	**(4.9)**	2.1	0.9	3.0
Capital schemes – property, plant and equipment		**15.7**	**4.5**	**20.2**	14.2	8.9	23.1
Total employment costs		**85.7**	**134.9**	**220.6**	83.5	148.4	231.9

Details of Directors' emoluments are set out in note 14. There are no personnel, other than Directors, who as key management exercise authority and responsibility for planning, directing and controlling the activities of the Group. Members of other executive committees assist the Directors in their duties but do not hold authority to control the activities of the Group.

	2020	2019
Employees (average full-time equivalent number)		
The average monthly number of employees (including Executive Directors) was:		
Water	**1,623**	1,616
Non-household retail	**143**	104
Other	**101**	93
Total continuing operations	**1,867**	1,813
Waste management	**2,986**	3,426
Total – continuing and discontinued operations	**4,853**	5,239

The total number of employees (full-time equivalent) of the continuing operations at 31 March 2020 was 1,937 (2019 1,834). The total number of employees of the continuing operations and discontinued operations at 31 March 2020 was 4,801 (2019 5,382).

Notes to the financial statements
continued

14. Directors' emoluments

	2020 £000	2019 £000
Executive Directors:		
Salary	**951**	932
Performance-related bonus paid or payable	**372**	425
Share-based payments	**872**	936
Other emoluments, including payments in lieu of pension provision	**316**	307
Non-Executive Directors	**528**	508
	3,039	3,108

The cost of share-based payments represents the amount charged to the income statement, as described in note 33. The aggregate gains on vesting of Directors' share-based awards amounted to a total of £nil (2019 £nil). Total gains made by Directors on the exercise of share options were £nil (2019 £nil).

Total emoluments include £nil (2019 £nil) payable to Directors for services as directors of subsidiary undertakings.

At 31 March 2020 one Director (2019 one) is accruing retirement benefits under defined benefit pension schemes in respect of which the Group contributed £29,000 (2019 £29,000).

At 31 March 2020 no Director (2019 no) is a member of the Group's defined contribution pension scheme in respect of which the Group contributed £nil (2019 £nil).

At 31 March 2020 two Directors received payments in lieu of pension provision (2019 two).

More detailed information concerning Directors' emoluments (including pensions and the highest paid Director) and share interests is shown in the Directors' remuneration report on pages 92 to 115.

15. Goodwill

	£m
Cost:	
At 1 April 2018	385.0
At 31 March 2019	385.0
Disposals	(1.9)
Assets transferred to Disposal Group	(340.8)
At 31 March 2020	42.3
Carrying amount:	
At 1 April 2018	385.0
At 31 March 2019	385.0
At 31 March 2020	**42.3**

Goodwill acquired in a business combination is allocated at acquisition to the CGU expected to benefit from that business combination. Goodwill with a total carrying value of £340.8 million has been transferred to the Disposal Group. The remaining £42.3 million is allocated to the water business, representing the lowest level at which goodwill is monitored and tested.

Impairment testing of goodwill
The Group tests goodwill for impairment annually, or more frequently if there are any indications that impairment may have arisen.

The recoverable amount of the water business segment, for which goodwill was recognised on acquisition of Bournemouth Water in 2015, is assessed using level 2 fair value hierarchy techniques, with reference to the market value of the merged water business, using a market-based observable premium to regulated capital value.

The results of tests performed during the year demonstrate significant headroom in the water CGU, and it is judged that no reasonable change in the key assumptions would cause the carrying amount of the CGUs to exceed the recoverable amount.

16. Other intangible assets

	Service concession arrangements £m	Customer contracts £m	Patents £m	Other £m	Total £m
Cost:					
At 1 April 2018	69.6	34.3	0.2	3.6	107.7
Additions	24.7	–	–	–	24.7
At 31 March 2019	94.3	34.3	0.2	3.6	132.4
Additions	0.1	–	–	0.6	0.7
Disposals	–	(34.3)	–	(0.2)	(34.5)
Transferred to assets held for sale	(94.4)	–	–	–	(94.4)
At 31 March 2020	–	–	0.2	4.0	4.2
Accumulated amortisation:					
At 1 April 2018	0.4	32.7	0.2	1.8	35.1
Charge for year	3.3	1.2	–	0.7	5.2
At 31 March 2019	3.7	33.9	0.2	2.5	40.3
Charge for year	3.8	0.4	–	0.5	4.7
Disposals	–	(34.3)	–	(0.2)	(34.5)
Transferred to assets held for sale	(7.5)	–	–	–	(7.5)
At 31 March 2020	–	–	0.2	2.8	3.0
Carrying amount:					
At 1 April 2018	69.2	1.6	–	1.8	72.6
At 31 March 2019	90.6	0.4	–	1.1	92.1
At 31 March 2020	**–**	**–**	**–**	**1.2**	**1.2**

Assets that belong to Pennon Group plc's waste management business, Viridor, have been transferred to assets held for sale at 18 March 2020, at which point amortisation of its assets ceased.

Customer contracts were disposed in full during the year. Prior to disposal customer contracts were amortised over the useful life of each contract which at acquisition ranged between two and 15 years.

Patents have been amortised in full over their estimated useful lives which at acquisition was 13 years.

Other, including computer software, is amortised over the useful life of the assets which at acquisition was five years. The average remaining life is three years (2018 four years).

The carrying values of other intangible assets are reviewed annually or when events or changes in circumstance indicate that the carrying amounts may not be fully recoverable.

Notes to the financial statements
continued

.17. Property, plant and equipment

	Land and buildings £m	Infrastructure assets £m	Operational properties £m	Fixed and mobile plant, vehicles and computers £m	Landfill restoration £m	Construction in progress £m	Total £m
Group							
Cost:							
At 31 March 2018	555.0	1,894.5	719.3	2,855.1	82.8	555.4	6,662.1
Additions	5.2	16.4	2.2	50.0	22.8	290.6	387.2
Assets adopted at fair value	–	10.0	–	–	–	–	10.0
Grants and contributions	–	(2.2)	–	–	–	–	(2.2)
Disposals	(0.7)	(1.2)	–	(16.4)	–	–	(18.3)
Transfers/reclassifications	1.0	36.1	20.0	409.4	–	(466.5)	–
At 31 March 2019	560.5	1,953.6	741.5	3,298.1	105.6	379.5	7,038.8
IFRS 16 transition adjustment	116.6	–	–	15.6	–	–	132.2
At 1 April 2019 (adjusted for IFRS 16)	677.1	1,953.6	741.5	3,313.7	105.6	379.5	7171.0
Additions	11.6	27.8	1.8	59.6	5.3	220.8	326.9
Assets adopted at fair value	–	8.1	–	–	–	–	8.1
Grants and contributions	–	(1.8)	–	–	–	(0.9)	(2.7)
Disposals	(4.0)	(0.6)	–	(111.4)	–	–	(116.0)
Transfers/reclassifications	1.7	17.4	19.1	137.5	–	(175.7)	–
Transferred to assets held for sale	(560.6)	–	–	(1,439.4)	(110.9)	(304.6)	(2,415.5)
At 31 March 2020	125.8	2,004.5	762.4	1,960.0	–	119.1	4,971.8
Accumulated depreciation:							
At 31 March 2018	401.7	268.6	253.4	1,363.4	64.4	–	2,351.5
Charge for year	11.1	22.1	13.4	136.6	10.4	–	193.6
Disposals	(0.2)	(1.2)	–	(14.3)	–	–	(15.7)
At 31 March 2019	412.6	289.5	266.8	1,485.7	74.8	–	2,529.4
Charge for year	17.4	23.6	13.3	138.7	8.8	–	201.8
Disposals	(0.6)	(0.6)	–	(99.4)	–	–	(100.6)
Transferred to assets held for sale	(413.4)	–	–	(333.6)	(83.6)	–	(830.6)
At 31 March 2020	16.0	312.5	280.1	1,191.4	–	–	1,800.0
Net book value:							
At 31 March 2018	153.3	1,625.9	465.9	1,491.7	18.4	555.4	4,310.6
At 31 March 2019	147.9	1,664.1	474.7	1,812.4	30.8	379.5	4,509.4
At 31 March 2020	**109.8**	**1,692.0**	**482.3**	**768.6**	**–**	**119.1**	**3,171.8**

Assets that belong to Pennon Group plc's waste management business, Viridor, have been transferred to assets held for sale at a 18 March 2020 at which point depreciation of its assets ceased.

Of the total depreciation charge of £201.8 million (2019 £193.6 million), £2.6 million (2019 £1.6 million) has been charged to capital projects, £2.0 million (2019 £2.0 million) has been offset by deferred income and £197.2 million (2019 £190.0 million) has been charged against profits. Asset lives and residual values are reviewed annually. During the year borrowing costs of £10.6 million (2019 £15.2 million) have been capitalised on qualifying assets, at an average borrowing rate of 3.8% (2019 4.0%).

Groups of assets forming cash generating units are reviewed for indicators of impairment. No indicators of impairment were identified during the year.

Asset lives are reviewed annually. No significant changes were required in 2019/20.

17. Property, plant and equipment continued

Right-of-use assets held under leases included above were:

	Land and buildings £m	Infrastructure assets £m	Operational properties £m	Fixed and mobile plant, vehicles and computers £m	Construction in progress £m	Total £m
Group						
Cost:						
At 31 March 2019	3.3	428.4	471.1	672.9	5.2	1,580.9
IFRS 16 transition adjustment	116.6	–	–	15.6	–	132.2
At 1 April 2019 (adjusted for IFRS 16)	119.9	428.4	471.1	688.5	5.2	1,713.1
Additions	1.1	5.7	22.9	91.5	–	121.2
Disposals	(1.7)	(29.2)	(17.7)	(67.2)	–	(115.8)
Transfers/reclassifications	–	–	5.2	–	(5.2)	–
Transferred to assets held for sale	(84.2)	–	–	(193.8)	–	(278.0)
At 31 March 2020	35.1	404.9	481.5	519.0	–	1,440.5
Accumulated depreciation:						
At 31 March 2019	0.1	68.2	126.7	315.2	–	510.2
Charge for year	6.7	10.1	8.3	39.7	–	64.8
Disposals	(0.1)	–	–	(8.3)	–	(8.4)
Transferred to assets held for sale	(5.2)	–	–	(65.3)	–	(70.5)
At 31 March 2020 total	1.5	78.3	135.0	281.3	–	496.1
Net book amount:						
At 31 March 2019	3.2	360.2	344.4	357.7	5.2	1,070.7
At 31 March 2020	**33.6**	**326.6**	**346.5**	**237.7**	**–**	**944.4**

The net book value of right-of-use assets at 1 April 2019 was £1,202.9 million, comprising an adjustment upon transition to IFRS 16 of £132.2 million, and assets previously held under finance leases under IAS 17 of £1,070.7 million. Refer to note 45 for additional information relating to the Group's implementation of IFRS 16 'Leases'.

	Fixed and mobile plant, vehicles and computers £m
Company	
Cost:	
At 31 March 2018	0.4
Additions	0.1
At 31 March 2019	0.5
Additions	0.1
Disposals	(0.2)
At 31 March 2020	0.4
Accumulated depreciation:	
At 31 March 2018	0.2
Charge for year	–
At 31 March 2019	0.2
Charge for year	0.1
Disposals	(0.1)
At 31 March 2020	0.2
Net book value:	
At 31 March 2018	0.2
At 31 March 2019	0.3
At 31 March 2020	**0.2**

Asset lives and residual values are reviewed annually.

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18. Financial instruments by category

The accounting policies for financial instruments that have been applied to line items are:

	Notes	Fair value: Derivatives used for fair value hedging £m	Fair value: Derivatives used for cash flow hedging £m	Fair value: Derivatives not in a hedge accounting relationship £m	Amortised cost: Debt Instruments at amortised cost £m	Amortised cost: Trade receivables and trade payables £m	Total £m
Group							
31 March 2020							
Financial assets							
Trade receivables	22	**–**	**–**	**–**	**–**	**135.8**	**135.8**
Derivative financial instruments	23	**3.4**	**3.4**	**–**	**–**	**–**	**6.8**
Cash and cash deposits	25	**–**	**–**	**–**	**665.9**	**–**	**665.9**
Total		**3.4**	**3.4**	**–**	**665.9**	**135.8**	**808.5**
Financial liabilities							
Borrowings	28	**–**	**–**	**–**	**(3,714.8)**	**–**	**(3,714.8)**
Derivative financial instruments	23	**–**	**(34.1)**	**(0.2)**	**–**	**–**	**(34.3)**
Trade payables	26	**–**	**–**	**–**	**–**	**(64.2)**	**(64.2)**
Total		**–**	**(34.1)**	**(0.2)**	**(3,714.8)**	**(64.2)**	**(3,813.3)**
31 March 2019							
Financial assets							
Trade receivables	22	–	–	–	–	261.2	261.2
Other receivables	19,22	–	–	–	263.8	–	263.8
Derivative financial instruments	23	3.4	3.1	75.8	–	–	82.3
Cash and cash deposits	25	–	–	–	569.6	–	569.6
Total		3.4	3.1	75.8	833.4	261.2	1,176.9
Financial liabilities							
Borrowings	28	–	–	–	(3,649.1)	–	(3,649.1)
Derivative financial instruments	23	–	(20.5)	(0.5)	–	–	(21.0)
Trade payables	26	–	–	–	–	(127.6)	(127.6)
Other payables – amounts owed to joint ventures	26,29	–	–	–	–	(4.1)	(4.1)
Total		–	(20.5)	(0.5)	(3,649.1)	(131.7)	(3,801.8)
Company							
31 March 2020							
Financial assets							
Amounts owed by subsidiaries	19,22	**–**	**–**	**–**	**1,241.8**	**–**	**1,241.8**
Other receivables	22	**–**	**–**	**–**	**0.2**	**–**	**0.2**
Derivative financial instruments	23	**3.4**	**3.2**	**–**	**–**	**–**	**6.6**
Cash and cash deposits	25	**–**	**–**	**–**	**367.9**	**–**	**367.9**
Total		**3.4**	**3.2**	**–**	**1,609.9**	**–**	**1,616.5**
Financial liabilities							
Amounts due to subsidiaries	26	**–**	**–**	**–**	**(0.4)**	**–**	**(0.4)**
Borrowings	28	**–**	**–**	**–**	**(1,425.9)**	**–**	**(1,425.9)**
Derivative financial instruments	23	**–**	**(3.7)**	**–**	**–**	**–**	**(3.7)**
Trade payables	26	**–**	**–**	**–**	**–**	**(2.8)**	**(2.8)**
Total		**–**	**(3.7)**	**–**	**(1,426.3)**	**(2.8)**	**(1,432.8)**
31 March 2019							
Financial assets							
Amounts owed by subsidiaries	19,22	–	–	–	1,064.5	–	1,064.5
Other receivables	22	–	–	–	0.1	–	0.1
Derivative financial instruments	23	3.4	3.1	–	–	–	6.5
Cash and cash deposits	25	–	–	–	284.8	–	284.8
Total		3.4	3.1	–	1,349.4	–	1,355.9
Financial liabilities							
Amounts due to subsidiaries	26	–	–	–	(0.1)	–	(0.1)
Borrowings	28	–	–	–	(1,325.4)	–	(1,325.4)
Derivative financial instruments	23	–	(0.9)	–	–	–	(0.9)
Trade payables	26	–	–	–	–	(0.2)	(0.2)
Total		**–**	**(0.9)**	**–**	**(1,325.5)**	**(0.2)**	**(1,326.6)**

