TIDEWAY ANNUAL REPORT 2015/16

Tideway

RECONNECTING LONDON WITH THE RIVER THAMES

ANNUAL REPORT 2015/16

The Thames Tideway Tunnel will be a major new sewer, which is urgently needed to protect the tidal River Thames from pollution

Health, safety and the wellbeing of our people and the public are paramount – we intend to work safely or not at all

It is being delivered by Tideway, a newly created regulated company

We are working closely with our local stakeholders in delivering the tunnel

The tunnel is being financed by the private sector, giving more than 1.7 million UK pensioners an indirect investment in Tideway

We aim to deliver the project to the right quality, ahead of time and below budget, for the benefit of the environment, local stakeholders, Thames Water's bill payers, and investors

The tunnel is the largest project in the water sector since the construction of Sir Joseph Bazalgette's interceptor sewers in the 1860s

RECONNECTING LONDON, AND LONDONERS, WITH THE RIVER THAMES

Contents

Strategic Report

05 Chairman's Introduction
06 Chief Executive Officer's Statement
07 Key Developments in 2015/16
09 Who We Are and What We Do
16 Our Business Model
18 Our Vision and Strategy
22 Risk Management
26 Performance Review
32 Financial Performance Review

Governance

37 Corporate Governance Report
58 Audit Committee Report
64 Remuneration Report
72 Directors' Report
75 Long Term Viability Statement

Financial Statements

78 Independent Auditor's Report
80 Financial Statements
84 Notes to the Financial Statements

Regulatory Reporting

98 Introduction
98 Regulatory Annual Performance Report
110 Transfer Pricing Information
111 Risk and Compliance Statement
112 Condition K Reporting
113 Other Reporting Requirements
115 Data Assurance Summary
115 Auditor's Report
119 Glossary

Bazalgette Tunnel Limited (BTL) is the licensed Infrastructure Provider set up to design, build, commission and maintain the Thames Tideway Tunnel. BTL trades and is known to the public as 'Tideway'.

‘The River Thames is central to London’s prosperity’

Strategic Report

05 Chairman’s Introduction

06 Chief Executive Officer’s Statement

07 Key Developments in 2015/16

09 Who We Are and What We Do

16 Our Business Model

18 Our Vision and Strategy

22 Risk Management

26 Performance Review

32 Financial Performance Review

Jonothan Starkey, a Pimlico resident, has been helping Thames21 remove litter from the river since 2009. One of the charity’s most dedicated supporters, he can regularly be spotted venturing into the river in waders.

Strategic Report
Chairman's Introduction

SIR NEVILLE SIMMS
NON-EXECUTIVE CHAIRMAN

'The scheme benefits from a delivery model designed to encourage private-sector investors to finance major infrastructure'

In Great Britain we are indebted to the vision of our Victorian forebears, who laid the foundations of much of the public infrastructure we use today. This has served us extremely well, in many cases for decades longer than was originally intended, but now it must be upgraded both for our own use and to prepare it for future generations.

In that context one of the most urgent priorities, both for London and nationally, as recognised in the Government's 'Top 40 infrastructure investments', is to help address the regular pollution of the tidal River Thames with untreated sewage. To have an open sewer flowing through our capital city is simply unacceptable. A key part of the solution to this particular problem is the Thames Tideway Tunnel.

I am pleased to be part of the organisation brought together to ensure that this solution becomes a reality for the benefit of London and all users of the River Thames, for many years into the future.

Significant investment into major infrastructure projects is often best achieved by attracting private sector finance. The Thames Tideway Tunnel is the first scheme to benefit from a new delivery model, specifically designed to encourage pension funds and other long-term private sector investors to become involved in the financing of regulated water assets like ours.

It was therefore a great achievement by all those who had worked on the scheme for many years that in August 2015, when our licence was awarded by Ofwat, we became an independent, regulated water company – Bazalgette Tunnel Limited.

Bazalgette Tunnel Limited, trading as Tideway, is owned by a shareholder group comprised of funds managed by Allianz, Dalmore, Amber Infrastructure Group and DIF. Between them, more than 1.7m UK pensioners have an indirect investment in Tideway. The investor group is represented by four shareholder directors who sit on our Board, alongside five independent directors, including me, together with the three executive directors.

You will read more about the Board and its Committees elsewhere in this report, but I am sure you will be pleased that in the short time this Board has been together it has endorsed new plans to significantly improve the timetable for the delivery of the project.

To achieve these plans, the Board is delighted to have secured the services and commitment of a first class team of executives, to lead both the financing and construction activities and to rise to the challenge of doing this safely and efficiently, in alliance with our contractors and other partners.

Sir Neville Simms,
Chairman

Chief Executive Officer's Report

ANDY MITCHELL CBE,
CHIEF EXECUTIVE OFFICER

'We see the River Thames as a hugely important, and in many ways forgotten, asset for our capital city'

It is a great privilege to be the CEO of Tideway, charged with the establishment of a company to deliver the much needed expansion of Sir Joseph Bazalgette's London interceptor sewers. In doing so, we will clean the Thames to a level unlikely to have existed for more than a century. Hot on the heels of London's Lee Tunnel, Crossrail and National Grid cable tunnels, there never has been a better time to undertake this scheme and it is very encouraging to see so many top class, experienced professionals at all levels of the supply chain.

There is no doubt that this will be a vital asset for our capital city. There is however nothing that we will do that will be as important as the health, safety and wellbeing of all the people working for us or who are affected by us, be that on our sites, on the river, or in the areas of London in which we work. We intend to set new standards through our transformational health, safety and wellbeing programme, some details of which you will see in this report.

The team has done a tremendous job over a number of years, successfully securing planning approval and establishing a robust plan and budget, which culminated in the granting of the licence to Tideway to operate as an independent regulated water company in August 2015. The same day, we awarded the main works contracts and we have worked hard since, as we brought a new company into existence, to develop the design and construction thinking to deliver the best result possible for the environment, people living close to our construction sites, bill payers and investors alike. Through the Alliance framework that includes our main contractors, Thames Water and us, we have established a plan to de-risk the programme, with the aim of completing handover to Thames Water (tests completed and handover criteria met) earlier than the baseline date in 2024. The benefits of striving for this are clear - for our neighbours (as we know that our works will be a distraction and the sooner we finish the better), for bill payers and investors (the less time we take, the lower the overall cost), and for the environmental and economic health of the river and London generally.

The River Thames is a hugely important, and in many ways forgotten, asset for our capital city. Usage of the river has increased significantly in the last decade, but compared to many other capital city rivers the Thames remains underutilised and underappreciated. By our commitment to move as much of our material by river as we can (significantly increasing the freight usage of the river) and by supporting the Port of London Authority's (PLA) establishment of the Thames Skills Academy to train a new generation of over 300 skilled and qualified river workers, we intend to demonstrate how valuable the river can be to commerce and transport in London. This will result in less traffic on London's roads, benefiting the environment and reducing the risk of road-based incidents. By removing the sewage overflows into the river, we intend to change the common perception of a dirty river into one where Londoners and visitors see the Thames as a joy to be near and on.

Our challenge is to build a tunnel to remove the sewage from the river, and our vision is 'Reconnecting London, and Londoners, with the River Thames'. Our shareholders have demonstrated their confidence in Tideway by committing their financing of some £1.3bn. We have made further progress in securing the finance for our long-term investment programme, with a Revolving Credit Facility (RCF) of £1bn in place, and since year end we have agreed terms for a £700m European Investment Bank (EIB) loan and bond issues totalling £350m.

I strongly believe that the people delivering infrastructure for society will do a better job if they are representative of that society. Through our Encompass diversity programme we are striving to achieve this in all areas. If the past year was focused on setting the company and the scheme up for success, the coming year will be the first and most influential one in enabling the safest and earliest delivery. Through the unarguable strength, experience and commitment of the team, I am confident that Tideway is set to have a successful year.

Andy Mitchell CBE,
Chief Executive Officer

£1.3bn

THE EQUITY SUM COMMITTED BY THE COMPANY SHAREHOLDERS

KEY DEVELOPMENTS IN 2015/16

- **Established the largest newly formed independent regulated water company since the industry's privatisation and secured £2.3bn of capital.** Licence awarded by Ofwat in August 2015.
- **Established a clear vision and values, reflecting the legacy we aim to leave for London –** 'Reconnecting London, and Londoners, with the River Thames'.
- **Established our transformational health, safety and wellbeing programme.** No injuries or lost time incidents in 2015/16. Industry recognition for our Employee Project Induction Centre programme – innovative training designed to ensure we work safely, with over 2,500 people attending.
- **Formed the Tideway Alliance and started delivery.** Incentive framework established for all delivery partners to work together collaboratively. Started work in West, Central and East areas, with the delivery schedule on track.
- **Had our first Revenue Statement submission accepted by Ofwat.** First payment on its way from Thames Water's wastewater customers.
- **Community Liaison Working Groups launched.** Actively developing relationships with our neighbours – more than 20 meetings held across the West, Central and East areas.
- **Financing locked-in after year end.** Secured a £700m EIB loan and bond issues totalling £350m. *(Picture: Marking agreement of the loan with EIB)*

Who We Are and What We Do

A newly formed independent regulated water company, financed by private capital, established to intercept sewage otherwise destined for the tidal River Thames

‘A sewerage system that is able to meet its needs has been the backbone of London’s success over many decades’

Above: Andy Mitchell with the Doggett’s Men at Fishmongers’ Hall

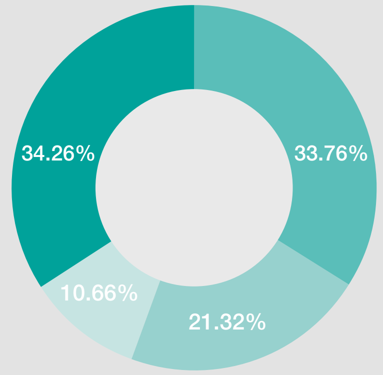
Left: The Lee Tunnel was completed by Thames Water in early 2016

Bazalgette Tunnel Limited, trading under the name of Tideway, began operating as an independent regulated water company when, in August 2015, Ofwat awarded us our licence to design, build, commission and maintain the Thames Tideway Tunnel. The 25km tunnel beneath London, which has been dubbed the ‘super sewer’, will store and transfer tens of millions of tonnes of untreated sewage each year that currently pollutes the tidal River Thames.

British money is helping to deliver this vital piece of infrastructure, which is fundamental to London’s success. The tunnel is being financed by the private sector, giving more than 1.7 million UK pensioners an indirect investment in Tideway, through pension funds managed by our investors.

