

Corporate governance report

Code principles

Leadership

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Code principle – Leadership

Introduction by Dr John McAdam

“There is renewed focus on how boards discharge their duties, having regard to the long-term success of the company for its members and wider stakeholders. I hope, when you have read our strategic report (on pages 10 to 49) and this corporate governance report, you will be left with an understanding of how we operate our business on a day-to-day basis, whilst looking to the future to ensure we continually focus on our strategy of delivering the best service to customers, at the lowest sustainable cost while acting in a responsible manner.”

Overview of the board’s responsibilities

- › Sets the strategy of the group, ensuring the long-term success of the group for customers, investors and wider stakeholders and in creating shareholder value
- › Is responsible for challenging and encouraging the executive team in its interpretation and implementation of how it manages the business, and that it is doing so in accordance with the strategic goals the board has set
- › Has responsibility for ensuring the company’s internal control systems (including financial, operational and compliance) and processes are sound and fit for purpose. See the ‘accountability’ section of this report on page 72 for more detail

- › Must ensure that the company has the necessary financial resources and people with the necessary skills to achieve its objectives. It also reviews managerial performance annually
- › Has oversight of capital expenditure projects within U UW which exceed £50 million, and any project which materially increases the group’s risk profile or is not in the ordinary course of the group’s business

Full details of the matters that the board has reserved for its own decision-making, due to their importance to the business or the working of the board, can be found on our website at:

corporate.unitedutilities.com/corporate-governance

Governance structure for our board and our committees

In line with the Code, the board delegates certain roles and responsibilities to its principal board committees, as shown in the diagram opposite. Whilst the board retains overall responsibility, a sub-committee structure allows these committees to probe the subject matter more deeply and gain a greater understanding of the detail, and then report back to the board on the matters discussed, decisions taken, and where appropriate, make recommendations to the board on matters requiring its approval. The reports of the principal board committees required by the Code can be found on the subsequent pages. Minutes of the board and principal committee meetings (with the exception of the remuneration committee) are tabled at board meetings and the chairs of each of the board committees report verbally to the board on their activities. The Chairman chairs the nomination committee; all other principal board committees are chaired by independent non-executive directors who have particular skills or interests in the activities of those committees.

The executive team is chaired by the Chief Executive Officer (CEO), and its members are the senior managers who have a direct reporting line to the CEO. The executive team meets monthly; it is responsible for operational matters and implementing the strategies that the board has set, and the day-to-day running of the business. Short biographies of the executive team can be found on our website at: corporate.unitedutilities.com/united-utilities-executive-team

The structure chart shown opposite also shows the principal management committees and a brief description of their roles. These committees enable senior management to understand and, if necessary, challenge the business in its interpretation of the implementation of the strategies the board has set. The board received reports from the CEO and Chief Financial Officer (CFO) at every scheduled board meeting, providing the board with an updated overview of the business and its financial performance and position.

Governance structure of the board and its principal committees and the principal management committees.



Key:

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

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Summary of board activity in 2016/17

	Cross reference	Link to strategic objectives
Leadership and employees		
— Regular review of health and safety incidents of employees and contractors reflecting the company's belief that 'nothing we do is worth getting hurt for'	See page 38	
— Considered board succession planning and the appointment of a new non-executive director	See page 68	
— Reviewed and discussed executive succession plans and the needs of the business; the potential changes arising out of market reform; and received an update on the activities to develop talented employees in the senior leadership team but also extending this focus to middle management and further increasing diversity, given the strong progress already made in the apprentice and graduate programmes	See page 66	
— Discussed the results of the annual employee engagement survey	See page 38	 
Strategy		
— Reviewed the group's corporate responsibility activities focusing on reputation management, particularly in our communication with stakeholders	See page 84	
— Received regular updates at each meeting of items with strategic component, such as emerging changes to regulation, major capital expenditure and business structuring decisions		  
— Held the annual full day strategy session debating and discussing the context of the next price review, the key issues to be addressed and considered the expectations of our key stakeholders	See page 5	  
Governance		
— Reviewed and debated the risk profile of the group and in particular the principal risks which included greater visibility of operational risks following a change in the underlying risk assessment process	See page 46	  
— Reviewed the effectiveness of the risk management systems, including financial, operational and compliance controls and reviewed the effectiveness of the internal control systems	See page 72	  
— Reviewed and discussed developments in cybercrime and the activities undertaken to enhance the effectiveness of the group's security controls and work with various government agencies and a number of other water companies to define cyber security guiding principles for use across the industry	See page 23	 
— Reviewed the terms of reference for the audit, remuneration, treasury and corporate responsibility committees and received post-meeting reports from the chairs of each committee summarising discussions and actions		
— Reviewed biannual updates on changes and developments in corporate governance and the implementation of any changes required	See page 64	
— Reviewed and discussed the annual evaluation of the board, its committees and individual directors and conflicts of interest	See page 63	
— Reviewed the performance of the external auditor and recommendation for reappointment	See page 76	 
— Reviewed the approach, background work and progress of work to identify areas where there is any risk of modern slavery occurring in our supply chain contributing to the development of and approval of the slavery and human trafficking statement	See page 115	