19. Other non-current assets

Non-current receivables

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Amounts owed by subsidiary undertakings	**–**	–	**1,223.5**	1,044.6
Amounts owed by related parties (note 44)	**–**	67.8	**–**	–
Service concession arrangements	**–**	188.3	**–**	–
Other receivables	**–**	0.3	**–**	–
	–	256.4	**1,223.5**	1,044.6

Non-current receivables were due:

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Between 1 and 2 years	**–**	44.0	**66.1**	48.6
Over 2 years and less than 5 years	**–**	135.2	**211.4**	148.1
Over 5 years	**–**	77.2	**946.0**	847.9
	–	256.4	**1,223.5**	1,044.6

The fair values of non-current receivables were:

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Amounts owed by subsidiary undertakings	**–**	–	**1,205.2**	1,160.4
Amounts owed by related parties	**–**	81.9	**–**	–
Service concession arrangements	**–**	188.3	**–**	–
Other receivables	**–**	0.3	**–**	–
	–	270.5	**1,205.2**	1,160.4

Excluded from the balances at 31 March 2020 above is £261.5 million relating to assets held for sale (see note 46 for further details).

20. Investments

Subsidiary undertakings

	£m
Company	
At 1 April 2018	1,980.8
At 31 March 2019	1,980.8
Transferred to assets held for sale	(1,135.6)
At 31 March 2020	**845.2**

The recoverable amount of investments is determined based on value-in-use calculations, which are set out in note 15.

Joint ventures

	Shares £m
Group	
At 1 April 2018	22.8
Additions	20.9
Share of post-tax profit	12.4
Share of other comprehensive income	0.5
Dividends received	(5.5)
At 31 March 2019	51.1
Share of post-tax profit	14.8
Share of other comprehensive income	0.2
Dividends received	(6.0)
Transferred to assets held for sale	(60.1)
At 31 March 2020	**–**

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20. Investments continued

The Group's joint ventures listed below all have share capital consisting solely of ordinary shares which is held directly by the Disposal Group.

Name of entity	Place of business/ country of incorporation	% of ownership	Measurement method
Lakeside Energy from Waste Holdings Limited(1)	England	50	Equity
INEOS Runcorn (TPS) Holdings Limited(2)	England	40	Equity

(1) Lakeside Energy from Waste Holdings Limited provides energy recovery facility services.
(2) INEOS Runcorn (TPS) Holdings Limited provides energy recovery facilities. The Group's economic interest is 75%, as set out in note 40, and voting rights are only 40% giving joint control over the Runcorn I ERF. As such the investment is classified as a joint venture and equity accounting has been applied.

Both joint ventures, which have non-coterminous year ends, are being sold with the Viridor business and as at 31 March 2020 are classified as assets held for sale. The aggregate capital and reserves of INEOS Runcorn (TPS) Holdings Limited at 31 December 2019 was £70.3 million (2019 £59.9 million) and its profit before tax for the year was £10.1 million (2019 £5.6 million). The aggregate capital and reserves of Lakeside Energy from Waste Holdings Limited at 30 September 2019 was £18.7 million (2019 £12.3 million) and its profit before tax for the year was £18.4 million (2019 £19.2 million).

Details of the Group's principal subsidiary and joint venture undertakings are set out in note 40.

The Group's joint ventures are all private companies and there are no quoted market prices available for their shares.

21. Inventories

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Raw materials and consumables	**4.9**	28.8	**–**	–

Excluded from the balance at 31 March 2020 above is £29.9 million relating to assets held for sale (see note 46 for further details).

22. Trade and other receivables – current

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Trade receivables	**241.9**	360.2	**–**	–
Less: allowance for expected credit losses in respect of trade receivables	**(106.1)**	(99.0)	**–**	–
Net trade receivables	**135.8**	261.2	**–**	–
Amounts owed by related parties (note 44)	**–**	7.7	**–**	–
Amounts owed by subsidiary undertakings	**–**	–	**18.3**	19.9
Other receivables	**10.0**	5.9	**0.2**	0.1
Accrued income	**29.3**	123.3	**0.2**	0.1
Prepayments	**10.7**	86.7	**6.0**	1.5
	185.8	484.8	**24.7**	21.6

Excluded from the balances at 31 March 2020 above is £277.9 million relating to assets held for sale (see note 46 for further details).

Trade receivables include accrued income relating to customers with water budget payment plan. Decreased demand in the water business has resulted in a decrease in trade receivables balances.

Accrued income includes £26.9 million in respect of metered accrual revenue in the retail water business. Metered accrual revenue relates to performance obligations that have been fully extinguished in providing services to customers prior to the reporting date. Payment in respect of these services is a matter of time following issuance of invoices.

The Directors consider that the carrying amounts of trade and other receivables approximate to their fair value.

There is no concentration of credit risk in trade receivables. The Group has a large number of customers who are dispersed and there is no significant loss on trade receivables expected that has not been provided for.

The Group applies the simplified approach in calculating the expected credit losses for trade receivables allowing a provision matrix to be used which is based on the expected life of trade receivables, default rates for different customer categories within the collection process and forward-looking information.

22. Trade and other receivables – current continued

As at 31 March, an analysis of the ageing of trade receivables is as follows:

	2020 £m	2019 £m
Group		
Not due	**33.7**	152.2
Past due 1 – 30 days	**15.8**	22.5
Past due 31 – 120 days	**17.2**	25.2
More than 120 days	**175.2**	160.3
	241.9	360.2

The aged trade receivables above are taken directly from aged sales ledger records before deduction of credit balances and other adjustments.

The Group's operating businesses specifically review separate categories of debt to identify an appropriate allowance for expected credit losses as outlined in note 2(p). South West Water Limited has a duty under legislation to continue to provide domestic customers with services regardless of payment. The expected credit loss rate applied ranges from 0% (not due) to 100% (>120 days and untraced previous occupier).

No material expected credit loss provision has been recognised in respect of amounts owed by subsidiary undertakings.

The movement in the allowance for expected credit losses in respect of trade receivables was:

	2020 £m	2019 £m
At 1 April	**99.0**	104.3
Provision for expected credit losses	**11.6**	3.2
Receivables written off during the year as uncollectable	**(1.6)**	(8.5)
Transfer to assets held for sale	**(2.9)**	–
At 31 March	**106.1**	99.0

23. Derivative financial instruments

	Group		Company	
	2020 £m	2019 £m	2020 £m	2019 £m
Derivatives used for cash flow hedging				
Non-current assets	**1.2**	1.0	**1.2**	1.1
Current assets	**2.2**	2.1	**2.0**	2.0
Current liabilities	**(6.9)**	(10.7)	**(0.9)**	(0.2)
Non-current liabilities	**(27.2)**	(9.8)	**(2.8)**	(0.7)
Derivatives used for fair value hedging				
Non-current assets	**2.9**	2.6	**2.9**	2.6
Current assets	**0.5**	0.8	**0.5**	0.8
Current liabilities	**–**	–	**–**	–
Non-current liabilities	**–**	–	**–**	–
Derivatives not in a hedge accounting relationship				
Non-current assets	**–**	66.9	**–**	–
Current assets	**–**	8.9	**–**	–
Current liabilities	**(0.2)**	(0.4)	**–**	–
Non-current liabilities	**–**	(0.1)	**–**	–

The Group's financial risks and risk management policies are set out in note 3. The fair value of derivatives is split between current and non-current assets or liabilities based on the maturity of the cash flows. The ineffective portion recognised in the income statement arising from hedging relationships was £nil (2019 £nil).

During the year a £8.6 million charge (2019 £6.8 million) was recognised in profit and loss relating to cash flow hedges previously recognised through other comprehensive income and recorded in the hedging reserve. A £14.3 million charge (2019 £6.4 million charge) was recognised as an other comprehensive loss/income for cash flow hedges that may be classified subsequently to profit and loss.

Interest rate swaps, primarily cash flow hedges, and fixed rate borrowings are used to manage the mix of fixed and floating rates to ensure at least 60% of Group net borrowings are at fixed rate. At 31 March 2020 55% of Group net borrowings were at fixed rate (2019 63%). While this level is below our policy of maintaining at least 60% of interest-bearing liabilities at fixed rates, it reflects considerations regarding Pennon's debt levels following the Group's announcement of the strategic review and the subsequent announcement of the proposed sale of Viridor.

At 31 March 2020 the Group had interest rate swaps to swap from floating to fixed rate and hedge financial liabilities with a notional value of £1,178 million and a weighted average maturity of 4.0 years (2019 £1,529 million, with 3.2 years). The weighted average interest rate of the swaps for their nominal amount was 1.4% (2019 1.7%).

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23. Derivative financial instruments continued

The periods for which the cash flow hedges are expected to affect future profit or loss are as follows:

	Due within 1 year £m	Due between 1 and 2 years £m	Due between 2 and 5 years £m	Due over 5 years £m	Total £m
Group					
31 March 2020					
Assets	**2.2**	**0.8**	**0.4**	**–**	**3.4**
Liabilities	**(7.3)**	**(7.0)**	**(19.4)**	**(0.8)**	**(34.5)**
31 March 2019					
Assets	2.1	0.5	0.5	–	3.1
Liabilities	(10.7)	(2.1)	(5.8)	(1.9)	(20.5)
Company					
31 March 2020					
Assets	**2.0**	**0.8**	**0.4**	**–**	**3.2**
Liabilities	**(0.9)**	**(0.8)**	**(1.6)**	**(0.4)**	**(3.7)**
31 March 2019					
Assets	2.0	0.5	0.6	–	3.1
Liabilities	(0.2)	(0.2)	(0.4)	(0.1)	(0.9)

Valuation hierarchy

The Group uses the following hierarchy for determining the fair value of financial instruments by valuation technique:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1)
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2)
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

The fair value of financial instruments not traded in an active market (level 2, for example over-the-counter derivatives) is determined by using valuation techniques. A variety of methods and assumptions are used based on market conditions existing at each balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows.

The Group's financial instruments are valued using level 2 measures:

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Assets				
Derivatives used for cash flow hedging	**3.4**	3.1	**3.2**	3.1
Derivatives used for fair value hedging	**3.4**	3.4	**3.4**	3.4
Derivatives not in a hedge accounting relationship	**–**	75.8	**–**	–
Total assets	**6.8**	82.3	**6.6**	6.5
Liabilities				
Derivatives used for cash flow hedging	**(34.1)**	20.5	**(3.7)**	0.9
Derivatives not in a hedge accounting relationship	**(0.2)**	0.5	**–**	–
Total liabilities	**(34.3)**	21.0	**(3.7)**	0.9

24. Financial instruments at fair value through profit

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Current liabilities	**1.5**	3.8	**0.5**	0.4
Non-current liabilities	**43.1**	43.1	**1.1**	1.4

Financial instruments at fair value through profit reflect the fair value movement of the hedged risk on the hedged item which had been designated in a fair value hedging relationship.

The hedged item was the £150 million bond issued by South West Water Finance Plc in 2010 which matures in July 2040 (see note 28). The hedging relationship was de-designated in previous periods at which point the fair value amount recognised at that point ceased to be revalued. The fixed financial liability at the point of de-designation is released to the income statement over the remaining life of the debt. Due to the de-designation the Group held a fixed to floating interest rate swap which was classified as a derivative not in a hedging relationship as disclosed in note 23. This derivative arrangement was settled early in the first half of the year ended 31 March 2020.

25. Cash and cash deposits

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Cash at bank and in hand	**64.9**	110.5	**17.8**	109.7
Short-term bank deposits	**175.0**	45.0	**150.0**	45.0
Other deposits	**426.0**	414.1	**200.1**	130.1
Total cash and cash deposits	**665.9**	569.6	**367.9**	284.8

Excluded from the balances at 31 March 2020 above is £33.3 million relating to assets held for sale (see note 46 for further details).

Group short-term deposits have an average maturity of 1 working day.

Group other deposits have an average maturity of 50 days.

Group other deposits include restricted funds of £227.2 million (2019 £203.9 million) to settle long-term lease liabilities (note 28). Restricted funds are available for access, subject to being replaced by an equivalent valued security.

For the purposes of the cash flow statement cash and cash equivalents comprise:

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Cash and cash deposits as above	**665.9**	569.6	**367.9**	284.8
Cash and cash deposits held in the Disposal Group	**33.3**	–	**–**	–
Less: deposits with a maturity of three months or more (restricted funds)	**(227.2)**	(203.9)	**–**	–
	472.0	365.7	**367.9**	284.8

26. Trade and other payables – current

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Trade payables	**64.2**	127.6	**2.8**	0.2
Contract liabilities	**2.0**	10.3	**–**	–
Amounts owed to subsidiary undertakings	**–**	–	**0.4**	0.1
Amounts owed to joint ventures (note 44)	**–**	4.1	**–**	–
Other tax and social security	**2.8**	32.5	**0.8**	0.8
Accruals	**15.5**	–	**–**	–
Other payables	**30.8**	123.5	**15.8**	14.7
	115.3	298.0	**19.8**	15.8

Excluded from the balances above is £141.7 million relating to liabilities directly associated with assets classified as held for sale (see note 46 for further details).