At licence award, our shareholders committed total financing of £1,274m. This backing helps fulfil a key component of HM Treasury's National Infrastructure Plan, to finance the development of UK infrastructure with the support of private investors. Our shareholder group has extensive experience of investing in and managing a wide range of infrastructure assets in the UK and overseas. ›

The shareholder group comprises:



- Allianz
- Dalmore Capital Limited
- INPP & Swiss Life (managed and advised by Amber Infrastructure)
- DIF

The shareholders are represented on our Board, with one director each for Allianz, the Amber group, Dalmore and DIF. More information can be found in the Corporate Governance section of this report, on pages 54 to 55

Who We Are and What We Do
Continued

Did you know Sir Joseph Bazalgette's brick sewers are made up of 318 million bricks all laid by hand?

LONDON TIDEWAY IMPROVEMENTS PROGRAMME

The network of sewers built by Sir Joseph Bazalgette in the 1860s still forms the backbone of London's sewerage system. Constructed when London's population was two million and designed to cope with four million, the system now struggles to serve a city of more than eight million people.

London's current sewerage system includes 57 combined sewer overflows (CSOs), designed to allow the release of excess sewage flows into the River Thames during heavy storms. In Victorian times, this happened once or twice a year. The current lack of capacity means that the network is regularly overwhelmed, resulting in discharges in recent years averaging (based on a typical year) once a week and around 39 million cubic metres of sewage per year entering the tidal section of the Thames.

An independent study, which concluded in 2006, assessed the environmental impact of these discharges and proposed the London Tideway Improvements Programme. This has three main components:

- upgrades to the five sewage treatment works that discharge to the tidal River Thames, which were completed by Thames Water in 2015;
- construction of the Lee Tunnel, which runs from Abbey Mills Pumping Station to Beckton sewage treatment works, and was completed by Thames Water in early 2016; and
- construction of the larger Thames Tideway Tunnel, which will connect to the Lee Tunnel.

Thames Water is responsible for developing the Thames Tideway Tunnel, acquiring land, and enabling / interface activities.

25
kilometres long

Travelling from west to east London, the main tunnel will be 25km long. Two connection tunnels will be 4.6km and 1.1km long.

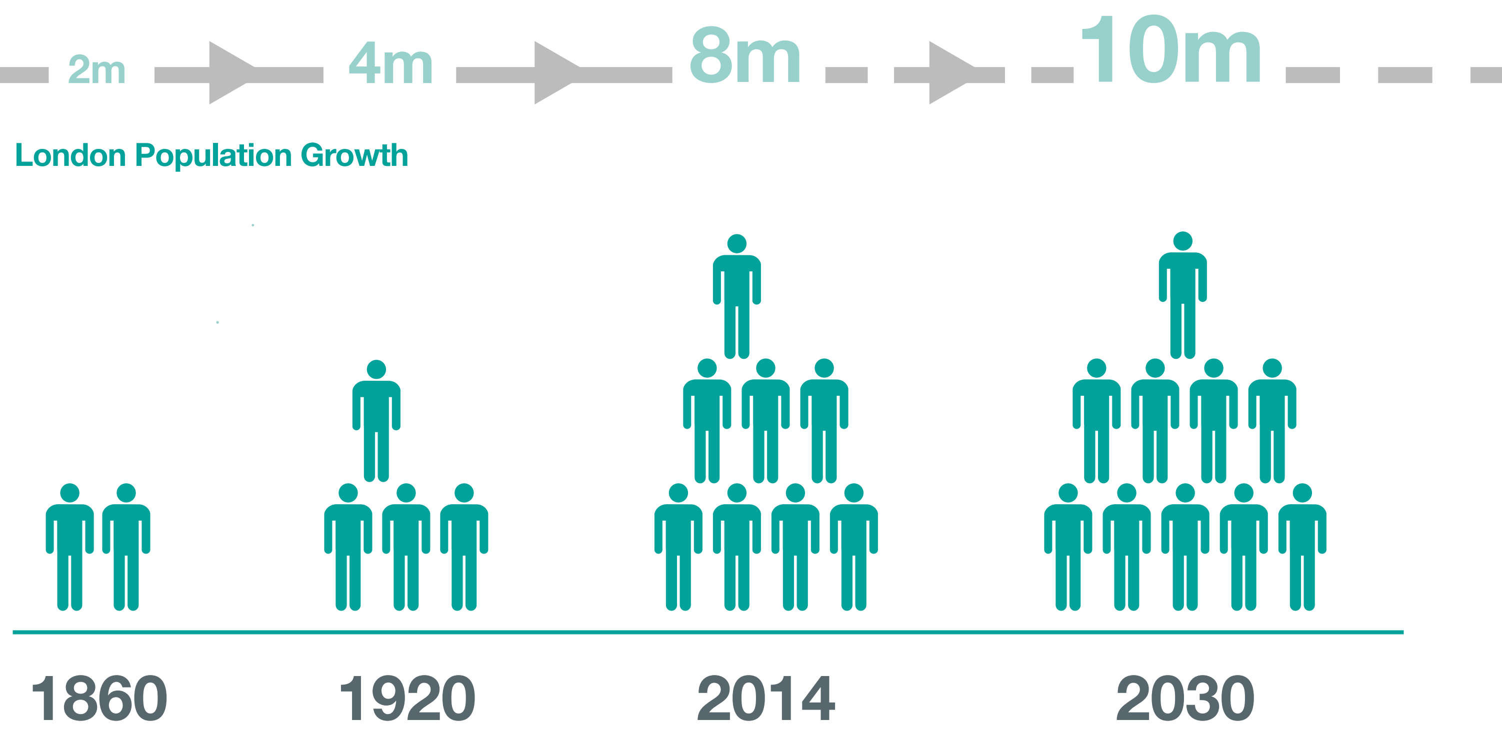
7.2
metres wide

The main tunnel will have an internal diameter of 6.5 metres between Acton Storm Tanks and Carnwath Road Riverside. It will have a 7.2 metre internal diameter at Abbey Mills Pumping Station. The Greenwich connection tunnel will have a 5 metre internal diameter and Frogmore connection tunnel will be 2.6 metres.

66
metres deep

The tunnel needs to fall one metre every 790 metres so it can be self-cleaning. Starting from 30 metres deep at Acton Storm Tanks, it will finish 66 metres deep at Abbey Mills Pumping Station.

London Population Growth



The total estimated cost is £4.2bn. Ofwat has set a regulatory baseline of £3.1bn for Tideway's element of the programme (in 2014/15 prices), with the rest delivered by Thames Water. The impact on Thames Water customers' annual bills is estimated to be around £20-25 per household, before inflation, by the mid-2020s, considerably lower than the £70-80 per household originally estimated.

THE ROUTE

The majority of the tunnel, which runs from the Acton Storm Tanks in West London to the Lee Tunnel at Abbey Mills in East London, will be under the River Thames. The flow from over 30 CSOs will be diverted from the existing sewerage network into the main tunnel, where it will continue to flow by gravity to the Lee Tunnel connection. From there it will run through the Lee Tunnel to the Tideway Pumping Station, to be pumped to Beckton Sewage Treatment Works. The tunnel's design will make it self-cleansing and minimise ongoing operational and maintenance requirements during its expected life of at least 120 years.

The construction of the tunnel will require works to drive the tunnel using tunnel-boring machines and to intercept ›

1.24m
cubic metres capacity

The tunnel will be able to store 1.24m cubic metres of sewage for transfer to treatment. That is the equivalent of 50 Olympic-sized swimming pools.

120
years design life

The design of the tunnel will mean it will last for at least the next 120 years.

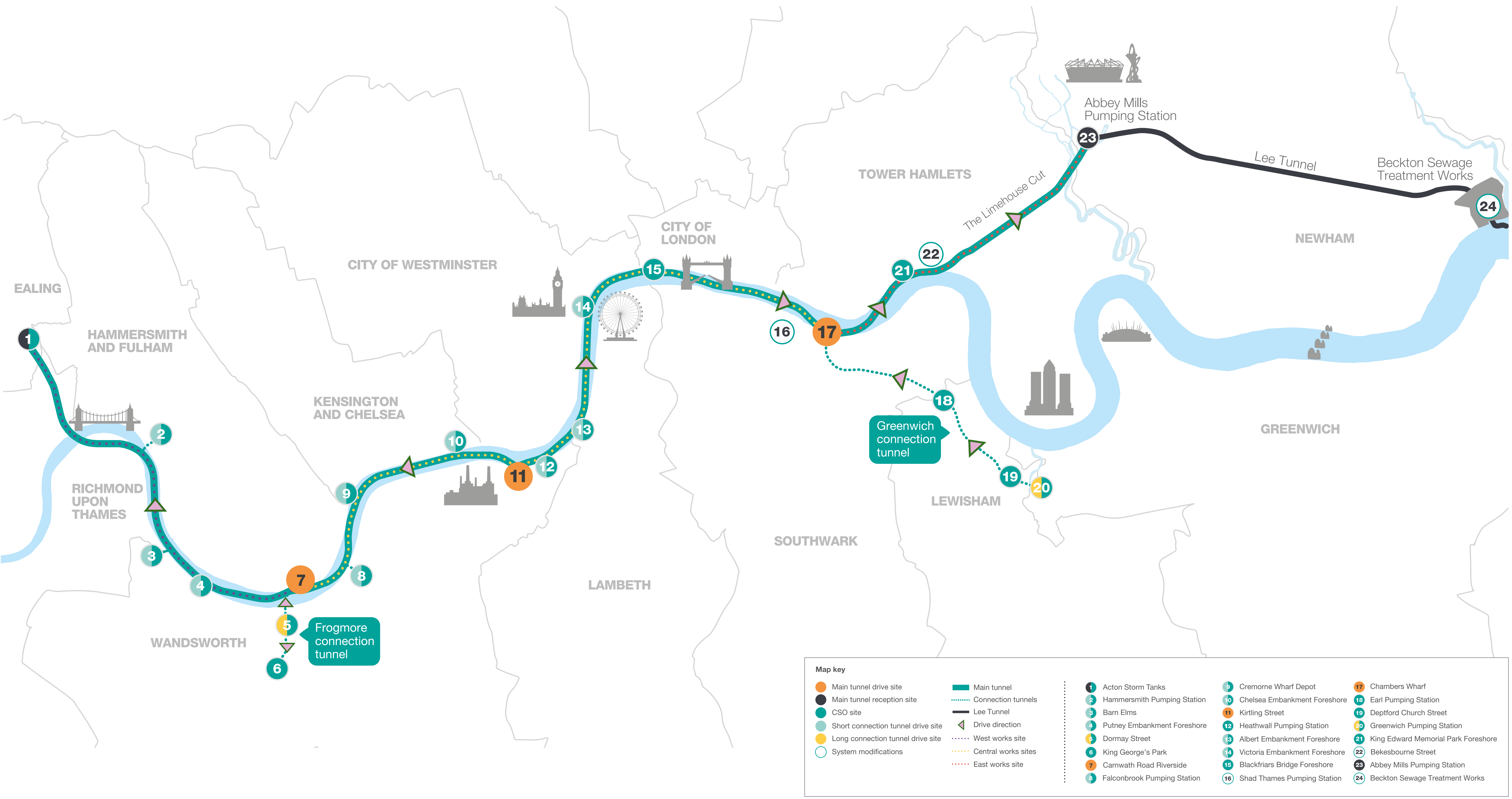
24
construction sites

Of the 24 sites, 11 are on the foreshore of the river. Sixteen sites intercept one or more CSOs, and there are five sites dedicated to the construction of the connection tunnels.