Key:

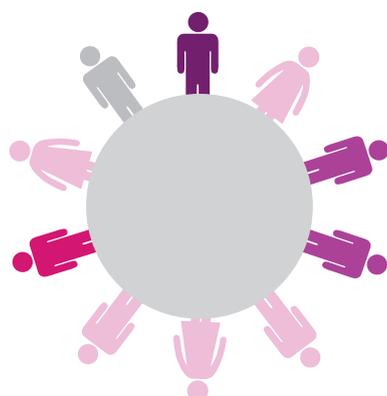
 The best service to customers  At the lowest sustainable cost  In a responsible manner

Summary of board activity in 2016/17

	Cross reference	Link to strategic objectives
United Utilities Water Limited (UW) regulated business		
— Reviewed the progress with the implementation of the recommendations of the internal investigation undertaken by Mark Clare, senior independent director, in relation to the August 2015 Lancashire water quality incident and lessons learnt	See page 72	
— Regular updates on the progress of our preparations (supported by independent assurance, particularly in relation to systems readiness), on the transfer of the commercial customer base to Water Plus (the group's joint venture with Severn Trent) prior to the opening of the market for commercial customers on 1 April 2017 along with monitoring the changes to our own systems and processes supporting our role as a wholesaler of water and wastewater services	See page 4	
— Monitored progress of the implementation of the customer experience programme to improve customer service including new initiatives such as 'Priority Services' and 'Moving Home', improved training for employees handling customer calls and systems improvements	See page 35	
— Received regular updates on developments by Ofwat's view of the next five-year asset management period (known as 'Water 2020') and its approach to the Price Review in 2019	See page 5	
Other group business		
— Reviewed progress on the group's renewable energy generation capabilities and opportunities for expansion and innovation including developing our plans around battery storage of power for use overnight when solar panels are not generating	See page 23	
— Regular updates on the progress of the joint venture Water Plus' preparedness prior to the opening of the market for commercial customers on 1 April 2017	See page 4	
Shareholder relations		
— Received and discussed a presentation by Makinson Cowell (in May 2016) on investors' views and perceptions (after a tender process Rothschild Investor Advisory were appointed as investor relations advisers with effect from 1 April 2017)	See page 71	
— Received and discussed feedback from roadshows/presentations to investors by the CEO and/or the CFO and communications from large investors	See page 71	
Financial		
— Reviewed the 2016-20 business plan and approved the 2017/18 budget		
— Reviewed and approved the half and full year results and associated announcements		
— Reviewed and approved the company's tax strategy	See page 110	
— Reviewed and approved the company's treasury policy, the group's funding requirements for the year and the potential sources to meeting these funding requirements (including the first issue of consumer price index-linked debt) and managing the group's interest rate and other market risk exposures including the impact of Brexit	See page 42	
— Reviewed progress with material litigation involving the group	See page 47	
— Reviewed and discussed pensions and proposals in relation to the United Utilities defined benefit pension scheme and related discussions with the trade unions		

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The boardroom table



- Chairman
- Executive director
- Senior independent non-executive director
- Independent non-executive director
- Company secretary

Attendance at board and committee meetings

Eight scheduled board meetings were planned and held during the year (2016: eight). A number of other board meetings and telephone conferences were also held during the year, as the need arose.

The table below shows the actual number of scheduled meetings attended and the maximum number of scheduled meetings which the directors could have attended. Only in exceptional circumstances would directors not attend board and committee meetings. Similarly, every effort is made to attend ad hoc meetings either in person or via the use of video or telephone conferencing facilities if needs be. None of our non-executive directors have raised concerns over the time commitment required of them to fulfil their duties.

On the evening before most scheduled board meetings all the non-executive directors meet together with the CEO; this time is usefully spent enabling board colleagues to share views and consider issues impacting the company. Time together also helps to build relationships on a personal level, which contributes to better relationships and decision-making around the board table.