The Directors consider that the carrying amount of trade and other payables approximates to their fair value.

The movement in the contract liabilities was:

Contract liabilities	**2020 £m**	2019 £m
At 1 April	**126.4**	120.2
Revenue recognised in the year	**(9.6)**	(12.2)
Consideration received in advance of completion of performance obligations	**24.7**	18.4
Transfer to liabilities associated with assets held for sale	**(16.6)**	–
At 31 March	**124.9**	126.4

The analysis of contract liabilities between current and non-current is:

	2020 £m	2019 £m
Current	**2.0**	10.3
Non-current (note 29)	**122.9**	116.1
	124.9	126.4

Performance obligations related to the current contract liabilities balance above are expected to be satisfied, and revenue will be recognised, within the financial year ended 31 March 2020.

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27. Current tax assets/(liabilities)

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Current year debtor/(creditor)	**0.7**	(12.9)	**(0.6)**	(1.9)
Prior year tax items	**1.2**	(6.2)	**(1.9)**	(1.7)
	1.9	(19.1)	**(2.5)**	(3.6)

Excluded from the balances above is £1.0 million of current tax liabilities relating to liabilities directly associated with assets classified as held for sale (see note 46 for further details).

28. Borrowings

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Current				
Short-term loans	**7.6**	59.8	**–**	51.8
European Investment Bank	**33.1**	27.0	**6.1**	–
Amounts owed to subsidiary undertakings (note 44)	**–**	–	**284.4**	283.9
	40.7	86.8	**290.5**	335.7
Leases (IAS 17 finance)	**18.2**	63.6	**–**	–
Leases (IAS 17 operating)	**1.0**	–	**–**	–
Total current borrowings	**59.9**	150.4	**290.5**	335.7
Non-current				
Bank and other loans	**702.1**	443.1	**520.4**	370.9
Private placements	**618.2**	616.2	**511.6**	509.3
Bond 2040	**134.5**	134.2	**–**	–
RPI index-linked bonds	**440.0**	434.5	**–**	–
European Investment Bank	**340.8**	373.9	**103.4**	109.5
Amounts owed to subsidiary undertakings (note 44)	**–**	–	**–**	–
	2,235.6	2,001.9	**1,135.4**	989.7
Leases (IAS 17 finance)	**1,384.2**	1,496.8	**–**	–
Leases (IAS 17 operating)	**35.1**	–	**–**	–
Total non-current borrowings	**3,654.9**	3,498.7	**1,135.4**	989.7
Total borrowings	**3,714.8**	3,649.1	**1,425.9**	1,325.4

Excluded from the balances above is £19.0 million of current and £229.4 million of non-current borrowings relating to liabilities directly associated with assets classified as held for sale (see note 46 for further details).

Refer to note 45 for further details regarding the impact of IFRS 16 'Leases'. References above to IAS 17 finance and IAS 17 operating leases represent the classification of these lease balances under IAS 17 prior to implementation of IFRS 16.

The Group has leases for various assets as shown in note 17.

The Company issued a £100 million private placement in July 2007 maturing in 2022. Interest is payable at a fixed rate of 3.3%.

South West Water Finance Plc issued a £200 million RPI index-linked bond in July 2008 maturing in 2057 with a cash coupon of 1.99%. South West Water Finance Plc issued a £150 million bond in July 2010 maturing in 2040 with a cash coupon of 5.875%.

Bournemouth Water Limited issued a £65 million RPI index-linked bond in April 2005 maturing in 2033 with a cash coupon of 3.084%. This instrument was transferred to South West Water Limited in April 2017.

28. **Borrowings** continued

The fair values of non-current borrowings, valued using level 2 measures (as set out in note 23) were:

	2020		2019	
	Book value £m	**Fair value £m**	Book value £m	Fair value £m
Group				
Bank and other loans	**702.1**	**709.7**	443.1	447.3
Private placements	**618.2**	**689.8**	616.2	657.7
Bond 2040	**134.5**	**206.1**	134.2	197.5
RPI index-linked bond	**440.0**	**536.0**	434.5	526.4
European Investment Bank	**340.8**	**324.3**	373.9	345.2
	2,235.6	**2,465.9**	2,001.9	2,174.1
Leases	**1,419.3**	**–**	1,496.8	1,431.6
	3,654.9	**2,465.9**	3,498.7	3,605.7
Company				
Bank and other loans	**520.4**	**528.0**	370.9	375.3
European Investment Bank	**103.4**	**103.4**	109.5	109.5
Private placements	**511.6**	**583.1**	509.3	557.7
Amounts owed to subsidiary undertakings (note 44)	**–**	**–**	–	–
	1,135.4	**1,214.5**	989.7	1,042.5

Following the application of IFRS 16 during the year ended 31 March 2020 the disclosure relating to the fair value of leases is no longer required.

Where market values are not available, fair values of borrowings have been calculated by discounting expected future cash flows at prevailing interest rates.

The maturity of non-current borrowings was:

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Between 1 and 2 years	**315.1**	68.3	**204.4**	51.8
Over 2 years and less than 5 years	**590.1**	834.5	**393.0**	557.7
Over 5 years	**2,749.7**	2,595.9	**538.0**	380.2
	3,654.9	3,498.7	**1,135.4**	989.7

The weighted average maturity of non-current borrowings was 17 years (2019 18 years).

The maturity of lease liabilities was:

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Within 1 year	**19.2**	63.6	**–**	–
Over 1 year and less than 5 years	**149.0**	188.9	**–**	–
Over 5 years	**1,270.3**	1,307.9	**–**	–
	1,438.5	1,560.4	**–**	–

The discount rate used to calculate the lease liabilities above involves estimation. Where there is no rate implicit in the lease the Group uses an estimated incremental borrowing rate (IBR). At 31 March 2020 the range of IBR's used for the Continuing Group was between 2.93% and 4.5% and the weighted average IBR across all leases was 3.8%. If the weighted average rate used increased or decreased by 10bps, this would result in a c.3.8% increase or reduction in the present value of lease liabilities recognised at 31 March 2020.

Included above is a total present value of liabilities of £1,402.3 million representing amounts previously classified as finance leases under IAS 17 prior to implementation of IFRS 16.

Included above are accrued finance charges arising on obligations under agreements previously classified as finance leases under IAS 17 totalling £165.0 million (2019 £163.7 million), of which £1.1 million (2019 £3.7 million) is repayable within one year.

The period for repayment of certain leases includes an agreement to deposit with the lessor group amounts equal to the difference between the original and revised payments due. The accumulated deposits, £107.9 million at 31 March 2020 (2019 £97.5 million), are currently being held to settle the lease liability, subject to rights to release by negotiation with the lessor. The deposits are subject to a registered charge given as security to the lessor for the balance outstanding.

The period for repayment of certain other existing leases includes an agreement to deposit with the lessor group amounts equal to the difference between the original and revised payments due. The accumulated deposits, £118.0 million at 31 March 2020 (2019 £105.1 million), are currently being held to settle the lease liability, subject to rights to release by negotiation with the lessor. The deposits are subject to a registered charge given as security to the lessor for the outstanding balance.

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28. Borrowings continued

Undrawn committed borrowing facilities at the balance sheet date were:

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Floating rate:				
Expiring within 1 year	**–**	–	**–**	–
Expiring after 1 year	**940.0**	600.0	**705.0**	405.0
	940.0	600.0	**705.0**	405.0

In addition, at 31 March 2020 the Group had undrawn uncommitted short-term bank facilities of £30.0 million (2019 £30.0 million) available to the Company.

29. Other non-current liabilities

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Amounts owed to subsidiary undertakings	**–**	–	**8.6**	8.6
Contract liabilities	**122.9**	116.1	**–**	–
Deferred income	**–**	7.5	**–**	–
Other payables	**–**	24.3	**–**	–
	122.9	147.9	**8.6**	8.6

Excluded from the balances above is £14.3 million relating to liabilities directly associated with assets classified as held for sale (see note 46 for further details).

Non-current contract liabilities relate to consideration received in advance of the Group performing its performance obligations to customers where performance obligations will not be completed within 12 months of the balance sheet date. The overall movement in total contract liabilities is disclosed in note 26. Contract liabilities reflect the fair value of assets transferred from customers in the water segment.

Included in other payables as at 31 March 2019 are amounts provided by the Group in relation to claims received which are considered by the Directors and the management of the Group to be the best estimate of the amounts that might be finally settled. Further disclosures have not been provided in accordance with IAS 37 paragraph 92. These amounts have been transferred to/from other non-current liabilities to provisions within liabilities associated with assets held for sale (see note 46 for further details).

30. Retirement benefit obligations

During the year the Group operated a number of defined benefit pension schemes and also a defined contribution scheme. The principal plan within the Group is the Pennon Group Pension Scheme, which is a funded defined benefit, final salary pension scheme in the UK. The Group's pension schemes are established under trust law and comply with all relevant UK legislation.

The assets of the Group's pension schemes are held in separate trustee administered funds. The trustees of the funds are required to act in the best interest of the funds' beneficiaries. The appointment of schemes' trustees is determined by the schemes' trust documentation. The Group has a policy for the main fund that one-half of all trustees, other than the Chairman, are nominated by members of the schemes, including pensioners.

Defined contribution schemes

Pension costs for defined contribution schemes were £9.0 million (2019 £8.8 million), of which £2.5 million (2019 £2.5 million) relates to the Continuing Group.

Defined benefit schemes

Assumptions

The principal actuarial assumptions at 31 March were:

	2020 %	2019 %	2018 %
Rate of increase in pensionable pay	**2.7**	3.3	3.2
Rate of increase for current and future pensions	**2.5**	3.2	3.0
Rate used to discount schemes' liabilities and expected return on schemes' assets	**2.30**	2.40	2.70
Inflation	**2.7**	3.3	3.2

Mortality

Assumptions regarding future mortality experience are set based on actuarial advice in accordance with published statistics and experience. The mortality assumption uses a scheme-specific calculation based on CMI 2019 actuarial tables with an allowance for future longevity improvement.

The average life expectancy in years of a member having retired at age 62 on the balance sheet date is projected as:

	2020	2019	2018
Male	**24.7**	23.9	24.9
Female	**26.9**	26.3	27.3

30. Retirement benefit obligations continued

The average life expectancy in years of a future pensioner retiring at age 62, 20 years after the balance sheet date, is projected as:

	2020	2019	2018
Male	**25.4**	25.0	26.3
Female	**27.9**	28.1	29.6

The sensitivities regarding the principal assumptions used to measure the schemes' liabilities are:

	Change in assumption	Impact on schemes' liabilities
Rate of increase in pensionable pay	+/– 0.5%	+/– 1.4%
Rate of increase in current and future pensions	+/– 0.5%	+/– 6.9%
Rate used to discount schemes' liabilities	+/– 0.5%	+/– 9.3%
Inflation	+/– 0.5%	+/– 7.0%
Life expectancy	+/– 1 year	+/– 4.0%

The sensitivity analysis shows the effect of changes in the principal assumptions used for the measurement of the pension liability. The method used to calculate the sensitivities is approximate and has been determined taking into account the duration of the liabilities and the overall profile of each schemes' membership. This is the same approach as has been adopted in previous years.

The amounts recognised in the balance sheet, excluding amounts transferred to liabilities directly associated with assets classified as held for sale, were:

	Group		Company	
	2020 £m	2019 £m	2020 £m	2019 £m
Present value of financial obligations	**(685.3)**	(974.2)	**47.9**	(58.5)
Fair value of plan assets	**691.9**	934.0	**(48.0)**	55.1
Surplus/(deficit) of funded plans	**6.6**	(40.2)	**(0.1)**	(3.4)
Impact of minimum funding asset ceiling	**–**	(20.6)	**–**	–
Net asset/(liability) recognised in the balance sheet	**6.6**	(60.8)	**(0.1)**	(3.4)

The movement in the net defined benefit obligation over the accounting period is as follows:

	2020			2019		
	Present value of obligation £m	Fair value of plan assets £m	Total £m	Present value of obligation £m	Fair value of plan assets £m	Total £m
At 1 April	**(994.8)**	**934.0**	**(60.8)**	(948.0)	898.5	(49.5)
Current service cost	**(8.1)**	**–**	**(8.1)**	(13.1)	–	(13.1)
Past service cost and gains and losses on settlements	**2.0**	**–**	**2.0**	(3.0)	–	(3.0)
Interest (expense)/income	**(23.1)**	**22.3**	**(0.8)**	(25.2)	23.8	(1.4)
	(29.2)	**22.3**	**(6.9)**	(41.3)	23.8	(17.5)
Remeasurements:						
(Loss)/return on plan assets excluding amounts included in interest expense	**–**	**(16.1)**	**(16.1)**	–	20.2	20.2
(Loss)/gain from change in demographic assumptions	**(3.9)**	**–**	**(3.9)**	41.6	–	41.6
Gain/(loss) from change in financial assumptions	**51.9**	**(9.0)**	**42.9**	(75.8)	–	(75.8)
Experience losses	**(5.2)**	**–**	**(5.2)**	(3.2)	–	(3.2)
	42.8	**(25.1)**	**17.7**	(37.4)	20.2	(17.2)
Contributions:						
Employers	**–**	**41.5**	**41.5**	–	23.4	23.4
Plan participants	**(0.3)**	**0.3**	**–**	(1.0)	1.0	–
Payments from plans:						
Benefit payments	**38.7**	**(38.7)**	**–**	32.9	(32.9)	–
	38.4	**3.1**	**41.5**	31.9	(8.5)	23.4
Transfer to liabilities directly associated with assets held for sale	**257.5**	**(242.4)**	**15.1**	–	–	–
At 31 March	**(685.3)**	**691.9**	**6.6**	(994.8)	934.0	(60.8)

Past service cost for the current year includes a non-underlying credit of £4.9 million representing the reduction in liabilities that result from the termination of the Greater Manchester contract (see note 6).