Who We Are and What We Do

Thames Tideway Tunnel

The tunnel generally follows the River Thames from Acton to Limehouse, then continues north-east to Abbey Mills Pumping Station where it will connect to the Lee Tunnel



Work progressing at the Kirtling Street site in Battersea. Opposite: The River Thames

› the CSOs and connect them to the main tunnel. The main tunnel construction will take place in four drives from shafts at three main tunnel drive sites, with two additional connection tunnel-drive sites. The main drive sites are located in Fulham in the West, Battersea in the Central section and Bermondsey in the East.

TIMELINE FOR DELIVERY

Following licence award, we agreed a baseline schedule with our works contractors. The expected timeline for the delivery of the tunnel is detailed below.

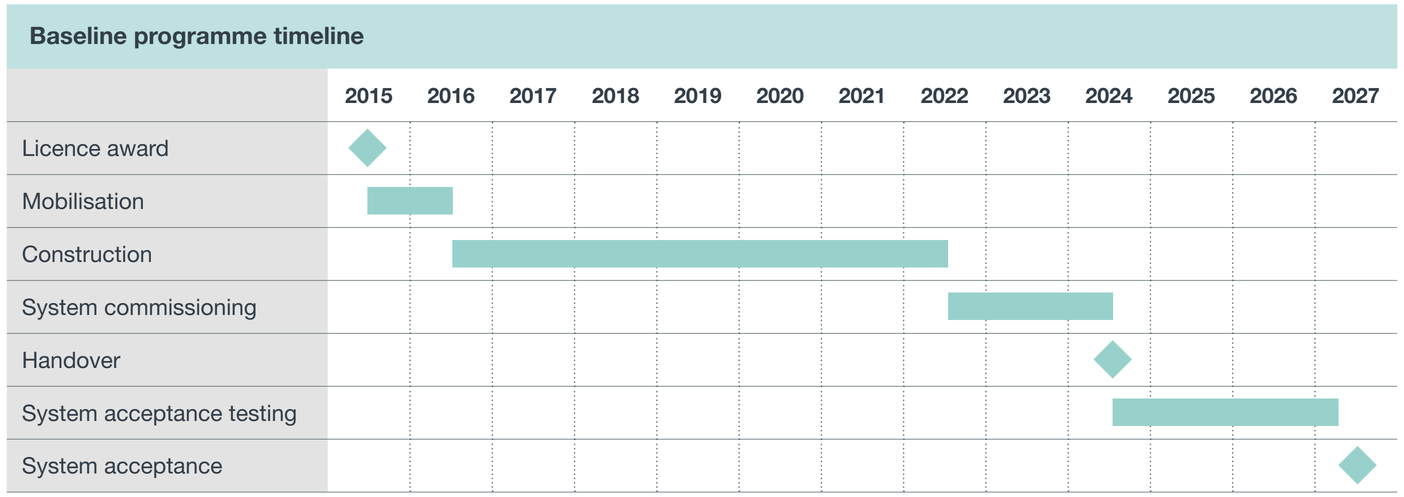
Work has started at the key drive sites ahead of schedule, with construction scheduled to complete in 2022. Our aim is to reduce risk in the construction phase and shorten the time to construction completion. Once construction has completed, a period of commissioning will take place to ensure that the tunnel is integrated effectively into the wider sewer network. When the system commissioning tests have been completed and the handover criteria met, Thames Water will conduct system acceptance tests to ensure that operations are optimised.

DELIVERING FOR OUR STAKEHOLDERS – OUR LEGACY FOR LONDON

We are committed to maximising the long-term benefits we create for all our stakeholders and to delivering a lasting legacy for London, with the ambition of delivering the Thames Tideway Tunnel as early and as safely as possible. Finishing earlier would reduce cost, benefiting both bill payers and investors, and deliver environmental benefits earlier.

Over the coming years, Tideway aims to transform how many things are done in the industry. Starting with health, safety and wellbeing, we intend to treat people differently from the very beginning, seeking much higher levels of engagement and commitment to doing things better and safer. We want to see a step change in the health and wellbeing of everyone working on the project, with people leaving healthier than when they started.

We have an aspiration for a diverse and inclusive workforce, attracting young people into the construction industry, particularly women. With an engaging programme for apprentices, Tideway is also helping to fill the skills gap, benefiting our delivery programme and future projects in London. Another key commitment is to use the River Thames, wherever possible, to transport materials in and out of our construction sites, including most of the tunnel's spoil and tunnel materials. This offers less disruption for Londoners, the environmental benefit of a lower carbon footprint and the safety benefit of fewer vehicles on London's roads.



Business Model

Tideway's business has two distinct phases: the construction period, leading up to Thames Water's acceptance of the Thames Tideway Tunnel (system acceptance), and the operational period thereafter

PREPARATION WORK AT BLACKFRIARS BRIDGE FORESHORE

'Following system acceptance, we will transfer to Thames Water the above-ground assets, structures and equipment we have constructed'

The construction period

Our key activities during the construction period are:

- overall programme management, including overseeing the main works contractors;
- engaging with our stakeholders to gain support for and minimise delays to construction;
- working alongside Thames Water to synchronise our construction work with the Thames Water Works (which are enabling and other works required to connect the tunnel to the sewer network) and to ensure the Thames Tideway Tunnel is effectively integrated into the sewerage network;
- developing a system control philosophy and supervisory control and data system that supports the integration with the existing sewer network; and
- managing the commissioning, handover and acceptance testing of the completed Thames Tideway Tunnel.

Our delivery partners

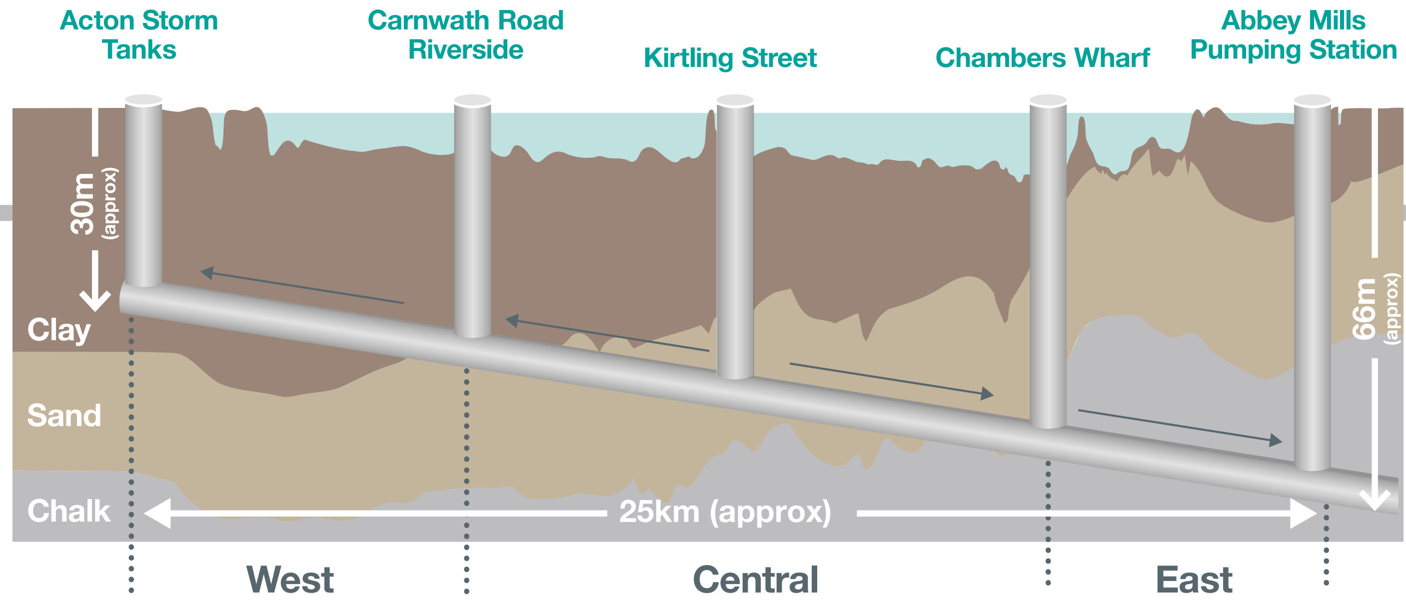
To construct the Thames Tideway Tunnel as efficiently as possible, we have entered into three main works contracts, a systems integration contract and a project management contract. The main works contracts and the respective contractors are summarised on page 17. Our contractors were selected through a comprehensive procurement programme prior to Tideway's creation. Each consortium will construct a specific section of the tunnel and includes contractors with valuable experience of recent major construction projects in London, such as the Lee Tunnel, Crossrail, the National Grid cable tunnels and the 2012 Olympics. Dividing the tunnel construction into three contracts, led by three different consortia, spreads delivery risks and enables us to benefit from the combined expertise of the most experienced construction contractors.

The contracts transfer certain key risks to the contractors, including design, discharge of consents and ground conditions identified before contract award. Each main works contract provides for cost reimbursement (costs incurred and a fee), as well as a gain/pain share mechanism against the target price.

We have also created an overarching Alliance, governed by an Alliance Agreement between us, Thames Water, the main works contractors and the system integrator. The Alliance Agreement provides for the establishment of an incentive framework, which will align all parties around the construction programme's aims and outcomes, including the key milestones and the objective of meeting overall cost, driving everyone to manage costs and risks in an integrated way. This will help us to manage and incentivise collaborative behaviour, so we realise economies of scale, synergies between activities and share best practice.

In addition to the main works contractors, we have a number of other partners who are key to delivering the tunnel:

- Amey OWR Ltd is the system integrator and is responsible for providing process control, communication equipment, and software systems for operation, maintenance and reporting across the London Tideway Tunnel (comprising of the Thames Tideway Tunnel and Lee Tunnel).
- CH2M is providing programme management support during the construction period. This gives us continuity in our programme team, with CH2M having undertaken the design management, development and delivery of the Thames Tideway Tunnel since 2008.
- Thames Water is designing, building and commissioning enabling works and other works that are needed to connect the Thames Tideway Tunnel to the sewer network.



The operational period

Following system acceptance, we will transfer to Thames Water the above-ground assets, structures and equipment we have constructed. The deep tunnels and shafts and other related non-mechanical assets will remain under our ownership.

During the operational period, we are responsible for ensuring the Thames Tideway Tunnel is available to allow flow to pass through into the Lee Tunnel. This involves inspecting the deep tunnels and shafts, which we expect to do on a ten-yearly cycle, and performing any maintenance required as a result of the inspections.