	Board meetings	Audit committee	Remuneration committee	Nomination committee	Corporate responsibility committee	Treasury committee
Dr John McAdam	8/8	–	–	4/4	–	–
Steve Mogford	8/8	–	–	–	2/2	–
Russ Houlden	8/8	–	–	–	–	4/4
Dr Catherine Bell ⁽¹⁾	4/4	1/1	3/3	2/2	–	–
Stephen Carter	8/8	4/4	–	3 ⁽²⁾ /4	2/2	–
Mark Clare	8/8	–	6/6	4/4	–	–
Alison Goligher	3/3	4/4	3/3	2/2	2/2	–
Brian May	8/8	4/4	–	4/4	–	4/4
Sara Weller	8/8	–	6/6	4/4	–	–

Actual number of meetings attended/maximum number of scheduled meetings which the directors could have attended during 2016/17.

Excludes Paulette Rowe who was not appointed until 1 July 2017.

(1) Dr Catherine Bell stepped down from the board on 22 July 2016.

(2) Stephen Carter was unable to attend a meeting of the nomination committee due to a conflicting commitment.

Code principle – Effectiveness

Introduction by Dr John McAdam

“Board colleagues have approached the evaluation process with resolve this year, underpinned by the forthcoming challenges of competition and the lessons learnt from the 2015 Lancashire water quality incident.”

Board evaluation

Our board evaluation was again conducted internally this year; our last external evaluation was conducted by Lintstock consultants in 2015.

The internal evaluation process was facilitated by the company secretary and his team. It was based on the completion of questionnaires (including questions to be scored and free text questions) by board members assessing both the performance of

the board and of each of its principal committees, and that of the Chairman and each of the individual non-executive directors. Board members were also asked to provide a view on how well the actions identified in the 2015/16 evaluation had been addressed.

In addition to board members, other members of the executive team who regularly attend and support the various committee meetings were asked to complete the same questionnaires where applicable.

The results, once reviewed by the company secretary, were then discussed with the Chairman and the chair of the relevant committee; tabled at a meeting of the relevant committee; and then presented to the board. The Chairman reviewed the performance of the individual directors. Mark Clare, as the senior independent director, in discussion with the other non-executive directors, led the review of the Chairman’s performance.

A summary of the analysis of the 2016/17 evaluation is as follows:

2016/17 areas of assessment	Commentary and actions
Board composition and expertise	Board members' skills and expertise were felt to be appropriate and the board was felt to be balanced in terms of composition. Board meetings were conducted in an atmosphere where open communication was encouraged to facilitate the proper resolution of issues.
Board agenda	The board was well informed about the regulatory environment the company operates within and had a good understanding of the views of investors, but would benefit from more opportunities to gain a better understanding of the views of customers and on service delivery and technical innovations for customers.
Board support	The timeliness of the distribution of board documentation was appropriate. A number of suggestions were made to the content, format and length of papers, and board time was being better used in discussion of the issues rather than merely receiving presentations. The support and training needs of board members continued to be addressed and there was considerable support amongst board members for directors individually to pursue opportunities to get a closer view of aspects of the business of particular interest to them.
Wider strategic oversight	The involvement of the board in the development of the strategic direction of the group was considered to be appropriate and the format and content of the board strategy away day held during the year was felt to have improved, but more time should be allowed for key strategic topics.
Risk management and internal control	The board's approach to the management of risk and to its systems of internal control were considered to be appropriate. The information received relating to risk management, in particular operational and reputational risks, was much improved.
Succession planning and human resource management	Board members felt that the senior management structure and succession planning for executive and key management positions supported the strategic objectives. The succession plans and board succession planning matrix for the appointments to the board and senior management had been developed and had gained a greater level of detail, particularly in relation to developing more granularity on timescales for key board positions. There had been improvements to the visibility of potential internal candidates for succession to the executive team and to their direct reports.
Committees	<p>The composition and performance of the audit, remuneration, nomination, corporate responsibility and treasury committees were considered to be appropriate, and the feedback from committee meetings by committee chairs was full and transparent and meetings chaired effectively. Specific actions identified were as follows:</p> <p>Nomination committee: ensure the focus on senior board succession was maintained over the next 12 months, but also ensure that there was thought given to the skills needed around the board over the next five years;</p> <p>Remuneration committee: to consider the timetable for the review of the committee's external advisers;</p> <p>Audit committee: continue the progress made during the year on making papers more concise; and</p> <p>Corporate responsibility committee: increase the committee's engagement with customer priorities.</p>
Individual directors	The individual performance of the directors was assessed, all of which were considered to be independent and effective, and all directors demonstrated the expected level of commitment to the role. The review of the Chairman's performance (led by the senior independent director) concluded he continued to demonstrate an effective and independent perspective, fulfil the expected commitment to the role and was an effective leader of the board. All directors would be offering themselves for reappointment/election at the 2017 AGM.