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continued

30. Retirement benefit obligations continued

The movement in the Company's net defined benefit obligation over the accounting period is as follows:

	2020			2019		
	Present value of obligation £m	**Fair value of plan assets £m**	**Total £m**	Present value of obligation £m	Fair value of plan assets £m	Total £m
At 1 April	**(58.5)**	**55.1**	**(3.4)**	(56.5)	53.2	(3.3)
Current service cost	**(0.2)**	**–**	**(0.2)**	(0.3)	–	(0.3)
Past service cost and gains and losses on settlements	**–**	**–**	**–**	(0.2)	–	(0.2)
Interest (expense)/income	**(0.4)**	**0.3**	**(0.1)**	(1.5)	1.4	(0.1)
	(0.6)	**0.3**	**(0.3)**	(2.0)	1.4	(0.6)
Remeasurements:						
(Loss)/return on plan assets excluding amounts included in interest expense	**–**	**(6.0)**	**(6.0)**	–	2.1	2.1
(Loss)/gain from change in demographic assumptions	**(0.2)**	**–**	**(0.2)**	2.6	–	2.6
Gain/(loss) from change in financial assumptions	**3.0**	**–**	**3**	(4.5)	–	(4.5)
Experience gains/(losses)	**6.1**	**–**	**6.1**	(0.2)	–	(0.2)
	8.9	**(6.0)**	**2.9**	(2.1)	2.1	–
Contributions:						
Employers	**–**	**0.7**	**0.7**	–	0.5	0.5
Payments from plans:						
Benefit payments	**2.2**	**(2.2)**	**–**	2.1	(2.1)	–
	2.2	**(1.5)**	**0.7**	2.1	(1.6)	0.5
At 31 March	**(48.0)**	**47.9**	**(0.1)**	(58.5)	55.1	(3.4)

The Group has one smaller pension scheme which is in surplus and is deemed to have irrecoverable assets in accordance with IFRIC 14 'The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction'. This relates to the Disposal Group and has been transferred to liabilities associated with assets held for sale (see note 46).

Changes in the effect of the asset ceiling during the year were:

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Irrecoverable asset at start of the year	**20.6**	16.8	**–**	–
Interest on irrecoverable surplus	**0.5**	0.5	**–**	–
Actuarial (losses)/gains	**(7.0)**	3.3	**–**	–
Transfer to liabilities associated with assets held for sale	**(14.1)**	–	**–**	–

The schemes' assets relating to the Continuing Group were:

	2020			2019		
	Quoted prices in active market £m	**Prices not quoted in active market £m**	**Fund %**	Quoted prices in active market £m	Prices not quoted in active market £m	Fund %
Equities	**109.9**	**–**	**23**	234.5	–	25
Government bonds	**78.1**	**–**	**10**	134.6	–	14
Other bonds	**174.2**	**104.0**	**35**	247.1	–	26
Diversified growth	**110.0**	**–**	**18**	154.7	13.1	18
Property	**48.5**	**6.8**	**7**	68.1	3.4	8
Insurance linked security	**49.2**	**–**	**6**	55.2	–	6
Other (including cash funds)	**11.2**	**–**	**1**	23.3	–	3
	581.1	**110.8**	**100**	917.5	16.5	100

Other assets at 31 March 2020 represented principally cash contributions received from the Group towards the year end which were invested during the subsequent financial year.

30. Retirement benefit obligations continued

The Company's share of the schemes' assets at the balance sheet date was:

	2020			2019		
	Quoted prices in active market £m	Prices not quoted in active market £m	Fund %	Quoted prices in active market £m	Prices not quoted in active market £m	Fund %
Equities	**7.6**	**–**	**16**	10.4	–	19
Government bonds	**5.4**	**–**	**11**	9.4	–	17
Other bonds	**19.3**	**–**	**40**	16.6	–	30
Diversified growth	**7.6**	**–**	**16**	8.9	–	16
Property	**3.8**	**–**	**8**	4.8	–	9
Insurance linked security	**3.4**	**–**	**7**	3.7	–	7
Other	**0.8**	**–**	**2**	1.3	–	2
	47.9	**–**	**100**	55.1	–	100

Through its defined benefit pension plan, the Group is exposed to a number of risks, the most significant of which are detailed below:

Asset volatility	The liabilities are calculated using a discount rate set with reference to corporate bond yields; if assets underperform this yield, this will create a deficit. The schemes hold a significant proportion of growth assets (equities and diversified growth funds) which are expected to outperform corporate bonds in the long term, but can give rise to volatility and risk in the short term. The allocation to growth assets is monitored such that it is suitable with the schemes' long-term objectives.
Changes in bond yields	A decrease in corporate bond yields will increase the schemes' liabilities, although this will be partially offset by an increase in the value of the schemes' bond holdings.
Inflation risk	The majority of the schemes' benefit obligations are linked to inflation, and higher inflation will lead to higher liabilities (although, in most cases, caps on the level of inflationary increases are in place to protect against extreme inflation). The majority of the assets are either unaffected by or loosely correlated with inflation, meaning that an increase in inflation will also increase the deficit.
Life expectancy	The majority of the schemes' obligations are to provide benefits for the life of the member, so increases in life expectancy will result in an increase in the liabilities.

In conjunction with its investment advisers, the trustees have structured the schemes' investments with the objective of balancing investment returns and levels of risk. The asset allocation for the main scheme has three principal elements:

- Holding of cash funds and bonds which are expected to be less volatile than most other asset classes and reflects market movements in the schemes' liabilities
- A proportion of assets with fund managers having freedom in making investment decisions to maximise returns
- Investment of a proportion of the schemes' assets in alternative asset classes which give the potential for diversification (currently property, insurance linked securities and diversified growth).

The liabilities of the defined benefit schemes are measured by using the projected unit credit method which is an accrued benefits valuation method in which the scheme liabilities make allowance for projected increases in pensionable pay.

The future cash flows arising from the payment of the defined benefits are expected to be settled primarily in the period between 15 and 40 years from the balance sheet date.

The 2019 triennial actuarial valuation of the principal defined benefit scheme has been agreed with an actuarial valuation deficit increasing of £53 million. The Group has made deficit recovery contributions of £31.9 million during the year (2019 £13.1 million), £18.8 million being in advance of the previously agreed recovery plan. Following the finalisation of the 2019 actuarial valuation, the Group is required to make further deficit recovery contributions, in addition to those amounts paid in the year to 31 March 2020, of £2.8 million and £0.4 million in March 2021 and March 2022 respectively, with these amounts being adjusted for inflation. The Group monitors funding levels on an annual basis and the Continuing Group expects to pay total contributions of around £7 million, including expenses, during the year ended 31 March 2021. The new schedule of contributions is in line with the 2016 triennial actuarial valuation.

31. Deferred tax

Deferred tax is provided in full on temporary differences under the liability method using enacted tax rates.

Movements on deferred tax were:

	Group		Company	
	2020 £m	2019 £m	2020 £m	2019 £m
Liabilities/(assets) at 1 April	**305.1**	295.6	**(1.2)**	(1.6)
Opening adjustment on adoption of IFRS 16 Leases	**(1.8)**	–	**–**	–
Charged/(credited) to the income statement	**33.2**	13.3	**(0.1)**	0.2
(Credited)/charged to equity, including impact of change in tax rate	**(4.6)**	(4.3)	**–**	0.2
Change of tax rate charged to the income statement – non-underlying	**40.6**	–	**(0.5)**	–
Other non-underlying charges in the income statement	**(12.7)**	0.5	**–**	–
Transferred to liabilities associated with assets classified as held for sale	**(98.2)**	–	**–**	–
Liabilities/(assets) at 31 March	**261.6**	305.1	**(1.8)**	(1.2)

Deferred tax assets have been recognised in respect of all temporary differences giving rise to deferred tax assets because it is probable that these assets will be recovered.

The majority of the Group's deferred tax liability is expected to be recovered over more than one year. The majority of the Company's deferred tax asset is expected to be recovered over more than one year. All deferred tax assets and liabilities within the same jurisdiction are offset.

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31. Deferred tax continued
The movements in deferred tax assets and liabilities were:

Group
Deferred tax liabilities

	Accelerated tax depreciation £m	Fair value adjustments £m	Revenue on service concession arrangements £m	Derivatives £m	Total £m
At 1 April 2018	259.9	20.6	43.7	0.7	324.9
Charged/(credited) to the income statement	12.1	(4.1)	4.4	(0.2)	12.2
Non-underlying credit to the income statement	–	–	–	1.0	1.0
Charged to equity/SOCI	–	–	–	(0.6)	(0.6)
At 31 March 2019	272.0	16.5	48.1	0.9	337.5
Opening adjustment on adoption of IFRS 16 Leases	(1.8)	–	–	–	(1.8)
Charged/(credited) to the income statement	24.8	(1.3)	2.1	–	25.6
Non-underlying charge/(credit) to the income statement	33.0	1.9	5.5	(12.5)	27.9
Charged to equity/SOCI	–	–	–	(3.1)	(3.1)
Transfer to deferred tax assets	–	–	–	14.7	14.7
Transferred to liabilities directly associated with assets classified as held for sale	(53.6)	–	(55.7)	–	(109.3)
At 31 March 2020	**274.4**	**17.1**	**–**	**–**	**291.5**

Deferred tax assets

	Short-term liabilities including provisions £m	Retirement benefit obligations £m	Derivatives £m	Share-based payments £m	Tax losses £m	Fair value adjustment £m	Other £m	Total £m
At 1 April 2018	(5.4)	(8.4)	–	(0.8)	(1.7)	(9.9)	(3.1)	(29.3)
Charged/(credited) to the income statement	0.1	0.5	–	0.1	0.5	1.3	(1.4)	1.1
Non-underlying credit to the income statement	–	(0.5)	–	–	–	–	–	(0.5)
Charged to equity/SOCI	–	(3.2)	–	(0.5)	–	–	–	(3.7)
At 31 March 2019	(5.3)	(11.6)	–	(1.2)	(1.2)	(8.6)	(4.5)	(32.4)
Charged/(credited) to the income statement	3.5	3.4	–	(0.3)	(0.1)	0.7	0.4	7.6
Non-underlying (credit)/charge to the income statement	(1.1)	2.8	–	(0.1)	(0.2)	(1.0)	(0.4)	–
Charged to equity/SOCI	–	(0.1)	–	(1.4)	–	–	–	(1.5)
Transfer from deferred tax liabilities	–	–	(14.7)	–	–	–	–	(14.7)
Transferred to liabilities directly associated with assets classified as held for sale	1.1	3.0	–	1.0	1.5	–	4.5	11.1
At 31 March 2020	**(1.8)**	**(2.5)**	**(14.7)**	**(2.0)**	**–**	**(8.9)**	**–**	**(29.9)**

Net liability	
At 31 March 2019	305.1
At 31 March 2020	**261.6**

Company
Deferred tax assets

	Retirement benefit obligations £m	Derivatives £m	Share-based payments £m	Other £m	Total £m
At 1 April 2018	(0.6)	(0.5)	(0.2)	(0.3)	(1.6)
Charged to the income statement	–	–	–	0.2	0.2
Charged to equity	–	0.2	–	–	0.2
At 31 March 2019	(0.6)	(0.3)	(0.2)	(0.1)	(1.2)
(Credited)/charged to the income statement	–	–	(0.2)	0.1	(0.1)
Non-underlying (credit) to the income statement	(0.5)	–	–	–	(0.5)
Charged/(credited) to equity, including impact on change in tax rate	1.0	(0.6)	(0.4)	–	–
At 31 March 2020	**(0.1)**	**(0.9)**	**(0.8)**	**–**	**(1.8)**

31. Deferred tax continued

Deferred tax (charged)/credited to equity during the year was:

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Remeasurement of defined benefit obligations	**(0.1)**	3.2	**1.0**	–
Cash flow hedges	**(3.1)**	0.6	**(0.6)**	0.2
Deferred tax on other comprehensive (gain)/loss	**(3.2)**	3.8	**0.4**	0.2
Share-based payments	**(1.4)**	0.5	**(0.4)**	–
	(4.6)	4.3	**–**	0.2

Capital allowances are available when a business incurs qualifying expenditure on capital items such as infrastructure assets. Capital allowances provide tax relief on these items in place of accounting depreciation which is not tax deductible. Over the period of ownership of an asset, cumulative depreciation and capital allowances will equalise. Capital allowance rates are set by the UK Government and every business receives the same rate of allowance. Capital allowance rates vary from 2% up to 100% in certain instances, with most items qualifying at either 6% or 18% per annum. Given the Group's continuing capital expenditure programme, it is likely that the deferred tax liability will continue in to the longer term.

The different accounting treatment of property, plant and equipment for tax and accounting purposes means that the taxable income of the Group is not the same as the profit reported in the financial statements. The adjustments for this are reflected in the current tax reconciliation.

Short-term temporary differences arise on items such as retirement benefit obligations, derivatives, fair value adjustments and share-based payments because the treatment of such items is different for tax and accounting purposes. These differences reverse over future years following that in which they arise, as is reflected in the deferred tax charge in these financial statements. Specifically, retirement benefit obligations will crystallise over the life of the pension scheme, the fair value items will be released over their useful remaining life which is up to 115 years while share-based payments will crystallise over the remaining period of the share schemes, which is up to five years. Short-term liabilities, including provisions typically crystallise in the following year.

Where interest charges or other costs are capitalised in the accounts, tax relief is either given as the charges are incurred or when the costs are taken to the income statement

32. Provisions

	Environmental and landfill restoration £m	Restructuring £m	Other provisions £m	Total £m
Group				
At 1 April 2019	209.6	1.1	21.1	231.8
Charged to the income statement	2.3	–	(5.0)	(2.7)
Capitalised	5.3	–	0.3	5.6
Utilised	(16.0)	(0.4)	(0.1)	(16.5)
Reclassification	–	(0.1)	0.1	–
Transferred to liabilities associated with assets classified as held for sale	(201.2)	–	(16.4)	(217.6)
At 31 March 2020	**–**	**0.6**	**–**	**0.6**

The amount charged to the income statement includes £7.9 million (2019 £11.1 million) charged to finance costs as the unwinding of discounts in provisions.