Regulatory oversight

Tideway is a newly formed independent regulated water company, with a new delivery model designed to attract private sector capital to finance infrastructure. This will enable us to finance our functions, earn a reasonable return on our investors' capital and maintain an investment grade credit rating. Our bespoke regulatory framework provides a revenue stream in both the construction and operational period. We received our first revenue in April 2016. Revenues are billed and collected on our behalf by Thames Water from its wastewater customers. The Secretary of State for Environment, Food and Rural Affairs, through the Government Support Package (GSP), has committed to provide contingent financial support while the Thames Tideway Tunnel is being built. Such support is available in exceptional circumstances only and mitigates certain risks which may arise during the construction period. This package provides strong mitigation for highly unlikely specific risks, such as extreme cost overruns, Tideway suffering a loss that exceeds the limit of our insurance policies, or our inability to issue debt due to disruption in the capital markets. The GSP ceases to apply on system acceptance.

For the period until 2030, revenues are calculated according to the framework set out in our licence. From 2030, we expect to be regulated in line with the rest of the water industry, with price control reviews every five years.

As with other water companies we publish an annual performance report in line with Ofwat guidelines. Our regulatory annual performance report can be found on pages 98 to 118. Due to the specific legal, commercial and regulatory arrangements for the company and the GSP, we engage regularly throughout the year with both Ofwat and the Government.

Contract	Contractors	Contract value (£m)
West	**BMB JV:** Bam Nuttall Ltd, Morgan Sindall Plc, Balfour Beatty Group Ltd	£416m
Central	**FLO JV:** Ferrovial Agroman UK Ltd, Laing O'Rourke Construction Ltd	£746m
East	**CVB JV:** Costain Ltd, Vinci Construction Grands Projets, Bachy Soletanche Ltd	£605m

Our Vision and Strategy

Our Vision

Our vision is reconnecting London, and Londoners, with the River Thames

'Achieving our vision requires us not only to protect the river from pollution, but to work in the right way'

Vision
Aim
Company Objectives

An artist's impression of the tunnel underground at Victoria Embankment Foreshore

Tideway's business is to design, build, commission and maintain the Thames Tideway Tunnel, to leave our capital city's river cleaner than it has been for over a hundred years. This alone could be a sufficient ambition for the Company but we see what we are doing in a broader way.

A number of factors have influenced our thinking. London is located where it is because of the River Thames and its use for shipping and commerce, as well as for personal transport, leisure and drinking water. The Thames has seen cycles of pollution and cleansing through increased population and industrialisation. In the 1950s, the river was declared biologically dead. As industrial pollution diminished, sewage pollution has increased. London turned its back to the river, breaking the once vital link between Londoners and the Thames. In a city whose roads are getting busier every year, wherever possible we will use the river to transport our materials. We estimate that we will treble freight usage of the river, creating the need to train around 300 new workers. When we have finished, we will have demonstrated the river's capacity to support time-critical, 24/7, high-volume logistics throughout the centre of London. This capability is a valuable resource to be re-appreciated by London. It will bring environmental benefits from a lower carbon footprint and safety benefits with fewer vehicles on London's roads. Equally, when the Thames Tideway Tunnel is commissioned and the health of the river is restored, Londoners will be able to reconsider the river's leisure value, whether that is water sports, pursuits on the foreshore, fishing, or simply the enjoyment of being near a clean and healthy watercourse. For these reasons, seeing the Thames Tideway Tunnel as simply a mechanical endeavour would be a huge lost opportunity. While our challenge is to build a tunnel and hence intercept sewage from reaching the river, our vision is to regain something that has been lost – 'Reconnecting London, and Londoners, with the River Thames'.

OUR VALUES AND BEHAVIOURS

We understand the significance of what we are doing and are proud of its importance for London's future health and prosperity. We are also very clear that we will not achieve it at any cost. First and foremost is the safety of those employed through us and of the public we work amongst. We intend to do things safely or not at all. Surveys confirm that most Londoners, including our neighbours, support what we are doing, but we recognise that we will be a distraction for our neighbours and those we come in contact with. We want to develop our relationships with our stakeholders and recognise that we will be more effective and efficient when we treat everyone with respect, empathy and integrity – treating people as we would like to be treated. We understand the need to be clear in our intentions and communications, and to respect our environment. We are inspired by what we are doing and we hope to inspire others by what we do, how we do it and the potential for London that we will unlock.

Our Vision and Strategy

Our Strategy

Through our rigorous business planning process, we have developed a strategy to deliver our objectives. This section describes our strategy in more detail

Five company objectives, long-term key activities & 2016/17 priorities

Our long-term objectives are described under five key headings:

- Health, safety and wellbeing
- Company and people
- Schedule, cost and quality
- Financing
- Vision, legacy and reputation

Health, Safety & Wellbeing

Objective:

We are targeting zero fatalities or serious injuries, off-site or on-site. We will achieve this by setting new standards for health, safety and wellbeing (HSW). This is the right thing to do for those involved, as well as improving productivity and reducing the chance of delays or stoppages.

Our key activities include:

- Implementing a transformational HSW programme.
- Delivering 'Right Way', our HSW strategy and approach, in line with the delivery programme.
- Providing river training, through the newly established Thames Skills Academy.

Our priorities for next year are to:

- Establish a 'Right Start' programme, which aims to reduce the number of incidents in the first six months on-site, when accidents typically occur.
- Continuing and developing our Employee Project Induction Centre programme, which is mandated for all people working on our sites.

Company & People

Objective:

A high-performing, motivated and engaged workforce will deliver better value and help us recruit and retain people.

Our key activities include:

- Implementing our 'Encompass' diversity programme.
- Providing training and development, and succession planning.
- Offering competitive terms and conditions, benefits and incentives.

Our priorities for next year are to:

- Support employee engagement by rewarding our people appropriately, recognising good performance and giving them the chance to develop their skills.
- Improve employee effectiveness by empowering our people to make decisions, while ensuring accountability for delivery within a strong governance framework.

Schedule Cost & Quality

Objective:

We want to deliver the Thames Tideway Tunnel safely and at the earliest time. Finishing earlier will reduce cost, benefiting bill payers and investors, and deliver environmental benefits more quickly.

Our key activities include:

- Implementing our Alliance Agreement, incentivising all our delivery partners to work together to deliver more quickly and at lower cost.
- Maintaining our focus on delivering a high-quality, fit for purpose asset and its integration into the wider sewer network.

Our priorities for next year are to:

- Make progress against our construction schedule to de-risk the programme, by beginning drop shaft construction at the three main drive sites.
- Agree the interface with Thames Water on the Counters Creek sewer flooding alleviation plan.

Financing

Objective:

We aim to deliver efficient financing and financial risk management, which minimises our cost of capital and supports our investment grade credit rating.

Our key activities include:

- Maintaining a low risk financing position by preserving our Baa1/BBB+ credit ratings.
- Maintaining at least 18 months of liquidity.
- Investing the funds committed by our shareholders ahead of any external debt.
- Maximising the proportion of index-linked debt, to minimise cash interest costs and match Tideway's financing profile to growth in its Regulatory Capital Value.

Our priorities for next year are to:

- Position ourselves to access the debt markets, to benefit from the current low interest rate environment.
- Agree terms on the £700m EIB loan (completed May 2016) and progress on the bond financing programme (June 2016 priced bond issues totalling £350m).

Vision, Legacy & Reputation

Objective:

We want to create a supportive environment for delivering the tunnel and build a positive reputation with our stakeholders. Looking after our neighbours and stakeholders reduces the scope for delays, so we can deliver the tunnel's benefits as soon as possible.

Our key activities include:

- Working closely with the consent granting bodies.
- Understanding how best to address the needs and concerns of our neighbours.
- Delivering on our legacy plan.

Our priorities for next year are to:

- Secure the consents necessary to support our earlier programme ambitions.
- Commence the programme for local employment and apprenticeships.
- Agree a 'more by river' plan that maximises benefits to the local communities at our key sites.
- Establish a robust river skills training programme.

Risk Management

OUR RISK MANAGEMENT FRAMEWORK

Risk management is embedded in our culture and is central to achieving our objectives and priorities. We have developed and implemented a framework which provides a clearly defined process for identifying, analysing and controlling risks throughout the business. We consider both corporate and project delivery risks. Our approach includes actively monitoring risks, which are maintained on a comprehensive risk management database. This database, called Active Risk Manager, includes quantifications for project risks in terms of both cost and schedule impact and allows us to monitor the effectiveness of our mitigating actions.

The following table sets out our principal risks, which could have a material adverse impact on our business, reputation and/or financial condition. Each principal risk is owned and managed by a named senior executive and is reviewed on a quarterly basis by the Executive Risk Committee. Our process includes a bi-annual review of the principal risks and the risk management process by the Board Risk Committee, which reports to the Board on its reviews. The Executive Risk Committee also considers on a rolling basis the risks for each of the West, Central and East areas and the different categories of corporate risks.

Risk	Effect	Mitigations
Health, Safety & Wellbeing The health, safety and wellbeing of our employees and the public is paramount. There is a risk that incidents could cause harm to individuals and delay progress.	A safety failure could cause injury, or loss of life. A single serious event or multiple events could also lead to delays or stoppages that could prevent time and cost targets from being met.	We are implementing our 'Right Way' programme, including the 'Right Start' approach to establishing the very best facilities and arrangements on-site. We are also continuing and developing our Employee Project Induction Centre programme, which is mandated for all people working on our sites.
Programme Delivery We are delivering a capital investment programme of £3.1bn (2014/15 prices). While there is experience of delivering similar projects in London, it is possible that the construction could take longer than planned and/or cost more.	A delay in delivering the tunnel would delay Londoners' benefits from the project and could attract regulatory enforcement. Cost increases above the regulatory baseline would increase charges to Thames Water's customers, increase financing requirements and reduce returns for our investors.	Our approach to selecting and working with our contractors will help us to deliver the programme on time and to budget. This includes: • world class contractors, with experience of tunnelling in London; • contracts that transfer certain risks to our contractors that they are better placed to manage; • establishment of the Alliance, to encourage co-operation and support across the project (see page 16 for more details); • the intent to pursue an earlier schedule; and • an integrated, proactive approach to risk management.
Supply Chain Failure Our delivery strategy is based on outsourcing works. Our ability to deliver therefore depends on our contractors' performance. Our contractors operate in a very competitive environment and may experience financial difficulties through the delivery of the project.	If our contractors do not deliver at the standards we expect, we may not be able to deliver our investment programme on time and on budget.	The procurement process ensured our contractors were technically excellent and financially strong, and limited our exposure to any one contractor. The contracts contain step-in rights, whereby one contractor could replace another, which would help mitigate against financial failure. All three consortia are joint and severally liable.
High impact, low probability events Major investment programmes are complex and challenging, and we could suffer incidents that were highly unlikely but have a significant impact. These could affect the tunnel or assets belonging to others.	These events could have a significant effect on cost, schedule, health and safety, or our reputation. Their financial impact could exceed our insurance cover, damaging our financial position and our ability to deliver the tunnel.	We minimise the chance of these events occurring by using best in class design, programme planning and appropriate construction techniques. Our contractors have extensive experience of similar projects in London and we mandate compliance with the Joint Code of Practice for Risk Management of Tunnelling Works in the UK. Tideway is a member of the industry-wide Tunnel Boring Machine and Concrete Lining (SCL) working groups. In the unlikely event that we make a claim that exceeds the limits of our insurance, the GSP provides support.
Financial risks **Liquidity risk** We need to raise significant financing for our investment programme over the construction period. This could be affected by company specific, sector specific or general market factors impacting on the cost-effective availability of credit. The company notes the results of the recent referendum on the UK's membership of the European Union. The company will continue to monitor events and any possible impact on the business.	Failure to raise financing would impact on our ability to meet our cash flow requirements as and when they fall due.	Tideway enjoys a strong liquidity position, with committed shareholder funds, £1.7bn in undrawn loan facilities and bond issues totalling £350m. Our investment grade credit ratings facilitate efficient access to debt capital. Furthermore we have a £500m Market Disruption Facility available as part of the GSP.