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2015/16 evaluation recommendations	Actions taken during 2016/17
Strengthen the board with additional skills/experience from an engineering/industrial background.	Alison Goligher was appointed on 1 August 2016 (see page 53).
The board should allow time to consider the customer experience, and the key strategic issues of market reform and competition in the sector.	The board received a paper and presentation on the customer experience programme along with updates on progress. Furthermore, regular updates were provided throughout the year on the group's progress and readiness for market reform and the opening of the industrial market to competition on 1 April 2017.
Continued focus on improvements to keeping board papers concise.	Content, format and length of board papers had improved but the focus for continued improvement should be maintained.
Allow more time for the discussion of key strategic topics at the board strategy away day.	Improvements had been made to the timetable for the board strategy away day to allow more time for discussion of the group's strategic priorities.
Nomination committee: develop a board succession planning matrix and gain an understanding of the granularity of timescales for succession planning.	The succession plans and board succession planning matrix for the appointments to the board and senior management had been developed and had gained a greater level of detail, particularly in relation to developing more granularity on timescales for key board positions.
Remuneration committee: ensure that succession planning activities and remuneration activities were aligned.	The remuneration committee considered succession planning during the nomination process for the Long Term Plan awards made in 2016. In the coming year, as the talent programme at the senior level progresses, the committee will further review the alignment of remuneration to the outcomes of the programme.
Audit committee: review the effectiveness of the assurance of risk management systems, particularly in relation to the oversight of the management of operational and reputational risk.	Regular updates have been provided to the audit committee (and the board) on the implementation of actions identified by Mark Clare, senior independent director, in his review of the 2015 Lancashire water quality incident.
Corporate responsibility committee: review the analysis of reputational risk to ensure alignment with the audit committee.	Changes have been made to risk reporting to improve the presentation of the reputational aspects of risks as appropriate and these are considered at both the audit committee and the corporate responsibility committee.

Board development

Board directors regularly receive updates to improve their understanding and knowledge about the business and in particular its regulatory environment. As part of the individual directors element of the board evaluation exercise (see page 63) directors are asked to identify any skills or knowledge gaps they would like to address.

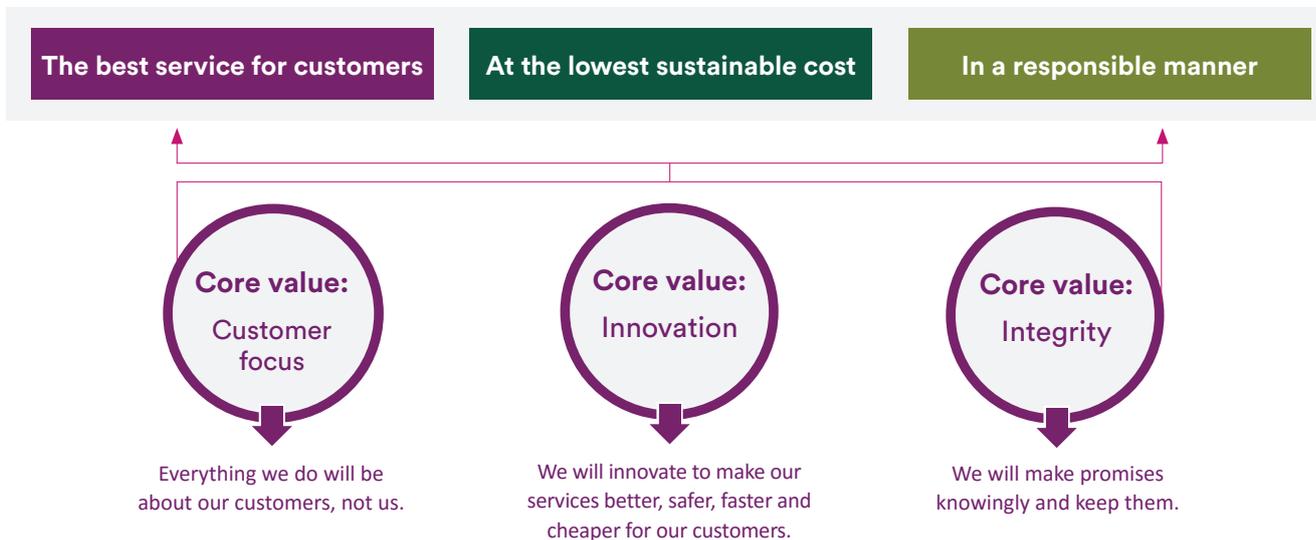
Consideration of environmental and social issues are fundamental to the way in which we operate as a responsible business at United Utilities; such matters are central to board discussions (see the summary of board activity on pages 60 to 61). The board's approach to these matters is reflected in our strategic objective of acting in a responsible manner, and information relating to this can be found throughout the strategic report. Board awareness of in-region environmental and social matters has also been raised during the year by the independent customer challenge group, known as 'YourVoice'. In addition to this less formal approach to board development, during the year the board also received briefings from both Slaughter and May (legal and governance matters) and KPMG (governance changes relating to the audit committee and audit reform) along with a number of other advisers.