The analysis of provisions between current and non-current is:

	2020 £m	2019 £m
Current	**0.6**	28.7
Non-current	**–**	203.1
	0.6	231.8

Environmental and landfill restoration provisions are incurred during the operational life of each landfill site and for a considerable period thereafter. The period of aftercare post-closure and the level of costs expected are uncertain and can vary significantly from site to site. Key factors are the type of waste, the speed at which it decomposes, the volume of leachate requiring treatment and regulatory requirements specific to the site. Environmental and landfill restoration provisions are expected to be substantially utilised throughout the operational life of a site and for landfill sites within 60 years of closure. The provisions have been established assuming current waste management technology based upon estimated costs at future prices which have been discounted to present value. The Group has applied a discount rate of 4.220% (2019 4.825%) and an inflation rate of 2.0% (2019 2.5%) to its aftercare provision and a discount rate of 2.9% (2019 3.8%) and an inflation rate of 2.0% (2019 2.5%) to its restoration provision.

The restructuring provision relates principally to severance costs and will be utilised within one year.

Other provisions include underperforming contracts of £4.1 million (2019 £7.1 million), which are provided for at the net present value of the operating losses of the underperforming contracts and are to be utilised over the remaining period of the contract to which they relate. The weighted average contract life of underperforming contracts is three years (2019 five years).

Following the announced sale of the Group's waste management business, Viridor, the environmental, landfill restoration and other provisions have been transferred to liabilities directly associated with assets classified as held for sale, see note 46.

Notes to the financial statements
continued

33. Share capital

Allotted, called-up and fully paid

	Number of shares		
	Treasury shares	Ordinary shares	£m
Group and Company			
At 1 April 2018 ordinary shares of 40.7p each	8,443	419,743,183	170.8
For consideration of £5.1 million, shares issued under the Company's Sharesave Scheme	–	777,415	0.3
At 31 March 2019 ordinary shares of 40.7p each	8,443	420,520,598	171.1
For consideration of £3.6 million, shares issued under the Company's Sharesave Scheme	–	515,959	0.2
At 31 March 2020 ordinary shares of 40.7p each	**8,443**	**421,036,557**	**171.3**

Shares held as treasury shares may be sold or reissued for any of the Company's share schemes, or cancelled.

Employee share schemes

The Group operates a number of equity-settled share plans for the benefit of employees. Details of each plan are:

i) Sharesave Scheme

An all-employee savings-related plan is operated that enables employees, including Executive Directors, to invest up to a maximum of £500 per month for three or five years. These savings can then be used to buy ordinary shares, at a price set at a 17% discount to the market value at the start of the savings period, at the third or fifth year anniversary of the option being granted. Options expire six months following the exercise date and, except for certain specific circumstances such as redundancy, lapse if the employee leaves the Group before the option exercise period commences.

Outstanding options to subscribe for ordinary shares of 40.7p each under the Company's share option schemes are:

	Date granted and subscription price fully paid	Period when options normally exercisable	Thousands of shares in respect of which options outstanding at 31 March	
			2020	2019
14 July 2014	611p	2017 – 2019	**2**	142
24 June 2015	683p	2018 – 2020	**142**	194
29 June 2016	709p	2020 – 2021	**76**	478
28 June 2017	767p	2020 – 2022	**327**	462
3 July 2018	635p	2021 – 2023	**1,115**	1,367
9 July 2019	635p	2022 – 2024	**874**	–
			2,536	2,643

The number and weighted average exercise price of Sharesave options are:

	2020		2019	
	Number of ordinary shares (thousands)	**Weighted average exercise price per share (p)**	Number of ordinary shares (thousands)	Weighted average exercise price per share (p)
At 1 April	**2,643**	**674**	2,490	700
Granted	**925**	**620**	1,456	635
Forfeited	**(295)**	**678**	(437)	717
Exercised	**(514)**	**680**	(777)	661
Expired	**(223)**	**681**	(89)	661
At 31 March	**2,536**	**652**	2,643	674

The weighted average price of the Company's shares at the date of exercise of Sharesave options during the year was 820p (2019 750p). The options outstanding at 31 March 2020 had a weighted average exercise price of 652p (2019 674p) and a weighted average remaining contractual life of 1.9 years (2019 2.0 years). The number of exercisable Sharesave options at 31 March 2020 was 4,000 (2019 1,000) and the weighted average exercise price of exercisable Sharesave options was 649p (2019 683p).

The aggregate fair value of Sharesave options granted during the year was £0.9 million (2019 £0.8 million), determined using the Black-Scholes valuation model. The significant inputs into the valuation model at the date of issue of the options were:

	2020	2019
Weighted average share price	**765**	801
Weighted average exercise price	**620**	635
Expected volatility	**20.0%**	20.0%
Expected life	**3.3 years**	3.3 years
Risk-free rate	**0.75%**	0.5%
Expected dividend yield	**5.7%**	5.2%

Expected volatility was determined by calculating the historical volatility of the Group's share price over the previous three years.

33. Share capital continued

ii) Performance and Co-investment Plan

Executive Directors and senior management receive a conditional award of ordinary shares in the Company and are also required to hold a substantial personal shareholding in the Company. The eventual number of shares, if any, which vest is dependent upon the achievement of conditions of the plan over the restricted period, being not less than three years. From 2017/18, no further awards are made under this Plan as it has been superseded by a long-term incentive plan (see iii below).

The number and price of shares in the Performance and Co-investment Plan are:

	2020		2019	
	Number of ordinary shares (thousands)	**Weighted average exercise price per share (p)**	Number of ordinary shares (thousands)	Weighted average exercise price per share (p)
At 1 April	**256**	**920**	571	865
Vested	**(86)**	**920**	–	–
Lapsed	**(170)**	**920**	(315)	820
At 31 March	**–**	**–**	256	920

There were no outstanding awards at 31 March 2020. The awards outstanding at 31 March 2019 had a weighted exercise price of 920p and a weighted average remaining contractual life of 0.3 years.

iii) Long-term incentive plan (LTIP)

Executive Directors and senior management receive an annual grant of conditional shares. Share awards vest subject to the achievement of specific performance conditions measured over a performance period of not less than three years.

The number and price of shares in the LTIP are:

	2020		2019	
	Number of ordinary shares (thousands)	**Weighted average exercise price per share (p)**	Number of ordinary shares (thousands)	Weighted average exercise price per share (p)
At 1 April	**962**	**796**	510	803
Granted	**509**	**753**	526	790
Vested	**–**	**–**	–	–
Lapsed	**(125)**	**787**	(74)	798
At 31 March	**1,346**	**781**	962	796

The awards outstanding at 31 March 2020 had a weighted exercise price of 781p (2019 796p) and a weighted average remaining contractual life of 1.4 years (2019 1.9 years).

The aggregate fair value of awards granted during the year was £1.5 million (2019 £1.7 million), determined from market value. No option pricing methodology is applied since the vesting of the shares depend on non-market performance vesting conditions.

iv) Annual Incentive Bonus Plan – deferred shares

Awards under the plan to Executive Directors and senior management involve the release of ordinary shares in the Company to participants. There is no performance condition since vesting is conditional upon continuous service with the Group for a period of three years from the award. The number and weighted average price of shares in the Annual Incentive Bonus Plan are:

	2020		2019	
	Number of ordinary shares (thousands)	**Weighted average exercise price per share (p)**	Number of ordinary shares (thousands)	Weighted average exercise price per share (p)
At 1 April	**450**	**825**	405	843
Granted	**215**	**755**	191	761
Vested	**(113)**	**950**	(117)	791
Lapsed	**(28)**	**786**	(29)	790
At 31 March	**524**	**772**	450	825

The awards outstanding at 31 March 2020 had a weighted average exercise price of 772p (2019 825p) and a weighted average remaining contractual life of 1.5 years (2019 1.5 years). The Company's share price at the date of the awards ranged from 761p to 950p.

The aggregate fair value of awards granted during the year was £1.6 million (2019 £1.1 million), determined from market value. No option pricing methodology is applied since dividends paid on the shares are receivable by the participants in the scheme.

Further details of the plans and options granted to Directors, included above, are shown in the Directors' remuneration report.

Notes to the financial statements
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34. Share premium account

	£m
Group and Company	
At 1 April 2018	218.8
Shares issued under the Sharesave Scheme	4.8
At 31 March 2019	223.6
Shares issued under the Sharesave Scheme	3.4
At 31 March 2020	**227.0**

35. Capital redemption reserve

The capital redemption reserve represents the redemption of B shares and cancellation of deferred shares arising from a capital return to shareholders undertaken during 2006.

	£m
Group and Company	
At 1 April 2018	144.2
At 31 March 2019	144.2
At 31 March 2020	**144.2**

36. Retained earnings and other reserves

	Own shares £m	Hedging reserve £m	Retained earnings £m	Total £m
Group				
At 1 April 2018	(3.5)	(11.1)	821.7	807.1
Profit for the year	–	–	214.3	214.3
Other comprehensive loss for the year	–	(5.8)	(13.5)	(19.3)
Dividends paid relating to 2018	–	–	(162.0)	(162.0)
Credit to equity in respect of share-based payments (net of tax)	–	–	4.4	4.4
Charge in respect of share options vesting	1.0	–	(1.0)	–
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	(1.5)	–	–	(1.5)
At 31 March 2019	(4.0)	(16.9)	863.9	843.0
IFRS 16 Leases opening adjustment	–	–	(8.0)	(8.0)
At 1 April 2019 (adjusted for IFRS 16)	(4.0)	(16.9)	855.9	835.0
Profit for the year	–	–	200.4	200.4
Other comprehensive income for the year	–	(11.2)	18.0	6.8
Dividends paid relating to 2019	–	–	(172.6)	(172.6)
Credit to equity in respect of share-based payments (net of tax)	–	–	4.8	4.8
Charge in respect of share options vesting	1.1	–	(1.1)	–
Own shares acquired by the Pennon Employee Share Trust in respect of share options granted	(1.6)	–	–	(1.6)
At 31 March 2020	**(4.5)**	**(28.1)**	**905.4**	**872.8**

The own shares reserve represents the cost of ordinary shares in Pennon Group plc issued to or purchased in the market and held by the Pennon Group plc Employee Benefit Trust to satisfy awards under the Group's Annual Incentive Bonus Plan.

36. Retained earnings and other reserves continued

The market value of the 589,000 ordinary shares (2019 520,000 ordinary shares) held by the Trust at 31 March 2020 was £6.4 million (2019 £3.8 million).

	Hedging reserve £m	Retained earnings £m	Total £m
Company			
At 1 April 2018	(2.0)	1,113.1	1,111.1
Profit for the year	–	194.8	194.8
Other comprehensive income for the year	0.2	–	0.2
Dividends paid relating to 2018	–	(162.0)	(162.0)
Credit to equity in respect of share-based payments (net of tax)	–	1.5	1.5
Charge in respect of share options vesting	–	(0.9)	(0.9)
At 31 March 2019	(1.8)	1,146.5	1,144.7
Profit for the year	–	330.6	330.6
Other comprehensive (loss)/income for the year	(2.1)	2.6	0.5
Dividends paid relating to 2019	–	(172.6)	(172.6)
Credit to equity in respect of share-based payments (net of tax)	–	2.0	2.0
Charge in respect of share options vesting	–	(1.1)	(1.1)
At 31 March 2020	**(3.9)**	**1,308.0**	**1,304.1**

In making decisions about the level of dividends to be proposed the Directors take steps to check that retained earnings reflect realised profits and are therefore distributable within the requirements of the Companies Act 2006.

37. Perpetual capital securities

	£m
Group and Company	
At 1 April 2018	296.7
Distributions to perpetual capital security holders	(8.6)
Profit for the year attributable to perpetual capital security holders	8.6
At 31 March 2019	296.7
Distributions due to perpetual capital security holders	(8.6)
Current tax relief on distributions to perpetual capital security holders	1.6
Profit for the year attributable to perpetual capital security holders	7.0
At 31 March 2020	**296.7**

On 22 September 2017 the Company issued £300 million 2.875% perpetual capital securities. Costs directly associated with the issue of £3.3 million were set off against the value of the issuance. They have no fixed redemption date but the Company can at its sole discretion redeem all, but not part, of these securities at their principal amount on 22 May 2020 or any subsequent periodic return payment date after this.

The Company has the option to defer periodic returns on any relevant payment date, as long as a dividend on the ordinary shares has not been paid or declared in the previous 12 months. Deferred periodic returns shall be satisfied only on redemption or payment of dividend on ordinary shares, all of which only occur at the sole discretion of the Company.

As the Company paid a dividend in the 12 months prior to the periodic return date of 22 May 2020, a periodic return of £8.6 million (2019 £8.6 million) has been recognised as a financial liability at the year end.

Notes to the financial statements
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38. Analysis of cash flows given in the statement of cash flows

Reconciliation of profit for the year to cash generated from operations:

Cash generated from operations

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Profit for the year	**206.3**	222.6	**337.7**	203.4
Adjustments for:				
Share-based payments	**3.4**	3.6	**1.7**	1.5
Profit on disposal of property, plant and equipment	**(2.5)**	(3.9)	**–**	–
Depreciation charge	**197.2**	190.0	**–**	–
Amortisation of intangible assets	**4.7**	5.2	**–**	–
Non-underlying increase in customer debt provisions	**9.0**	–	**–**	–
Non-underlying past service pension credit	**(4.9)**	–	**–**	–
Non-underlying remeasurement of fair value movement in derivatives	**(18.0)**	(5.8)	**–**	–
Share of post-tax profit from joint ventures	**(14.8)**	(12.4)	**–**	–
Finance income	**(26.6)**	(23.5)	**(45.4)**	(45.9)
Finance costs (before non-underlying items)	**115.3**	106.7	**38.2**	35.5
Dividends receivable	**–**	–	**(335.6)**	(196.7)
Taxation charge	**95.2**	37.7	**4.2**	3.7
Changes in working capital:				
Increase in inventories	**(6.0)**	(4.2)	**–**	–
(Increase)/decrease in trade and other receivables	**32.6**	(46.4)	**(182.9)**	(178.8)
Decrease/(Increase) in service concession arrangements receivable	**(17.4)**	6.8	**–**	–
(Decrease)/Increase in trade and other payables	**(19.2)**	(47.7)	**2.5**	(45.6)
Decrease in retirement benefit obligations from contributions	**(30.8)**	(7.3)	**(0.7)**	(0.1)
Decrease in provisions	**(7.2)**	(21.6)	**–**	–
Cash generated/(outflow) from operations	**516.3**	399.8	**(180.3)**	(223.0)

Reconciliation of total interest paid:

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Interest paid in operating activities	**97.7**	83.9	**37.4**	36.8
Interest paid in investing activities	**10.6**	15.2	**–**	–
Total interest paid	**108.3**	99.1	**37.4**	36.8

The above includes the entire Group, including cash flows relating to the discontinued operations business. Disaggregated information relating to the discontinued business is provided in note 46.