Risk Management
continued

Risk	Effect	Mitigations
Interest rate risk Increases in interest rates would increase the cost of new borrowings and any existing floating rate debt.	Higher interest costs would adversely effect our cash flow and debt service.	Our treasury policy is to maintain a high proportion of our debt on a fixed and index-linked basis. Tideway will seek to pre-finance debt to reduce the exposure to increases in interest rates. The Financing Cost Adjustment in the regulatory revenue calculation provides partial protection against market movements in the cost of debt above certain thresholds.
Credit ratings Adverse operational or financial performance, or factors external to the company, could result in a credit rating downgrade.	The loss of an investment grade credit rating would impact our ability to raise debt.	We have a robust delivery model, within a regulated framework, and a Government Support Package. Maintaining or improving the timeline to deliver the tunnel will enhance confidence in our credit worthiness. We maintain a conservative financial profile and actively manage risks. We regularly engage with rating agencies.
Inflation risk There is a risk of inflation that is lower than assumed in our business plan.	Our revenues are directly linked to the Retail Price Index (RPI), and lower inflation would therefore reduce our cash flow unless our costs moved on the same basis. Our RCV is indexed to RPI until 2030, and lower inflation would reduce nominal cashflows and returns.	Tideway plans to issue a high proportion of RPI-indexed debt. Reductions in revenue due to low inflation will be partially offset by reductions in interest cost. The resulting correlation between nominal RCV and nominal debt will help to protect equity returns.

Risk	Effect	Mitigations
Reputational risk Poor performance on our sites, on the river or with our neighbours could damage our reputation and support.	The loss of support from our neighbours or consent granting bodies could lead to delays and higher costs.	We actively develop relationships with key stakeholders. For example, through our Community Liaison Working Groups we seek to find the best ways of addressing neighbours' concerns, in advance of works happening. The 'more-by-river' strategy will see us using the river wherever feasible to ease congestion and to promote the use of the river. We have established the Tideway brand, as part of our efforts to build trust and confidence and communicate the legacy and long-term benefits we aim to deliver.
Thames Water performance Thames Water is a key delivery partner for Tideway. In addition to the Revenue Agreement, we have a number of important interactions with Thames Water, including its delivery of the Thames Water Works during the construction period, the handover and acceptance process and in the operational period.	Thames Water's failure to deliver its share of the works could affect our ability to deliver our investment programme on time and on budget. If Thames Water does not comply with the Revenue Agreement for Tideway, it could have a financial impact.	The Thames Water team deployed on the project is co-located in our offices to encourage good communication and cooperation. The Alliance Agreement incentivises Thames Water to help us deliver the programme. Thames Water is also incentivised to deliver its share of the works in a timely manner, through its regulatory settlement. We have worked with Thames Water to develop and agree arrangements for managing the revenue process.
Regulatory risk We operate under a licence granted by Ofwat, which places restrictions and obligations on us. We need to ensure we comply with our licence at all times. Changes to the regulatory framework may affect our performance.	If we do not meet Ofwat's requirements, we could face enforcement which could include financial penalties and, in the worst case scenario, the loss of our licence. A revised regulatory framework could affect our financial performance and investors' returns.	Our licence sets out a specific framework for revenue until 2030. Ofwat's explanatory memorandum to our licence states that any modification of Appendix 1 of our licence, which considers the period to 2030, is only likely to be made with the agreement of Tideway. We are focused on being a compliant and high performing regulated company, with positive regulatory relationships.

Performance Review

In this section, we describe the progress we made against each of the objectives set out on pages 20 to 21

HEALTH, SAFETY AND WELLBEING

KPIs	2015/16
Accident Frequency Rate (number of reportable accidents per 100,000 hours worked – includes both Tideway employees and contractors)	0.00
Number of people that have gone through the Employee Project Induction Centre (EPIC)	2,549 (to end of March 2016)

Ensuring the highest standards of health and safety is paramount for Tideway. We are pleased to report that we did not have any significant incidents during the period. We introduced a new health, safety and wellbeing strategy, “Right Way”. The first element of Right Way is “Right Start”, a collection of actions and standards designed to prevent incidents that typically occur at the start of major projects. Right Start includes:

- risk profiling early works, and reviewing and ensuring effective controls for significant risks;
- an innovative induction process to engage all new staff and operatives; and
- defining and committing to significantly higher standards for the things we do, from personal protection equipment, site layout and arrangements, to welfare facilities and marine logistics.

In late summer 2015, we established the Transforming Health and Safety Group (THSG). This group looks at how we can make a difference to on-site activities through staff and operatives involved in the day-to-day leadership of health and safety, with appropriate support and challenge from senior management. This facilitates sharing of best practice to achieve high-levels of health, safety and wellbeing performance across the Alliance. THSG includes representatives from Tideway, the main works contractors, the systems integrator and Thames Water.

As part of the first stages of the transformational HSW programme, this year we established EPIC. This forms part of the induction process and every person engaged on the project is required to attend. To date, 2,549 employees and contractors from 150 different organisations have attended the course, for which we have received outstanding feedback. EPIC’s innovative and interactive training has been recognised by the industry, winning the EvCom live training award in November 2015.

We recognised that clear communication is key to preventing incidents. Research has shown that 30% of all incidents in the construction industry are due to poor communication. We therefore delivered an HSW communication assessment, with technical, understanding and pictorial questions. This is the first time this approach has been undertaken on a major project.

Our safety documentation was audited by an independent certification body, BSI, and achieved OHSAS18001 accreditation. We also achieved accreditation for our environmental and quality management systems to ISO14001 and ISO9001 respectively. We expect the main works contractors to achieve the same standard in 2016.

Tideway also partnered with Loughborough University, which is undertaking a study into health and safety approaches and practices. This study will look at the early stages and activities we have completed already, such as EPIC and early contractor engagement. The learning from this research will be available in Autumn 2016.

COMPANY AND PEOPLE

KPIs	2015/16
Gender diversity* (percentage of women within Tideway at 31 March 2016)	37%
Employee engagement (Tideway employee survey: percentage of favourable responses)	59%
Employee enablement (Tideway employee survey: percentage of favourable responses)	59%

** Includes Tideway employees and our project management contractors (CH2M)*

During the year, we implemented a number of important initiatives in relation to our people. Two months after licence award (October 2015), we conducted an externally benchmarked employee engagement survey (overall score achieved in 2015/16; 59%). This showed that Tideway has strong results that exceed HayGroup external benchmarks in the following areas: social responsibility, ethical business dealings, respecting diversity and our people and understanding of the Company’s strategy and goals. However, more work is required to improve decision making, performance management and enabling all employees to be effective. Company and local team action plans are in place to address these areas.

Effective performance management is important and our people identified this as a focus area in the engagement survey. We look to give employees clear objectives and regular reviews to help develop performance and recognise and reward achievements. To ensure that we deliver against our milestones and goals, we cascaded targets through the organisation from the CEO down. These targets also formed the basis for the company element of the performance-related bonus for Tideway staff. As part of this process, we carried out our first talent management and succession planning review after licence award. This will form a regular health check of the business and ensure we have appropriate bench strength for key roles, as part of Tideway’s structured performance review process.

Tideway recognises the importance of diversity, since diverse organisations have been shown to make better decisions and have higher performance. We improved our gender balance within Tideway from 30% female at the start of the year to 37% at year end. We achieved this through a number of initiatives, including how and where we advertise roles to ensure the broadest range of candidates, unconscious bias training for all employees, and implementing the first returners programme outside the banking industry. This programme is open to people who have been out of employment for two years or more, typically because they had caring responsibilities. While the programme is open to men and women, all the successful candidates were women. Seven joined Tideway on a 12-week paid internship, in disciplines including operations, asset management, finance, legal and business planning. Six remain with the Company and five have become permanent employees. At the end of the year, the gender mix of our people was as follows:

Headcount* as at 31 March 2016	Male	Female	Total
Board	9	3	12
Senior management	31	12	43
Other employees	214	137	351
Total	254	152	406

** Includes Tideway employees and our project management contractors (CH2M)*

We look to develop the next generation of talent and to help local and disadvantaged people into employment, so we leave a lasting skills legacy for London and beyond. As part of the planning process, the project entered into section 106 agreements with most of our local authorities, which included targets for employing apprentices, local people and ex-offenders. Tideway and our contractors are committed to employing one in 50 staff as an apprentice, one in 100 to be an ex-offender and 25% of our workforce being residents of the London Boroughs.

Performance Review
Continued

We have developed plans to meet these targets. Tideway has effective apprenticeship programmes, which we extended in 2015/16 from just engineering to include corporate functions. Our on-site café is provided by Changing Paths, a charitable trust helping to get serving offenders, ex-offenders and the long-term unemployed into full time employment, through training and work experience placements. Tideway is committed to ensuring that all employees are paid at or above the London Living Wage.

Human rights
Our approach to business and how we work provide a clear ethical and legal framework for our employees, contractors and stakeholders, setting out the minimum behaviours we expect. Our policies and procedures cover a wide range of human rights issues, including discrimination, working conditions and equal opportunities. Tideway has a confidential 24-hour whistleblowing helpline, allowing any employee to ask questions or raise concerns.

SCHEDULE, COST AND QUALITY

KPIs	2015/16
Delivery against the regulatory baseline – cost*	£3.1bn (on target)
Delivery against accepted programme - schedule	Handover by Q1 2024 (on target)

** Tideway's element of the programme, up to system acceptance by Thames Water (in 2014/15 prices)*

Working closely with our contractors, we developed plans to unlock opportunities to de-risk the delivery of the tunnel against the regulatory baseline schedule and complete the tunnel at the earliest, safe time. The ambition of starting tunnelling earlier and subsequently handing over the tunnel earlier should de-risk the programme and drive cost savings against the regulatory baseline of £3.1bn, benefiting both investors and Thames Water's customers, as well as delivering environmental benefits sooner and reducing community disruption.