Our non-executive directors are conscious of the need to keep themselves properly briefed and informed about current issues and to deepen their understanding of the business. During the year, Sara Weller visited both the Lingley Mere offices and the Water Plus offices in Stoke-on-Trent, to meet with management and discuss customer treatment, competition and capital programmes. She also attended sessions run by Ofwat and received independent remuneration briefings from external sources. Brian May spent a day at the group's Lingley Mere offices where he met with a number of members of the senior management team and had discussions relating to internal audit and risk management, progress with the customer experience, and in relation to Systems Thinking and our approach to the wholesale operations. He also met with our business development director and our IT director. Mark Clare also spent a day visiting the customer operations team based at Lingley Mere.

Following appointment each director will have an induction programme arranged for them in order to help them gain an understanding of the business and the key issues and to provide them with information that will help them to be effective and make a contribution to board debates. Details of Alison Goligher's induction are given on page 70.

Values and culture

The values identified by the board (see page 57) underpin our strategic objectives:



The United Utilities way of doing things is to act as a responsible business and is set out in our 'Business Principles' document. A copy can be found at:

corporate.unitedutilities.com/united-utilities-business-principles

In July 2016, the FRC published a report of its observations on 'Corporate Culture and the Role of Boards'. This report defined culture in a corporate context 'as a combination of the values, attitudes and behaviours manifested by a company in its operations and relations with its stakeholders. These stakeholders include shareholders, employees, customers, suppliers and the wider community and environment which are affected by a company's conduct.'

The board's aim is to lead by example and set the standard of behaviour we expect from our employees. By treating our board colleagues

with respect we aim to foster an environment of trust and one that is conducive to open and frank discussions. This approach is in the best interests of our business and all our stakeholders. Furthermore, culture in its various forms/guises is treated as business as usual. Cultural indicators such as customer service, employee matters and risk management form part of the board's regular discussions and further contribute towards our objective of acting responsibly (see the summary of board activity on pages 60 to 61). Our CEO is responsible for cascading our culture and behaviour of acting responsibly throughout the business and he is supported and facilitated in this by the executive and wider management team. As part of their role, we expect our employees to live the values of customer focus, integrity and innovation. More information can be found on our website at:

corporate.unitedutilities.com/cr-our-values

In the table below are examples of how we aim to act responsibly towards our different stakeholders:

How we act responsibly towards our customers	How we act responsibly towards our employees	How we act responsibly towards our other stakeholders (shareholders, environment, communities, and regulators)
<p>We offer 'Priority Services' that customers can register for if they require extra support due to such things as ill health, age related issues, disability, mental health problems, financial worries or language barriers. Our 'Moving Home' services are available to those moving house in our region. We are making improvements to our written communications with customers to make them easier to understand and remove technical jargon along with launching a new customer website and mobile app.</p>	<p>Our offering to employees includes: a competitive base salary; an employee benefits offering; family friendly policies that go beyond the statutory minimum; the opportunity to express their views about the company in the annual employee survey; an employee assistance support helpline; company paid healthcare and the opportunity to join our share incentive plan. Our whistleblowing helpline allows employees to raise any concerns they may have.</p>	<p>Our investor relations team provides a point of contact for investor queries; our sustainability team champions sustainability issues with the business; our stakeholder teams provide support in areas where we are undertaking major capital projects; our communications teams raise awareness and respond to press and media queries; our corporate affairs team provides information to public organisations; and our regulatory team is in constant communication with our various regulators.</p>

We have made significant progress in improving the customer experience and embedding a customer service orientated culture in recent years. On page 32 of the strategic report, details of the KPIs used to monitor customer service can be found. Our employee survey (see page 38 of the strategic report) shows employee engagement at 89 per cent. The management team is working hard to embed these values in our business. Furthermore, with the implementation of our Systems Thinking approach and improving the technology deployed across our asset base during the current regulatory period, we would expect to see further improvements in the standard and efficiency of our service to our customers.