During the year, the Group completed a number of sale and leaseback transactions in respect of its infrastructure assets as part of its ongoing financing arrangements. Cash proceeds of £115.0 million were received and a gain of £nil was recognised. These assets are primarily being leased back over an initial term of 10-year lease term at market rentals.

39. Net borrowings

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Cash and cash deposits	**665.9**	569.6	**367.9**	284.8
Borrowings – current				
Bank and other loans	**(7.6)**	(59.8)	**–**	(51.8)
Other current borrowings	**(33.1)**	(27.0)	**(6.1)**	–
Lease obligations (IAS 17 finance)	**(18.2)**	(63.6)	**–**	–
Lease obligations (IAS 17 operating)	**(1.0)**	–	**–**	–
Amounts owed to subsidiary undertakings	**–**	–	**(284.4)**	(283.9)
Total current borrowings	**(59.9)**	(150.4)	**(290.5)**	(335.7)
Borrowings – non-current				
Bank and other loans	**(1,894.8)**	(1,628.0)	**(1,032.0)**	(880.2)
Other non-current borrowings	**(340.8)**	(373.9)	**(103.4)**	(109.5)
Lease obligations (IAS 17 finance)	**(1,384.2)**	(1,496.8)	**–**	–
Lease obligations (IAS 17 operating)	**(35.1)**	–	**–**	–
Total non-current borrowings	**(3,654.9)**	(3,498.7)	**(1,135.4)**	(989.7)
Total net borrowings in Continuing Group	**(3,048.9)**	(3,079.5)	**(1,058.0)**	(1,040.6)
Net borrowings in Disposal Group	**(215.1)**	–	**–**	–
Net borrowings in total Group	**(3,264.0)**	(3,079.5)	**(1,058.0)**	(1,040.6)

The movements in net borrowings during the periods presented were as follows:

Group	Net borrowings at 1 April 2018 £m	Cash flows – other £m	Foreign exchange adjustments £m	Other non-cash movements £m	Net borrowings at 31 March 2019 £m
Cash and cash deposits	585.3	(15.7)	–	–	569.6
Bank and other loans due within one year	(149.6)	149.6	–	(59.8)	(59.8)
Other current borrowings	(32.0)	32.0	–	(27.0)	(27.0)
Finance leases due within one year	(28.2)	28.2	–	(63.6)	(63.6)
Bank and other loans due after one year	(1,408.8)	(275.0)	1.6	54.2	(1,628.0)
Other non-current borrowings	(291.4)	(109.5)	–	27.0	(373.9)
Finance leases due after one year	(1,476.8)	(75.3)	–	55.3	(1,496.8)
	(2,801.5)	(265.7)	1.6	(13.9)	(3,079.5)

	Net borrowings at 1 April 2019 £m	**IFRS 16 transition adjustment £m**	**Cash flows – other £m**	**Transfer between non-current and current £m**	**Other non-cash movements £m**	**Transfer to Disposal Group £m**	**Net borrowings at 31 March 2020 £m**
Cash and cash deposits	**569.6**	**–**	**129.6**	**–**	**–**	**(33.3)**	**665.9**
Bank and other loans due within one year	**(59.8)**	**–**	**57.6**	**(8.0)**	**2.6**	**–**	**(7.6)**
Other current borrowings	**(27.0)**	**–**	**27.0**	**(33.1)**	**–**	**–**	**(33.1)**
Current lease obligations (IAS 17 finance)	**(63.6)**	**–**	**63.6**	**(23.4)**	**(3.8)**	**9.0**	**(18.2)**
Current lease obligations (IAS 17 operating)	**–**	**(8.6)**	**13.0**	**(10.6)**	**(4.8)**	**10.0**	**(1.0)**
Bank and other loans due after one year	**(1,628.0)**	**–**	**(268.0)**	**8.0**	**(6.8)**	**–**	**(1,894.8)**
Other non-current borrowings	**(373.9)**	**–**	**–**	**33.1**	**–**	**–**	**(340.8)**
Non-current lease obligations (IAS 17 finance)	**(1,496.8)**	**–**	**(48.8)**	**23.4**	**–**	**138.0**	**(1,384.2)**
Non-current lease obligations (IAS 17 operating)	**–**	**(137.1)**	**–**	**10.6**	**–**	**91.4**	**(35.1)**
	(3,079.5)	**(145.7)**	**(26.0)**	**–**	**(12.8)**	**215.1**	**(3,048.9)**
Net borrowings in Disposal Group							**(215.1)**
Net borrowing in total Group							**(3264.0)**

Other non-cash movements for the Group include the increase in the value of financial liabilities at fair value through profit in the year of £0.3 million and the increase in borrowings from interest which is rolled into the amount repayable.

Company	Net borrowings at 1 April 2018 £m	Cash flows – other £m	Other non-cash movements £m	Net borrowings at 31 March 2019 £m
Cash and cash deposits	303.3	(18.5)	–	284.8
Bank and other loans due within one year	(149.6)	149.6	(51.8)	(51.8)
Amounts due to subsidiary undertakings	(283.6)	(0.3)	–	(283.9)
Bank and other loans due after one year	(711.7)	(225.0)	56.5	(880.2)
Other non-current borrowings	–	(109.5)	–	(109.5)
	(841.6)	(203.7)	4.7	(1,040.6)

Notes to the financial statements
continued

39. Net borrowings continued

	Net borrowings at 1 April 2019 £m	Cash flows – other £m	Other non-cash movements £m	Net borrowings at 31 March 2020 £m
Cash and cash deposits	284.8	83.1	–	367.9
Bank and other loans due within one year	(51.8)	49.6	2.2	–
Other current borrowings	–	–	(6.1)	(6.1)
Amounts due to subsidiary undertakings	(283.9)	(0.5)	–	(284.4)
Bank and other loans due after one year	(880.2)	(150.0)	(1.8)	(1,032.0)
Other non-current borrowings	(109.5)	–	6.1	(103.4)
	(1,040.6)	(17.8)	0.4	(1,058.0)

The increase in the value of financial liabilities at fair value through profit in the year of £0.3 million for the Group and £0.3 million for the Company is attributable to other non-cash movements.

40. Subsidiary and joint venture undertakings at 31 March 2020

Principal subsidiary companies	Registered office address	Country of incorporation, registration and principal operations
Water		
South West Water Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
South West Water Finance Plc	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Source Contact Management Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Waste management		
Viridor Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste Exeter Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (West Sussex) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste Management Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor EnviroScot Limited	1 Exchange Crescent, Conference Square, Edinburgh, EH3 8UL	Scotland
Viridor Resource Management Limited	First Floor Offices, Riverside House, Sir Thomas Longley Road, Medway City, Rochester, ME2 4FN	England
Viridor Waste Kent Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Oxfordshire Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor EfW (Runcorn) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Landfill Restoration) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Somerset) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Thames) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Collections) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Electrical) 1 Limited	1 Exchange Crescent, Conference Square, Edinburgh, EH3 8UL	England
Viridor Waste (Electrical) 2 Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Greater Manchester) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Polymer Recycling Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Trident Park Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor (Glasgow) Limited	1 Exchange Crescent, Conference Square, Edinburgh, EH3 8UL	Scotland
Viridor (Lancashire) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Peterborough Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor South London Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Clyde Valley Limited	1 Exchange Crescent, Conference Square, Edinburgh, EH3 8UL	Scotland
Non-household retail		
Pennon Water Services Limited*(1)	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Other		
Peninsula Insurance Limited*(2)	Level 5, Mill Court, La Charroterie, St Peter Port, GY1 1EJ	Guernsey

(1) 80% of share capital owned by Pennon Group plc. All shares in issue are ordinary shares.
(2) Captive insurance company established with the specific objective of financing risks emanating from within the Group.

40. Subsidiary and joint venture undertakings at 31 March 2020 continued

Other trading companies	Registered office address	Country of incorporation
Dragon Waste Limited (81%)	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Peninsula Leasing Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Peninsula Properties (Exeter) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Peninsula Trustees Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon Defined Contribution Pension Trustee Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon Pension Trustees Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon Trustee Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Raikes Lane Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Source for Business Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
SSWB Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England

Other dormant companies	Registered office address	Country of incorporation
A.A. Best & Sons Limited	1 Exchange Crescent, Conference Square, Edinburgh, EH3 8UL	Scotland
Acetip	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Albion Water (Shotton) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Alderney Water Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Analaq Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Aquacare (BWH) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Astley Minerals Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Avon Valley Water Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Basecall Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Bournemouth Water Investments Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Bournemouth Water Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
BWH Enterprises Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Cambridge Water Business Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Centre for Environmental Research Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
City Reclamation Services Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Corby Skip Hire Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
DMP (Holdings) Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
ELE Datasystems	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Exe Continental	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Greater Manchester Sites Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Greenhill Environmental Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Handside Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Haul Waste Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Hodgejoy Recycling Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Industrial Waste Disposals (Sheffield) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Lavelle & Sons Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Mac-Glass Recycling Limited	1 Exchange Crescent, Conference Square, Edinburgh, EH3 8UL	Scotland
Oakley Recycling Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Oakley Skip Hire Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Parkwood Environmental Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Parkwood Group Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Parkwood Recycling Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pearsons Group Holdings Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Peninsula	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Peninsula Water Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon Power Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon Share Plans (Guernsey) Limited*	Albert House, South Esplanade, St Peter Port, GY1 1AW	Guernsey
Pennon Share Scheme Trustees Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon South West Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pennon Waste Management Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
pHOX Systems Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pilsworth Forest (1996) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Pilsworth Forest Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Roseland Plant Co. Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Rydon Properties Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Seal Security Systems Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Sheffield Waste Disposal Company Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Shore Recycling (Ozone) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
South Staffordshire Water Business Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
SWW Pension Trustees Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Thames Incineration and Recycling Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HT	England
Thames Incineration Services Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Thames Tankering Services Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Thames Waste Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England

Notes to the financial statements
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40. Subsidiary and joint venture undertakings at 31 March 2020 continued

Other dormant companies	Registered office address	Country of incorporation
The Metropolitan Water Company Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Tokenmarch Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor (Cheshire) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor (Community Recycling MK) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor (Community Recycling MKH) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor (Erith) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor (Martock) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor (Winsford) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Contracting Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Electrical Recycling (Holdings) Limited	1 Exchange Crescent, Conference Square, Edinburgh, EH3 8UL	Scotland
Viridor Electrical Recycling Limited	1 Exchange Crescent, Conference Square, Edinburgh, EH3 8UL	Scotland
Viridor Enterprises Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Glass Recycling Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor London Recycling Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor New England (EfW) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Resource (Peterborough) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Resource Transport Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor South Lanarkshire Limited	1 Exchange Crescent, Conference Square, Edinburgh, EH3 8UL	Scotland
Viridor South West Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Adapt) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Allwaste Disposal) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Atherton) Holdings Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Atherton) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Bristol Holdings) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Bristol) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Bury) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Corby) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Earls Barton) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (East Anglia) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Medway Holdings) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Medway) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Sheffield) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Thetford) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste (Wastenot Recycling) Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste 2 Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste Disposal Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste Suffolk Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste Hampshire Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Viridor Waste Wootton Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
VWM (Scotland) Limited	1 Exchange Crescent, Conference Square, Edinburgh, EH3 8UL	Scotland
Waste Treatment Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
Water West Limited*	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England
West Hampshire Water Limited	Peninsula House, Rydon Lane, Exeter, EX2 7HR	England

* Indicates the shares are held directly by Pennon Group plc, the Company.

The subsidiary undertakings are wholly owned unless stated otherwise and all shares in issue are ordinary shares. All companies above are consolidated in the Group financial statements.

40. Subsidiary and joint venture undertakings at 31 March 2020 continued

Joint ventures

All joint ventures and the subsidiary undertakings of Lakeside Energy from Waste Holdings Limited, INEOS Runcorn (TPS) Holdings Limited and Shelford Composting Limited are incorporated and registered in England which is also their country of operation. The registered office of Lakeside Energy from Waste Holdings Limited and Lakeside Energy from Waste Limited is Thames House, Oxford Road, Wallingford OX10 6LX. The registered office of Shelford Composting Limited is 900 Pavilion Drive, Northampton NN4 7RG. The registered office of INEOS Runcorn (TPS) Holdings Limited and INEOS Runcorn (TPS) Limited is PO Box 9, Runcorn Site Headquarters, South Parade, Runcorn, Cheshire WA7 4JE.

	Share capital in issue	Percentage held	Principal activity
Joint ventures			
Lakeside Energy from Waste Holdings Limited	1,000,000 A ordinary shares	–	
	1,000,000 B ordinary shares	100%	
Lakeside Energy from Waste Limited			Waste management
Shares in Lakeside Energy from Waste Holdings Limited are held by Viridor Waste Management Limited			
Shelford Composting Limited	50 A ordinary shares	–	
	50 B ordinary shares	100%	Waste management
INEOS Runcorn (TPS) Holdings Limited	1,000 A ordinary shares	40%	
	186,750 B1 ordinary shares	100%	
	62,250 B2 ordinary shares	–	
INEOS Runcorn (TPS) Limited			Waste management

Shares in INEOS Runcorn (TPS) Holdings Limited are held by Viridor Waste Management Limited.

The Group's economic interest in INEOS Runcorn (TPS) Holdings Limited is 75%, as returns from the investment are based on holdings of B1 and B2 ordinary shares.

41. Operating lease commitments

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
The future aggregate minimum lease payments under non-cancellable operating leases are:				
Within 1 year	**–**	12.5	**–**	–
Over 1 year and less than 5 years	**–**	37.7	**–**	–
Over 5 years	**–**	145.5	**–**	–
	–	195.7	**–**	–

Following the adoption of IFRS 16 on 1 April 2019 operating lease commitments are included in borrowings as lease liabilities.