The Alliance between us, the main works contractors, Amey and Thames Water is another key part of our strategy. It is governed by an Alliance Agreement which sets out an overarching framework for collaborative working between all parties and incentivises behaviours to promote the successful completion of the works.

How we work with our colleagues across the Alliance will be key to delivering success. Numerous team building activities have begun, to support team integration across Tideway and its delivery partners. This encourages collaborative behaviour, which helps to realise synergies, reduce costs and shorten the delivery schedule. Consents are critical to allow tunnelling to start earlier so a key focus has been to develop an integrated contractor-led consents schedule. With good progress in 2015/16, we were able to start on-site earlier than originally planned. This has enabled us to have more time to deal with the inevitable problems and challenges of tunnelling in London.

Our first site works began in December 2015, with the works at Blackfriars to relocate the Millennium Pier. We are building a new pier for the riverboats on the eastern side of Blackfriars Station. Work is under way to construct a new lift and stairs to improve access. HMS President, which was berthed close to the Millennium Pier, has been relocated by its owner as part of the early works.

Work continued throughout the year on the challenges associated with directly integrating Thames Water's proposed Counters Creek sewer flooding alleviation scheme with our works at Cremorne Wharf. After year end and in support of our earlier schedule ambitions, we have mobilised early on each of our three main tunnel drive sites with the establishment of offices and facilities, site surveys and investigations, and some temporary works. These activities should allow the early commencement of main construction works later in the year.

FINANCING

KPIs	2015/16
Maintain Group credit rating* / (Moody's / Fitch)	Baa1/BBB+
Total Liquidity at 31 March 2016	£2bn (>18 months)

** The Group has been assigned a corporate family credit rating of Baa1 by Moody's and the Company's Revolving Credit Facility (RCF) has been rated BBB+ by Fitch.*

Treasury policy
Tideway's treasury policy is to finance the Company, while minimising our weighted average cost of capital to drive shareholder value. Our target is to maintain a robust investment grade credit rating at all times. Tideway has a financing strategy which defines the implementation of the policy. Key elements of the strategy are detailed within the strategy section (page 21).

Financing activity
At Licence Award in August 2015, Tideway's shareholders committed £1.3bn of capital in the form of equity (40%) and shareholder loans (60%). Tideway also entered into a £1bn, ten-year revolving credit facility with a consortium of six banks. This facility remained undrawn over the year. Following licence award, the Group received investment grade credit ratings of Baa1 from Moody's and the RCF has been rated BBB+ by Fitch. Those ratings remained unchanged during the year.

As at 31 March 2016, a net £342.5m had been received from shareholders. This was in the form of £138.3m of equity and £204.2m of net shareholder loans. During the year, we progressed negotiations with the EIB to borrow financing for the Company's construction works and began work on the bond financing programme.

Distributions
Tideway capitalises its construction costs and does not expect to record distributable profits until after system acceptance. Accordingly Tideway does not expect to pay dividends during the construction period.

In order to provide a return to its shareholders during the construction period, Tideway makes distributions through payment of interest and repayment of principal on its shareholder loans. These payments are set to provide a sustainable growth profile, while maintaining an appropriate headroom to our financing covenants over the construction period.

Liquidity
At 31 March 2016, we had total liquidity in excess of £2bn, comprising £0.1bn of cash, £0.9bn of committed and undrawn capital from shareholders and the £1bn undrawn revolving credit facility. This provides liquidity significantly in excess of our 18-month target.

After year end
We have entered into financing transactions which further improve our liquidity and help lock-in financing costs. In May 2016, the EIB agreed to provide a £700m 35-year long-term loan to Tideway. The innovative structure enables us to lock-in financing costs, whilst also matching our funding requirements and profiling debt service, in line with the expected growth in our asset base.

In June 2016, Tideway priced bond issues totalling £350m. These deferred-purchase bond issues mark Tideway's debut on the capital markets. Combined with our EIB loan, they will help secure the financing for our long-term investment programme.

Performance Review
Continued

VISION, LEGACY AND REPUTATION

KPIs	2015/16
Volunteering*: STEM (science, technology, engineering, maths) sessions and time spent supporting community causes and charities. * *Includes Tideway employees and contractors*	STEM – 506 volunteering hours Community – 757 volunteering hours
Number of apprentices working at Tideway	1 per 64 FTEs

Establishing Tideway's vision and identity was a key part of our work this year. Our vision of "Reconnecting London, and Londoners, with the River Thames" (see page 18) defines what we want to achieve and was developed through in-house workshops with our staff. We selected the Tideway name for its simplicity and effective communication of our connection to the river.

To deliver our vision, we have to ensure that we build a strong reputation with stakeholders, forge close links with local communities and deliver a lasting legacy for the capital.

Engaging communities and stakeholders is a key priority. The quarterly Thames Tideway Tunnel Forum is independently chaired and has brought together officer representatives of the directly affected London boroughs and other statutory consultees since 2008. Now with a number of sub groups, it is a very effective way of exchanging information and creating a consensus on project-wide issues in a timely and cost-efficient manner.

Tideway is committed to building relationships with local communities and getting residents involved in what we are doing. Community Liaison Working Groups operate where we have active construction sites and regular community meetings, to help share information on the project and seek input from residents on arrangements. In the past year, Tideway held more than 20 of these meetings for three sites, with a number of further smaller meetings for specific residents.

Tideway has established a dedicated helpdesk to answer all public enquiries. Staffed 24/7 as a one-stop-shop for local communities and those wanting to know more about the project, it took more than 2,400 calls in the year. In addition, we have put in place a series of measures to help those who can benefit from our mitigation and compensation policies. Specifically, these include an:

- Independent Advisory Service – to offer free advice about mitigation and compensation.
- Independent Compensation Panel – to ensure that claims are assessed fairly and quickly.
- Independent Complaints Commissioner – to provide a high level point of contact for those who wish to escalate a complaint or claim.

As well as being a good neighbour, Tideway is determined to give back to the communities in which we work. We engage directly with a number of community investment projects, which aim to create enduring partnerships. In 2015/16 these included Thames River Watch, a citizen science project run by environmental charity Thames 21, which aims to improve understanding of the health of the tidal Thames. Another key community investment project was London Youth Rowing. This project aims to establish an indoor rowing programme and competition across the London boroughs that border the Thames. The scheme forms part of our efforts to encourage young people to reconnect with the river and take advantage of the leisure opportunities it provides.

We support three staff-nominated London charities, which gained from staff fundraising and the voluntary contribution of our staffs' skills and time. They are: Thames Reach, which helps homeless and vulnerable people; Envision, which develops young people's employability; and KEEN London, which provides sports and arts/crafts activities for children with special needs.

Tideway aims to leave lasting benefits for London and our legacy programme will make this aspiration a reality. The Tideway Alliance has developed a Skills and Employment Plan, together with a more wide-reaching Legacy Plan. This defines our commitments under five themes - Environment, Health and Safety, Economy, People and Place.

The STEM and education programme is part of Tideway's legacy

Environment
While we have a clear objective to significantly improve the environment of the River Thames, another key commitment is to reduce the environmental impact of constructing the tunnel. We have started to develop a carbon management plan and, once this is finalised, we will agree a target to reduce our carbon footprint below current predictions of 840,000 tonnes of CO_2. We have also signed up to the Government's Infrastructure Carbon Review.

Health and Safety
Tideway is aiming to deliver a transformational programme which sets new standards for major projects to follow. Details of our achievements in 2015/16 are in the Health, Safety and Wellbeing section of this review.

Economy
The Tideway Alliance has signed up to the Fair Payment Charter, which requires companies to pay suppliers within 30 days. We also held our first 'Meet The Buyer' events in Greenwich, to highlight opportunities for local businesses. It was attended by 99 companies, of which 91 were local and 93 were small and medium enterprises.

People
The development of the Tideway-supported Thames Skills Academy, which will train a new generation of river workers, was a milestone in 2015/16. With the UK predicted to need 182,000 new engineers by 2022, our STEM and education programme is a key part of our legacy. We delivered 36 STEM sessions in the year (506 STEM volunteering hours) and our education programme delivered classroom resources, careers information and focused on employability skills.

Place
Tideway's community partnerships helped deliver 757 hours of volunteering (1.16 hours per FTE), well ahead of the published target. Good progress was also made against the commitment to employ ex-offenders.

See the Company and People section for more detail.

Financial Performance Review

Accounting Basis

Our financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). Under IFRS, lease accounting is considered the most appropriate accounting basis for Tideway post system acceptance. Accordingly during the construction period all costs are being capitalised under the heading "Asset under Construction" within the Statement of Financial Position. All revenue is being recognised as "deferred income" within the Statement of Financial Position.

Reporting of Allowable Project Spend

Under Tideway's licence, its regulated costs are classed as either "Allowable Project Spend" or "Excluded Project Spend". Allowable Project Spend (on a cash basis) is added to the Regulatory Capital Value (RCV) while Excluded Project Spend, such as financing costs, is not added to the RCV. In our financial statements we present costs on an accruals basis and there is no distinction between Allowable and Excluded costs.

Income Statement

During the period ended 31 March 2016, Tideway reported a profit of £nil and no dividends were paid or proposed. Tideway did not recognise any taxable profits in the period and has no corporation tax liability.

Statement of Financial Position

The table below provides an analysis of costs capitalised in the Statement of Financial Position (on an accruals basis) and cash outflows for the period ended 31 March 2016.

Analysis of costs and cash outflows	Costs £m	Timing differences £m	Cash outflows £m
Direct costs	69.0	(11.6)	57.4
Indirect costs	49.9	43.0	92.9
Total allowable costs	118.9	31.4	150.3
Total excluded costs	42.3	19.5	61.8
Total	161.2	50.9	212.1

The £150.3m Allowable Project Spend (on a cash basis) is higher than the £118.9m of Allowable costs (on an accruals basis) as it includes upfront payments for insurance and the Government Support Package (GSP).

During the period, £161.2m of costs were capitalised as "Asset under Construction" within the Statement of Financial Position. These include £118.9m of Allowable costs and £42.3m of excluded costs. The table below provides an analysis of the costs relating to Allowable costs:

Allowable costs	£m
Main works costs	54.9
Other direct costs	14.1
Direct costs	69.0
Resources	31.1
Other indirect costs	18.8
Indirect costs	49.9
Total	118.9

Main works costs

The main works contract costs are split between three regional contracts, West, Central and East, for the design and construction of the main tunnel. All three main works contracts are based on the New Engineering Contract (NEC3) Option C Target Price with Activity Schedule terms and conditions. The costs incurred in the period include contractors' staff, design, consents and preliminary costs to support the "Right Start" readiness and mobilisation at the three main drive sites.