42. Contingencies

Contingent liabilities

	Group		Company	
	2020 £m	2019 £m	**2020 £m**	2019 £m
Guarantees:				
Borrowing facilities of subsidiary undertakings	**–**	–	**460.9**	561.5
Performance bonds	**197.1**	201.7	**197.1**	201.7
	197.1	201.7	**658.0**	763.2

Guarantees in respect of performance bonds are entered into in the normal course of business. No liability is expected to arise in respect of the guarantees. All of the performance bonds relate to the activities of the Disposal Group.

In connection with the application of the audit exemption under Section 479A of the Companies Act 2006 the Company has guaranteed all the outstanding liabilities as at 31 March 2020 of Viridor Waste 2 Limited since this company qualifies for the exemption.

Other contractual and litigation uncertainties

The Group establishes provisions in connection with contracts and litigation where it has a present legal or constructive obligation as a result of past events and where it is more likely than not an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Matters where it is uncertain that these conditions are met include potential prosecutions by the Health and Safety Executive.

Notes to the financial statements
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43. Capital commitments

	Group 2020 £m	Group 2019 £m	Company 2020 £m	Company 2019 £m
Contracted but not provided relating to the Continuing Group	**72.0**	68.3	**–**	–

Excluded from the balances at 31 March 2020 above is £98.6 million relating to discontinued operations (see note 46 for further details).

44. Related party transactions

During the year Group companies entered into the following transactions with joint ventures who are not members of the Group. The year end balances as at 31 March 2020 with joint ventures are included within assets held for sale (see note 46 for further details).

	2020 £m	2019 £m
Sales of goods and services		
INEOS Runcorn (TPS) Limited	**18.2**	16.6
Purchase of goods and services		
Lakeside Energy from Waste Limited	**12.8**	12.4
INEOS Runcorn (TPS) Limited	**8.3**	7.1
Dividends received		
Lakeside Energy from Waste Holdings Limited	**6.0**	5.5

Year-end balances

	2020 £m	2019 £m
Receivables due from related parties		
Lakeside Energy from Waste Limited (loan balance)	**7.1**	7.7
INEOS Runcorn (TPS) Limited (loan balance)	**59.5**	65.0
	66.6	72.7
Lakeside Energy from Waste Limited (trading balance)	**1.0**	1.0
INEOS Runcorn (TPS) Limited (trading balance)	**1.2**	1.8
	2.2	2.8
Payables due to related parties		
Lakeside Energy from Waste Limited (trading balance)	**1.1**	0.9
INEOS Runcorn (TPS) Limited (trading balance)	**1.7**	3.2
	2.8	4.1

The £66.6 million (2019 £72.7 million) receivable relates to loans to related parties due for repayment in instalments between 2018 and 2033. Interest is charged at an average of 13.0% (2019 13.0%).

Company

The following transactions with subsidiary undertakings occurred in the year:

	2020 £m	2019 £m
Sales of goods and services (management fees)	**17.9**	19.7
Purchase of goods and services (support services)	**0.6**	2.0
Interest receivable	**43.4**	43.3
Interest payable	**0.1**	0.1
Dividends received	**335.6**	196.7

Sales of goods and services to subsidiary undertakings are at cost. Purchases of goods and services from subsidiary undertakings are under normal commercial terms and conditions which would also be available to unrelated third parties.

44. Related party transactions continued

Year-end balances

	2020 £m	2019 £m
Receivables due from subsidiary undertakings		
Loans	**1,225.6**	1,044.6
Trading balances	**16.0**	19.9

Interest on £591.8 million of the loans has been charged at fixed rates during the year with an average effective rate of 4% (2019 £499.8 million charged at 5%), and on £591.8 million at an average effective rate of three-month LIBOR plus 2.6% (2019 £499.8 million charged at 12-month LIBOR + 2.2%). Interest on £16.0 million (2019 £18.1 million) has been charged at a fixed rate of 6.0%. These loans are due for repayment in instalments over the period 2021 to 2045.

Interest on £13.0 million (2019 £13.5 million) of the loans has been charged at a fixed rate of 5.0%. Interest on £13.0 million (2019 £13.5 million) of the loans has been charged at 12-month LIBOR + 3.0%. These loans are due for repayment in instalments over a five-year period following receipt of a request to repay.

No material expected credit loss provision has been recognised in respect of loans to subsidiaries (2019 £nil).

	2020 £m	2019 £m
Payables due to subsidiary undertakings		
Loans	**284.4**	283.9
Trading balances	**9.1**	14.3

The loans from subsidiary undertakings are unsecured and interest-free without any terms for repayment.

45. Change in accounting policy on leases

Adjustments recognised on the adoption of IFRS 16

This note explains the impact of the adoption of IFRS 16 'Leases' on the Group's financial statements, and it discloses the new accounting policies that have been adopted from 1 April 2019, where they are different from those applied in earlier periods.

On adoption of IFRS 16, the Group recognised lease liabilities in relation to leases which had previously been classified as 'operating leases' under the principles of IAS 17 'leases'. These liabilities were measured at the present value of the remaining leases payments, discounted using the Group's weighted average incremental borrowing rate (IBR).

Following adoption of IFRS 16, the Group no longer distinguishes between an on the balance sheet finance lease and an off the balance sheet operating lease. For leases previously classified as finance leases, the Group recognised the carrying amount of leased assets and lease liabilities immediately prior to transition as the carrying amount of the right-of-use asset and lease liability at the date of initial application. The measurement principles of IFRS 16 only apply after this date.

As permitted under IFRS 16, the Group will present right-of-use assets and lease liabilities within property, plant and equipment and borrowings respectively. This approach is consistent with the Group's previous presentation of finance leases under IAS 17.

At 31 March 2019, the Group had non-cancellable operating lease commitments of £195.7 million. These predominantly relate to leases of properties occupied by the Group in the course of carrying out its businesses. On transition on 1 April 2019, the Group recognised the following items in the balance sheet:

- Right-of-use assets – increase by £132.2 million
- Prepayments – decrease by £0.5 million
- Lease liabilities – increase by £145.7 million
- Accruals – decrease by £4.2 million
- Deferred tax liabilities – decrease by £1.8 million
- Retained earnings – decrease by £8.0 million.

The discount rate used in the calculation of the lease liability involves estimation. The discount rate is calculated on a lease by lease basis. For vehicle leases, which account for less than 1% of the present value of future lease payments, the discount rate is determined by the implicit rate within the lease. For all other leases, where implicit rates are not available, discount rates are calculated using the Group's estimated IBR for each lease. The IBR is determined with reference to applicable reference rate borrowing curves (e.g. LIBOR or its successor), credit margins for the different business segments and lease terms. At the commencement of new leases discount rates are updated to ensure the Group applies the IBR that reflects current market conditions. At 1 April 2019, the date of transition to IFRS 16, the range of rates used was between 2.43% and 4.5% and the weighted average IBR across all leases was 3.6%. If the weighted average rate used was increased by 10bps, this would result in a c.0.9% reduction in the present value of lease liabilities recognised at 1 April 2019.

Notes to the financial statements
continued

45. Change in accounting policy on leases continued

A reconciliation of the lease liability recognised at 1 April 2019 to operating lease commitments at 31 March 2019 is shown below:

	£m
IAS 17 operating lease commitments	**195.7**
Less: contracts to which the short-term leases exemption has been applied	(0.1)
Less: contracts to which the low-value leases exemption has been applied	(1.6)
Add: adjustment due to different assessment of lease term	0.5
Less: impact of discounting at weighted average discount rate of 3.6%	(48.8)
Operating lease liabilities recognised at 31 March 2019	**145.7**
Add: finance lease liabilities recognised at 31 March 2019	1,560.4
IFRS 16 lease liability as at 1 April 2019	**1,706.1**
Of which:	
Current lease liabilities	19.4
Non-current lease liabilities	1,686.7
	1,706.1

Associated right-of-use assets for selected land and building leases were measured on a retrospective basis as if IFRS 16 had always applied from lease inception. All remaining right-of-use assets were measured at the amount equal to the lease liability, adjusted by prepaid or accrued lease payments under IFRS 16 transition provisions relating to leases recognised on the balance sheet at 31 March 2019.

A reconciliation between the opening lease liabilities and right-of-use assets at 1 April 2019 is shown below:

	£m
Lease liabilities following first application of IFRS 16	145.7
Less: adjustment for onerous lease accruals	(1.5)
Less: adjustment for other accruals	(2.9)
Add: adjustment for prepaid lease rentals	0.5
Less: adjustment due to application of IFRS 16 at lease inception	(9.6)
Right-of-use assets on first application of IFRS 16	**132.2**

In applying IFRS 16 for the first time, the Group has used the following practical expedients and made the following elections permitted by the standard:

- The use of single discount rates to portfolios of leases with similar characteristics
- Reliance on previous onerous lease assessments
- Accounting for operating leases with terms less than 12 months as at 1 April 2019 as short-term leases
- The application of hindsight, such as in determining the lease term if the contract contains options to extend or terminate the lease
- Applying the modified retrospective approach: the cumulative effect of initially applying IFRS 16 has been calculated as a reduction to retained profits at 1 April 2019 of £8.0 million. Under this election no restatement of comparative figures will be made
- Electing to apply the standard to contracts that were previously identified as leases when applying IAS 17.

Cash outflows in respect of leasing relate to principal repayments of £142.8 million and interest repayments of £37.7 million, in addition to inflows from lease financing arrangements of £115.0 million.

References to disclosures required by IFRS 16 but not included within this note are outlined below:

- Right-of-use asset depreciations, additions and net book value (see page 161)
- Interest on lease liabilities (see page 153)
- Short-term and low value lease expense (see page 153)
- Maturity analysis of lease liabilities (see page 169).

Based on the additional lease liability and associated assets recognised at 1 April 2019 for the Continuing Group the impact on profit for the year ended 31 March 2020 was a reduction in profit after tax of £0.6 million, resulting from:

- An increase in EBITDA of £1.9 million
- An increase in depreciation of £1.4 million
- An increase in finance costs of £1.2 million; and
- A reduction in corporation tax of £0.1 million.

EBITDA increased as operating lease costs previously charged against EBITDA under IAS 17 has been replaced under IFRS 16 with charges for depreciation and interest which are excluded from EBITDA (albeit included in earnings). Short-term and low value leasing costs continue to be charged against EBITDA.

Net operating cash flows increased under IFRS 16 as the element of cash paid attributable to the repayment of principal is included in financing cash flows. The net increase/decrease in cash and cash equivalents remains unchanged.

46. Discontinued operations and non-current assets held for sale

On 18 March 2020, the Group entered into a formal sale agreement to dispose of Viridor Limited to Planets UK Bidco Limited (Bidco), a newly formed company established by funds advised by Kohlberg Kravis Roberts & Co. L.P. (KKR). In accordance with IFRS 5 'Non-current assets held for sale and discontinued operations', the assets and liabilities related to Viridor were classified as a disposal group held for sale at 31 March 2020. The sale is conditional on approval by the Group's shareholders, merger control clearance from the European Commission and certain other conditions. The first two of these conditions have now been met and the sale is expected to complete in early summer 2020.

The agreed proceeds indicate a £3.7 billion estimated fair value less costs to sell, which exceeds the carrying value of Viridor's net assets, and accordingly no impairment losses have been recognised on reclassification as a disposal group.

The tables below show the results of the discontinued operations which are included in the Group income statement and cash flow statement for the year ended 31 March 2020, together with the classes of assets and liabilities comprising the operations held for sale in the Group balance sheet as at 31 March 2019.

	Notes	Before non-underlying items 2020 £m	Non-underlying items (note 6) 2020 £m	Total 2020 £m	Before non-underlying items 2019 £m	Non-underlying items (note 6) 2019 £m	Total 2019 £m
Discontinued operations							
Revenue	5	**753.2**	**–**	**753.2**	845.6	–	845.6
Operating costs							
Employment costs		**(130.4)**	**4.9**	**(125.5)**	(138.6)	(0.9)	(139.5)
Raw materials and consumables used		**(87.2)**	**–**	**(87.2)**	(94.3)	–	(94.3)
Other operating expenses		**(337.5)**	**(1.1)**	**(338.6)**	(433.8)	(28.7)	(462.5)
Earnings before interest, tax, depreciation and amortisation	5	**198.1**	**3.8**	**201.9**	178.9	(29.6)	149.3
Depreciation and amortisation		**(82.1)**	**–**	**(82.1)**	(78.0)	–	(78.0)
Operating profit		**116.0**	**3.8**	**119.8**	100.9	(29.6)	71.3
Finance income		**22.5**	**–**	**22.5**	20.0	–	20.0
Finance costs		**(48.7)**	**–**	**(48.7)**	(44.8)	–	(44.8)
Net finance costs		**(26.2)**	**–**	**(26.2)**	(24.8)	–	(24.8)
Share of post-tax profit from joint ventures		**14.8**	**–**	**14.8**	12.4	–	12.4
Profit before tax	5	**104.6**	**3.8**	**108.4**	88.5	(29.6)	58.9
Taxation (charge)/credit	9	**(13.6)**	**(11.0)**	**(24.6)**	(10.6)	5.7	(4.9)
Profit for the year		**91.0**	**(7.2)**	**83.8**	77.9	(23.9)	54.0
Attributable to:							
Ordinary shareholders of the parent				**83.8**			54.0

	2020 £m	2019 £m
Cash flows from operating activities	**149.1**	69.2
Cash flows from investing activities	**(133.0)**	(255.6)
Cash flows from financing activities	**(23.1)**	(73.1)
Net decrease in cash and cash equivalents from discontinued operations, net of inter-company	**(7.0)**	(259.5)

Notes to the financial statements
continued

46. Discontinued operations and non-current assets held for sale continued

The net assets relating to the Disposal Group at 31 March 2020 in the Group and Company balance sheet are shown below:

	Group £m	Company £m
Assets of the Disposal Group		
Goodwill	**340.8**	–
Other intangible assets	**86.9**	–
Property, plant and equipment	**1,584.9**	–
Other non-current assets	**261.5**	–
Investment in subsidiary undertakings	**–**	1,135.6
Investments in joint ventures	**60.1**	–
Inventories	**29.9**	–
Trade and other receivables	**277.9**	–
Cash and cash deposits	**33.3**	–
Total assets	**2,675.3**	1,135.6
Liabilities of the Disposal Group		
Borrowings	**(248.4)**	–
Trade and other payables	**(141.7)**	–
Current tax liabilities	**(1.0)**	–
Provisions	**(237.6)**	–
Other non-current liabilities	**(14.3)**	–
Retirement benefit obligations	**(15.1)**	
Deferred tax liabilities	**(98.2)**	–
Total liabilities	**(756.3)**	–
Net assets	**1,919.0**	1,135.6

At 31 March 2020 trade and other receivables include a net other receivable of £43.7 million (2019 £43.3 million) relating to gross contractual compensation amounts due totalling £72.0 million (2019 £72.0 million) arising from additional costs incurred in the construction of the Glasgow Recycling and Renewable Energy Centre (GRREC). A full credit risk appraisal has been carried out on this receivable and a provision of £28.3 million (2019 £28.7 million) has been recognised for expected credit losses as detailed in note 4.