Other direct costs

The other direct costs of £14.1m mainly consist of £10.8m of marine vessel relocation and design costs. These costs relate to a contract with VolkerStevin Ltd to provide services and works for the removal and replacement of piers and the relocation of marine vessels. Also within other direct costs are £1.7m of third party costs for the management, monitoring and mitigation of the impact of construction on third parties.

Indirect costs

The largest indirect cost is the resource costs of £31.1m. This represents the cost to employ the circa 400 FTEs either employed or contracted by the Company. The other indirect costs include information systems, insurance, payment for the GSP, office and other running costs.

Excluded costs

The Excluded costs to 31 March 2016 were £42.3m on an accruals basis, comprising mainly of financing costs, with part of the fees related to the GSP and loan interest.

Net Cash and Financing

The net cash for Tideway at 31 March 2016 was £130.4m. This included £17.5m of short-term cash deposits with a maturity of greater than three months and £112.9m of cash and cash equivalents. The table below summarises the net cash movements during the period:

Net cash	£m
Net proceeds from loans	204.2
Proceeds from equity	138.3
Cash inflows	342.5
Cash outflows	(212.1)
Total	130.4
Cash and cash equivalents	112.9
Short-term cash deposits	17.5

During the period, Tideway received funds of £342.5m from shareholder injections. This was in the form of equity (£138.3m) and net shareholder loans (£204.2m). The cash outflows of £212.1m included £160.3m for investing activities, being the construction of infrastructure assets. The balance of £51.8m reflects working capital movements.

At 31 March 2016, Tideway had debt of £205.1m in the form of shareholder loans. The £205.1m represents the £204.2m of net proceeds and £0.9m of capitalised interest. Tideway also had access to a £1.0 billion Revolving Credit Facility which was undrawn at 31 March 2016.

On 1 April 2016, Tideway received further shareholder injections of £107.1m, in the form of £42.8m equity and £64.3m of shareholder loans. During May 2016, Tideway entered into a £700m loan with the EIB. In June 2016, Tideway priced bond issues totalling £350m.

Regulatory Financial Reporting

For regulatory financial reporting, interest is expensed through the Regulatory Income Statement. The Regulatory Income Statement contains £8.3m of loan interest expense partly offset by £0.4m of interest income, resulting in a net loss of £7.9m.

Within the £212.1m of cash outflows (per the Net Cash table above) is £150.3m of Allowable Project Spend for the period. When adjusted to 31 March 2016 outturn prices, consistent with the licence definitions, this amount equals the £151.3m of RCV as shown in Table 5b on page 109.

Revenue

Within the financial statements, all revenue is recorded as deferred income in the Statement of Financial Position, in line with the revenue recognition accounting policy on page 85. Revenue of £8.8m is reported for 2015/16, which is based on the latest estimate as at April 2016. This is lower than the £11.2m included in the final December 2015 revenue statement submitted to Ofwat, largely reflecting lower Allowable Project Spend in 2015/16. While the Company did not receive any cash inflows from revenue during the period, monthly revenue receipts commenced in April 2016.

The Strategic Report was approved by the Board on the 21 June 2016 and was signed on its behalf by:

A. Mitchell
Director

Governance

37 Corporate Governance Report

Chairman's Introduction

Board Leadership, Transparency and Governance

58 Audit Committee Report

64 Remuneration Report

72 Directors' Report

75 Long Term Viability Statement

Louis Pettipher from Gravesend won the 300th anniversary Doggett's Coat and Badge Wager in 2015, joining an elite group of watermen entitled to wear the trappings from which the historic race derives its name. The annual single sculls challenge from London Bridge to Chelsea is open to recently qualified river apprentices, testing not only their physical prowess, but also their knowledge of the river. Louis' day job is as a captain with City Cruises.

Preparatory works taking place in the Central region

Chairman's Introduction

'Good corporate governance must be at the heart of any enterprise, but it is particularly important for a private-sector organisation working in a regulated sector'

SIR NEVILLE SIMMS
NON-EXECUTIVE CHAIRMAN

As Chairman of the Board, I am pleased to present our first corporate governance report since the Project Licence was awarded in August 2015.

Good corporate governance must be at the heart of any enterprise. As an organisation working in the regulated utility sector, we consider strong governance and leadership, together with properly transparent reporting, effective risk management and long-term decision making, to be of the highest importance.

Tideway is therefore committed to achieving the highest standards of corporate governance. Although we are a private company, as a regulated entity we are expected to operate as if we were a public company. As a result, we look to comply with the UK Corporate Governance Code 2014 (the Code) and Ofwat's guidance. I am pleased to report that we comply with the Code, except in respect of the requirement that at least half of the Board, excluding the Chairman, should comprise independent non-executive directors. However, we do comply with all of Ofwat's published guidance, including Ofwat's requirement that the independent non-executive directors, including the Chairman, are the largest single group on the Board.

As Tideway is owned by private investors, we also take into account the relevant section of the Guidelines for Disclosure and Transparency in Private Equity (the Walker Guidelines) for portfolio companies and the work of the Guidelines Monitoring Group. To aid transparency, our holding companies also comply with Ofwat's holding company principles.

The Board has recognised the challenge and the opportunity represented by Tideway being a completely new company. Bringing the right skills onto the Board and establishing best practice governance structures and procedures has been at the forefront of the establishment of Tideway's governance system, controls and procedures. Whilst Tideway was only formally established at licence award, the good governance practices that we now observe were initiated by the Board of Thames Tideway Tunnel Limited, a company set up prior to licence award and which is now a Tideway subsidiary company. All the Directors of Thames Tideway Tunnel Limited are now Directors of Tideway.

Reflecting the Board's commitment to strong governance, we monitor, review and amend our procedures and performance as required, to ensure we remain at the forefront of UK corporate governance best practice.

Sir Neville Simms,
Chairman

Fish surveys monitor the habitat at Blackfriars

Board Leadership, Transparency and Governance

The Board

NON-EXECUTIVE DIRECTORS

Sir Neville Simms FREng
Non-Executive Chairman, (Chair of Nominations Committee)

Sir Neville is a Chartered Civil Engineer. He was previously Chairman of International Power plc and of Carillion plc, following its demerger from Tarmac plc, where he was Group CEO. He was joint Chairman of TML, the Channel Tunnel contractors' consortium, for the final three years of the Channel Tunnel project.

Sir Neville chaired a number of construction industry bodies and the regional leadership teams for Business in the Community in the West Midlands and the Solent Regions. He was a founder member of the UK Government's Private Finance Panel, Chairman of the Government's Sustainable Procurement Task Force, Deputy Chairman of Ashridge Management College and Chairman of the Building Research Establishment Trust. He was also a member of the President's Committee of the CBI for 12 years and served for seven years on the Court of the Bank of England.

Richard Morse
Deputy Chairman and Independent Non-Executive Director (Chair of the Audit Committee)

Richard is an investment banker with more than 30 years' experience of infrastructure and energy transactions, having been head of energy and infrastructure corporate advisory teams at Dresdner Kleinwort Wasserstein, Goldman Sachs International and Greenhill International. Richard joined the board in 2015, having sat on the board of subsidiary Thames Tideway Tunnel Limited since 2013 to assist in the set-up of Tideway. He chairs Tideway's Audit Committee and is also a partner at Opus Corporate Finance, Chairman of John Laing Environmental Assets Group and Chairman-designate of Woodard Corporation.

Anne Baldock
Independent Non-Executive Director (Chair of the Remuneration Committee)

Anne is a lawyer by background, having been a partner at international law firm Allen & Overy LLP for 25 years, where she helped to structure many innovative infrastructure and energy deals. Anne joined the Board in 2015, having sat on the board of subsidiary Thames Tideway Tunnel Limited since 2013 to assist in the set-up of Tideway. She chairs Tideway's Remuneration Committee. Until last year, Anne sat on the Nuclear Liabilities Financial Assurance Board and was a trustee of Cancer Research UK. She is a Non-Executive Director of the Low Carbon Contracts Company and the Electricity Settlements Company Limited.

Board Leadership, Transparency and Governance

The Board

Mark Fairbairn OBE
Independent Non-Executive Director
(Chair of the Risk Committee and HSSE Committee)

Mark has significant experience running regulated gas and electricity utilities, both in the UK and USA. He joined the board in 2015, having sat on the board of subsidiary Thames Tideway Tunnel Limited since 2013 to assist in the set-up of Tideway. He chairs Tideway's Health, Safety, Security & Environment and Risk Committees. He is a Director of Photonomi, an innovative global renewable energy business, and has also served as a Non-Executive Director of the Office of Rail and Road Regulation and as a member of a Business Advisory Board to the Government's Living with Environmental Change Programme.

Michael Queen
Independent Non-Executive Director
(Chair of the Treasury Committee)

Michael is a Chartered Accountant and has spent 30 years in the alternative finance sector, having previously been CEO of 3i Group plc. He chairs Tideway's Treasury Committee. Michael joined the board in 2015. He is currently Chief Executive of Aquilys Investment Management Ltd, Non-Executive Director of Coller Capital, a member of the Advisory Board of CKGSB (a Beijing-based business school) and a Member of the Council at the University of Surrey, where he is also President of Surrey 100, a business angel group. He has also served as a Non-Executive Director and Chairman of the Audit Committee of PA Consulting Group and was a member of the Prime Minister's Business Advisory Group.

COMPANY SECRETARY

Tracey Lee
Company Secretary

Tracey was appointed Company Secretary and Senior Legal Counsel of Tideway in November 2014, having advised Thames Water on developing the legal agreements and procuring and negotiating of the Main Works Contracts since February 2014. Prior to this, she was involved in the development and delivery of infrastructure projects in the United Kingdom and Canada. Tracey is an Associate Chartered Accountant and a Solicitor of the High Court of New Zealand.

NON-EXECUTIVE SHAREHOLDER DIRECTORS

Gavin Tait
Amber Infrastructure

Gavin has 20 years' experience of developing and investing in global infrastructure and utility assets. He joined the Tideway Board in August 2015, representing Amber Infrastructure as a Shareholder Director.

Jaroslava Korpanec
Allianz

Jaroslava was awarded a Masters and a Master of Arts degree in Law from Cambridge University. She is a member of the New York bar and a solicitor of the Supreme Court of England and Wales. Jaroslava joined the Tideway Board in August 2015. Prior to joining Allianz Capital Partners in 2008, she worked on a number of debt and equity investments in the infrastructure sector. Among other transactions, Jara was responsible for the acquisition in February 2009 of the 75-year concession to own, manage and operate the on-street parking system of the City of Chicago; the acquisitions of stakes from Total and Statoil in the Norwegian offshore gas system, Gassled; the acquisition of the gas transmission and transport system in the Czech Republic, Net4Gas; and the acquisition of Porterbrook, one of the three major UK rolling stock leasing companies. Jaroslava also worked at AIG Financial Products in the principal finance group, where she made several investments in the infrastructure sector. Jaroslava was one of the principals responsible for the acquisition and management of London City Airport on behalf of AIG Financial Products. Prior to her position at AIG Financial Products, Jaroslava was a senior attorney with the US law firm of Simpson Thacher and Bartlett, where she spent six years.