The Company has classified its investment in ordinary shares in Viridor Limited as an asset held for sale. On completion of the proposed sale of Viridor, expected in early summer 2020, loans made to Viridor of £1,200 million at 31 March 2020 will be repaid.

Provisions include environmental and landfill provisions relating to landfill sites totalling £201.2 million at 31 March 2020.

Included in provisions are amounts provided in relation to the expected economic outflow of resources required to settle claims associated with ongoing litigation which were transferred from other non-current liabilities in the year. These amounts are considered by the Directors and the management of the Group to be the best estimate of the amounts that might be finally settled. Further disclosures have not been provided in accordance with IAS 37 paragraph 92, as the Group believes they are commercially sensitive and doing so would be seriously prejudicial to the Group's position.

47. Events after the reporting period

Repayment of perpetual capital securities

On 6 May 2020, the Company exercised its sole discretionary right to redeem all of the £300 million perpetual capital securities at their principal amount on 22 May 2020, this being the first available date to exercise this right.

Disposal of Viridor

On 18 March 2020 the Group announced the sale of Viridor to KKR subject to shareholder, competition authority approval and other conditions. The first two of these conditions have now been met and the final condition can be waived at Pennon's discretion, giving the Group control of the timetable to complete the transition during early summer 2020.

Impact of COVID-19

The World Health Organization (WHO) announced that COVID-19 was a global pandemic on 11 March 2020 and the UK Government announced its wide ranging lockdown restrictions on 23 March 2020. Given these events took place prior to the Group and Company's financial year end of 31 March 2020, the Directors have taken the impact of these events into account when making its key judgements and estimates at the balance sheet date, as outlined in note 4 to the accounts, up to the date of approving the annual report and accounts.

The Group's operational response to COVID-19 is set out throughout the strategic review section of the annual report on pages 6 to 57. In addition, the risk report on pages 58 to 67 sets out the updated risk assessment in response to the pandemic.

In assessing its going concern and viability the impacts of COVID-19 on these assessments has been considered in full and are set out on pages 119 and page 68 respectively.

Alternative performance measures and glossary

Alternative performance measures (APMs) are financial measures used in this report that are not defined by International Financial Reporting Standards (IFRS). The Directors believe that these APMs assist in providing additional useful information on the underlying trends, performance and position of the Group as well as enhancing the comparability of information between reporting periods. As the Group defines the APMs they might not be directly comparable to other companies' APMs. They are not intended to be a substitute for, or superior to, IFRS measurements.

Underlying earnings

Underlying earnings are presented alongside statutory results as the Directors believe they provide a more useful comparison on business trends and performance. Note 6 in the financial statements provides more detail on non-underlying items, and a reconciliation of underlying earnings for the current year and the prior year is as follows:

Underlying earnings reconciliation 2020

£m	Total Group underlying (incl. discontinued operations)	Underlying discontinued operations	Non-underlying items from continuing operations	Statutory results	Earnings per share (p)
EBITDA (see below)	563.4	198.1	(7.9)	357.4	
Operating profit	361.5	116.0	(7.9)	237.6	
Profit before tax	287.6	104.6	10.1	193.1	
Taxation	(52.0)	(13.6)	(32.2)	(70.6)	
Profit after tax from continuing operations				122.5	
Profit after tax from discontinued operations				83.8	
Profit after tax (PAT)				206.3	
PAT attributable to perpetual capital holders				(7.0)	
Non-controlling interests				1.1	
PAT attributable to shareholders				200.4	47.7
Deferred tax before non-underlying items				33.2	7.9
Non-underlying items post tax				29.3	6.9
Non-controlling interests' share of non-underlying items				(1.0)	(0.2)
Adjustment for full year depreciation charge in the Disposal Group				(2.6)	(0.6)
Underlying earnings				259.3	61.7

Underlying earnings reconciliation 2019

£m	Total Group underlying (incl. discontinued operations)	Underlying discontinued operations	Non-underlying items from continuing operations	Statutory results	Earnings per share (p)
EBITDA (see below)	546.2	178.9	3.9	371.2	
Operating profit	351.0	100.9	3.9	254.0	
Profit before tax	280.2	88.5	9.7	201.4	
Taxation	(42.7)	(10.6)	(0.7)	(32.8)	
Profit after tax from continuing operations				168.6	
Profit after tax from discontinued operations				54.0	
Profit after tax (PAT)				222.6	
PAT attributable to perpetual capital holders				(8.6)	
Non-controlling interests				0.3	
PAT attributable to shareholders				214.3	51.1
Deferred tax before non-underlying items				13.3	3.1
Non-underlying items post tax				14.9	3.6
Underlying earnings				242.5	57.8

EBITDA

EBITDA (earnings before interest, tax, depreciation and amortisation) is used to assess and monitor operational underlying performance. An adjusted EBITDA is also presented that includes Viridor's share of EBITDA from its joint ventures and finance income on service concession arrangements. This measure is presented to aggregate earnings from all the Viridor ERFs which are accounted for differently depending upon the contractual relationships, as shown in the reconciliation below.

Alternative performance measures and glossary
continued

Adjusted EBITDA reconciliation

£m	2020			2019		
	Total Group underlying (incl. discontinued operations)	**Discontinued operations**	**Continuing operations**	Total Group underlying (incl. discontinued operations)	Discontinued operations	Continuing operations
Statutory EBITDA	**559.3**	**201.9**	**357.4**	520.5	149.3	371.2
Non-underlying items	**4.1**	**(3.8)**	**7.9**	25.7	29.6	(3.9)
Underlying EBITDA	**563.4**	**198.1**	**365.3**	546.2	178.9	367.3
IFRIC 12 interest receivable(1)	**15.1**	**15.1**	**–**	14.6	14.6	–
Joint venture EBITDA(1)	**41.3**	**41.3**	**–**	31.9	31.9	–
Adjusted EBITDA	**619.8**	**254.5**	**365.3**	592.7	225.4	367.3

(1) These adjustments relate to the waste management business, resulting in adjusted waste management EBITDA of £254.5 million (2018/19 £225.4 million).

Total Group effective interest rate

A measure of the mean average interest rate payable on the Group's net debt, which excludes interest costs not directly associated with Group net debt. This measure is presented to assess and monitor the relative cost of financing for the Group.

	2020 £m	2019 £m
Net finance costs after non-underlying items	**70.7**	77.4
Non-underlying net finance costs	**18.0**	5.8
Interest receivable on shareholder loans to joint ventures	**5.3**	5.3
Net interest on retirement benefit obligations	**(0.8)**	(1.4)
Unwinding of discounts on provisions	**(8.2)**	(11.1)
Interest receivable on service concession agreements	**15.1**	14.6
Capitalised interest	**11.0**	15.2
Net finance costs for effective interest rate calculation	**111.1**	105.8
Opening net debt	**3,079.5**	2,801.5
Closing net debt	**3,264.0**	3,079.5
Average net debt (opening net debt + closing net debt divided by 2)	**3,171.8**	2,940.5
Effective interest rate	**3.5%**	3.6%

Total Group interest cover

Underlying net finance costs (excluding pensions net interest cost, discount unwind on provisions and IFRIC 12 interest receivable on service concession arrangements) divided by Group operating profit before non-underlying items.

	2020 £m	2019 £m
Net finance costs after non-underlying items	**70.7**	77.4
Non-underlying net finance costs	**18.0**	5.8
Net interest on retirement benefit obligations	**(0.8)**	(1.4)
Unwinding of discounts in provisions	**(8.2)**	(11.1)
Interest receivable on service concession arrangements	**15.1**	14.6
Net finance costs for interest cover calculation	**94.8**	85.3
Operating profit before non-underlying items	**361.5**	351.0
Interest cover (times)	**3.8**	4.1

Total Group dividend cover

Proposed dividends divided by profit for the year before non-underlying items and deferred tax.

	2020 £m	2019 £m
Proposed dividends	**184.3**	172.7
Profit for the year attributable to ordinary shareholders	**200.4**	214.3
Deferred tax charge before non-underlying items	**33.2**	13.3
Non-underlying items after tax in profit for the year	**29.3**	14.9
Non-controlling interests' share of non-underlying items	**(1.0)**	–
Adjustment for full year depreciation charge in the Disposal Group	**(2.6)**	–
Adjusted profit for dividend cover calculation	**259.3**	242.5
Dividend cover (times)	**1.4**	1.4

Total Group capital investment

Property, plant and equipment additions plus IFRIC 12 service concession expenditure (ERFs) less landfill restoration asset (spend accounted for through provisions). The measure is presented to assess and monitor the total capital investment by the Group.

	2020 £m	2019 £m
Additions to property, plant and equipment	**326.8**	387.2
Additions to intangible assets	**0.6**	–
Landfill restoration asset	**(5.3)**	(22.8)
IFRIC 12 additions to other intangible assets – service concession agreements	**–**	24.7
IFRIC 12 additions to non-current assets – service concession agreements	**17.1**	6.8
IFRIC 12 additions to current trade and other receivables – prepayments and accrued income	**–**	3.3
Less: IFRIC 12 additions subject to legal contractual process	**–**	(3.3)
Capital investment	**339.2**	395.9

Following the adoption of IFRS 16 Property, plant and equipment additions in 2020 include right-of-use assets £6.2 million (2019 £nil million). These assets are directly associated with leases previously classified as operating leases under IAS 17. In 2019, under IAS 17, operating leases and associated assets were not held on the balance sheet.

Total Group capital payments

Payments for property, plant and equipment additions net of proceeds from sale of property, plant and equipment plus IFRIC 12 service concession expenditure (ERFs). The measure is presented to assess and monitor the net cash spend on property, plant and equipment.

	2020 £m	2019 £m
Cash flow statements: purchase of property, plant and equipment	**332.8**	356.0
Cash flow statements: purchase of intangible assets	**0.6**	–
Cash flow statements: proceeds from sale of property, plant and equipment	**(10.6)**	(6.3)
IFRIC 12 additions to other intangible assets – service concession agreements	**–**	24.7
IFRIC 12 additions to non-current assets – service concession agreements	**17.1**	6.8
IFRIC 12 additions to current trade and other receivables – prepayments and accrued income	**–**	3.3
Capital payments	**339.9**	384.5

Total Group return on capital employed

The total of underlying operating profit, joint venture profit after tax and joint venture interest receivable divided by capital employed (net debt plus total equity invested). An average value for this metric is part of the long-term incentive plan for Directors.

	2020 £m	2019 £m
Underlying operating profit	**361.5**	351.0
Underlying joint venture profit after tax	**14.8**	12.4
Joint venture interest receivable	**5.3**	5.3
Adjusted profit for return on capital employed calculation	**381.6**	368.7
Values at year end:		
Net debt	**3,264.0**	3,079.5
Share capital	**171.3**	171.1
Share premium account	**227.0**	223.6
Capital redemption reserve	**144.2**	144.2
Perpetual capital securities	**296.7**	296.7
Capital employed for return on capital employed calculation	**4,103.2**	3,915.1
Return on capital employed	**9.3%**	9.4%

Alternative performance measures and glossary
continued

Total Group operational cash inflows
Cash generated from operations before construction spend on service concession agreements, pension contributions and other tax payments.

	2020 £m	2019 £m
Cash generated from operations per cash flow statements	**516.3**	399.8
IFRIC 12 additions to other intangible assets – service concession agreements	**–**	24.7
IFRIC 12 additions to non-current assets – service concession agreements	**17.1**	6.8
IFRIC 12 additions to current trade and other receivables – prepayments and accrued income	**–**	3.3
Pension contributions	**48.1**	32.2
Other tax payments[1]	**147.1**	137.9
Payment in respect of terminated synthetic derivative, related to a prior period non-underlying charge	**–**	44.3
Operational cash inflows	**728.6**	649.0

(1) Other taxes include business rates, employers' national insurance, fuel excise duty, carbon reduction commitment, environmental payments, climate change levy and external landfill tax.

RoRE
This is a key regulatory metric which represents the returns to shareholders expressed as a percentage of regulated equity.

Returns are made up of a base return (set by Ofwat the water business regulator at c.6.0% for 2015-20) plus totex outperformance, financing outperformance and ODI outperformance. Returns are calculated post tax and post sharing (only a proportion of returns are attributed to shareholders and shown within RoRE). The three different types of return calculated and added to the base return are:

- Totex outperformance – totex is defined below and outperformance is the difference between actual reported results for the regulated business compared to the Final Determination (Ofwat published document at the start of a regulatory period), in a constant price base
- Financing outperformance – is based on the difference between a company's actual effective interest rate compared with Ofwat's allowed cost of debt
- ODI outperformance – the net reward or penalty a company earns based on a number of different key performance indicators, again set in the Final Determination.

Regulated equity is a notional proportion of regulated capital value (RCV which is set by Ofwat at the start of every five-year regulatory period, adjusted for actual inflation). For 2015-20, the notional equity proportion is 37.5%.

Further information on this metric can be found in South West Water's Annual Performance Report and regulatory reporting, published in July each year. The most recent can be found at: www.southwestwater.co.uk/about-us/how-are-we-performing.

Totex
Operating costs and capital expenditure of the regulated water and wastewater business (based on the Regulated Accounting Guidelines).

ODI
ODIs are designed to incentivise companies to deliver improvements to service and outcomes based on customers' priorities and preferences. If a company exceeds these targets a reward can be earned through future higher revenues. If a company fails to meet them, they can incur a penalty through lower future allowed revenues.