Moira Turnbull-Fox
DIF

Moira is a Senior Director of DIF. She joined the Board in March 2016. She is primarily responsible for the asset management of a number of UK and Irish assets held in the DIF funds. Prior to joining DIF, Moira was an Assistant Fund Manager in the Lend Lease PPP/PFI Infrastructure Fund (LLPIF). The LLPIF fund team was responsible for the asset management, origination, reporting and valuation of a £220m committed fund. She is a member of the Institute of Chartered Accountants in England and Wales. Moira has worked in infrastructure projects for over 15 years as an advisor, banker, equity investor and lately, asset managment. This included roles within Arthur Andersen, Commerzbank, BAE Systems and Lend Lease Corporation.

Alistair Ray
Dalmore Capital

Alistair has worked in the infrastructure investment business for 19 years, including at Edison Capital, Noble Group, Merrill Lynch and 3i Infrastructure plc, where he was one of the founding members of the infrastructure team and involved in a number of transactions, including the acquisition of Anglian Water and purchase of stakes in Oiltanking GMBH. Alistair joined the Board in August 2015. He is currently the Chief Investment Officer of Dalmore Capital and also holds a Non-Executive Director role with CAF Bank.

Board Leadership, Transparency and Governance

The Board

EXECUTIVE DIRECTORS (ALSO PART OF EXECUTIVE COMMITTEE)

Andy Mitchell CBE, FREng
Chief Executive Officer

Andy was appointed Chief Executive Officer (CEO) after leaving Crossrail in summer 2014, where he was Programme Director and a member of the Board. Andy has managed a number of high-profile projects in the UK and overseas. After 12 years working in the United Arab Emirates, France and South Africa, and on major developments such as Hong Kong Airport and the Hong Kong West Rail, he joined Network Rail in 2001.

He was Project Director for Network Rail's Southern Power Upgrade project and the Senior Programme Director of the Thameslink Programme. Andy is a Fellow of both the Royal Academy of Engineering and the Institute of Civil Engineers and Chairman of the IUK Infrastructure Client Group. He holds a degree in Civil Engineering from Imperial and an MBA in Project Management from Henley, and is a visiting professor at Leeds University.

Mark Sneesby
Chief Operating Officer

Mark joined Tideway as Chief Operating Officer (COO) in May 2014. He is a Chartered Civil Engineer with extensive experience in delivering major infrastructure in the water industry. He was formerly Head of Major Projects at Thames Water, which included the Lee Tunnel project, one of the largest contracts ever awarded in the UK water industry.

Mark Corben
Chief Financial Officer

Mark joined Tideway in February 2014 and was appointed Chief Financial Officer (CFO) in July 2014. Prior to this he was Head of European Power & Utilities at UBS, where he advised Thames Water on the development of the delivery model for Tideway. Mark has 17 years' investment banking experience in corporate finance, mergers and acquisitions and capital raising. He qualified as a Chartered Accountant with Price Waterhouse in 1996.

EXECUTIVE COMMITTEE

The Executive Committee has nine members and is responsible for overseeing the management of the company day-to-day, recommending business development strategies to the Board and implementing the Board's objectives and policies. In addition to the Executive Directors, the Executive Committee comprises the following individuals:

Peter Shipley
Programme Delivery Director

Peter is a Chartered Civil Engineer with 30 years' experience. He has worked for CH2M for 17 years and held a key role in delivering the infrastructure for the London 2012 Olympics and the Lee Tunnel.

Roger Bailey
Asset Management Director

Roger is a Fellow of the Institution of Civil Engineers, with more than 30 years' experience in the planning, design and construction of complex infrastructure projects in the UK and internationally.

Julie Thornton
Head of Human Resources

Julie joined the project in October 2013. Her corporate career started over 25 years ago with IBM, where she was Head of HR for Global Services in the UK, before moving to Citibank Private Bank, where she was VP for HR in EMEA in Geneva and London.

Phil Stride
External Affairs Director

Phil is a Fellow of both the Institution of Civil Engineers and the Royal Institution of Chartered Surveyors. He worked for Thames Water for 41 years, where he was Head of Thames Tideway Tunnel for seven years. He had previously been Head of Capital Delivery.

Celia Carlisle
General Counsel

Celia joined the project in September 2013, having previously held the role of General Counsel at the Olympic Delivery Authority. She has over 20 years' experience advising on major infrastructure projects and their financing. Celia is also a Non-Executive Director for the Government Legal Department.

Steve Hails
Health, Safety and Wellbeing Director

Steve is a Chartered Member of IOSH and Associate Member of IEMA and has over 20 years' experience working in the engineering and manufacturing sectors. He joined Tideway at the beginning of June 2016 as the Director of Health, Safety & Wellbeing, having previously worked as Director of Health & Safety on Crossrail.

Board Leadership, Transparency and Governance

The Role & Responsibilities of the Board

THE ROLE OF THE BOARD

The Board's role is to govern Tideway so it delivers on its objectives, in particular the successful delivery of the Thames Tideway Tunnel. The Board is collectively responsible for the Company's long-term success and for delivering sustainable value to shareholders and other stakeholders. It sets the Company's strategy and risk appetite in all significant areas of the Company's operations and approves and monitors management's plans for achieving the Company's strategic objectives and targets, including risk mitigation.

Important aspects of the Company's business are subject to scrutiny by the Board Committees: Audit, Treasury, HSSE, Nomination, Remuneration and Risk. Further descriptions of the terms of reference and activities of these committees are set out on pages 48 to 53 of this report.

The Board has approved a schedule of delegated authority (SoDA), which defines the levels of authorisation required for key decisions in relation to funding and investment, contractual commitment and change, invoicing and payments, procurement, recruitment, treasury and the discharge of consents. The SoDA authorises management to approve decisions up to specified limits, beyond which the Board's approval must be obtained. The Board reviews the SoDA each year or by exception.

Certain decisions are reserved to the shareholders for ultimate approval and these are set out on pages 56 to 57 of this report. Nevertheless, the Board considers all such issues and advises the shareholders as appropriate.

The Board has 12 Directors, nine of which are Non-Executive, with five being independent Non-Executives in compliance with Ofwat's requirement that the independent Directors (including an independent Chair) be the largest single group on the Board. The Chairman of the Board, Sir Neville Simms, is one of the independent Non-Executives. The Board retains responsibility for the Company's overall direction, supervision and management.

The following matters are reserved to be decided by a simple majority of the Board:

- **Significant risks:** determining the nature and extent of the significant risks the Board is willing to take in achieving the Company's strategic objectives.
- **Chairman and Chief Executive Officer:** the division of responsibility between the Chairman and the Chief Executive Officer.
- **Directors' remuneration:** approval of the Directors' remuneration.
- **Director and executive training:** approval of induction training and development programmes for Directors and senior employees.
- **Reporting:** approval of preliminary and annual reports and accounts, half-yearly reports and interim reports.
- **Accounting policies and practices:** approval of accounting policies and practices and any changes to them.
- **External auditors:** approval of the Audit Committee's strategy for maintaining appropriate relationships with external auditors.
- **Risk and internal control policies:** setting risk management and internal control policies.
- **Risk and internal control review:** reviewing the effectiveness of risk management and internal control systems.
- **Policies:** setting the policy on business conduct, ethics, human rights, anti-bribery and corruption, corporate social responsibility and health and safety.
- **Insurance:** setting and monitoring the overall levels of insurance.
- **Shareholder general meeting:** approval of resolutions and related documentation to be put to shareholders at a general meeting.
- **Shareholder communications:** approval of any circulars, prospectuses and other documents to be sent to shareholders.
- **Political and charitable donations:** approval of all spend relating to political and charitable donations.
- **Related party transactions:** approval of the entry into, amendment to, or a step to resolve any dispute in relation to a related party transaction.

DIVISION OF RESPONSIBILITIES WITHIN THE BOARD

The roles of Chairman and Chief Executive Officer (CEO) are separate and clearly defined. The Chairman's primary role is to provide independent oversight and governance as leader of the Board, while the CEO is responsible for all the operations of the Company, as leader of the Executive Committee.

The Role of the Chairman

The Chairman is the most senior leader of the business and guardian of the interests of all shareholders and stakeholders. The Chairman is responsible for leadership of the Board and ensuring its effectiveness. It is important that the Chairman and CEO work well together, to provide effective and complementary stewardship. The Chairman takes overall responsibility for the Board's composition, capability and performance evaluation. He consults regularly with the CEO and is also available to provide the CEO with advice and support.

The Chairman's key functions are to:

- Manage the Board and run Board meetings;
- Take responsibility, with the Board, for agreeing and monitoring the Company's strategy and its delivery through the Business Plan;
- Ensure good corporate governance is maintained, in the interests of all stakeholders;
- Discuss with the CEO any recommendations from the Remuneration Committee;
- Agree with the CEO all key external communications;
- Represent the Company externally at the most senior level;
- Determine with the CEO which matters require Board approval; and
- Determine with the Company Secretary which decisions are reserved to the shareholders.

The Role of the Chief Executive Officer

The CEO is responsible for the Company's leadership and operational management, within the business plan approved by the Board. He is supported by the CFO, COO, and six other direct reports on the Executive Committee.

The CEO's key functions are to:

- develop the Company's vision and values;
- manage the Executive Committee and the Company's day to day activities;
- set the operating plans and budgets required to deliver the agreed Company strategy;
- ensure that the Company has appropriate risk management and control mechanisms;
- develop the necessary performance objectives and non-financial programmes required to enhance and develop the Company's culture;
- determine, strengthen and develop the Senior Management Team; and
- share with the Chairman the external representation duties for the Company.

The role of Non-Executive Directors

The Board includes nine Non-Executive Directors, four of whom represent the current shareholders and five of whom are independent.

Non-Executive Directors use their breadth of knowledge and experience to challenge, monitor and approve the strategy and policies recommended by the Executive Directors. The independent Non-Executive Directors each chair the Board Committees relevant to their skills and experience. The strong independent representation on the Board helps ensure that the Board is able to make decisions that are in the interests of the Company, independent of other objectives.

The Chairman holds periodic meetings to discuss the performance of management and the Board. These meetings are held with all the Non-Executive Directors without the Executive Directors present and with the independent Non-Executive Directors without the Shareholder Directors present.

The role of the Senior Independent Non-Executive Director

The Board has appointed Richard Morse as Deputy Chairman of the Board, in which role he fulfils the functions of the Senior Independent Non-Executive Director. He provides a sounding board for the Chairman and serves as an intermediary for other Directors, when necessary or appropriate.

The Deputy Chairman is also available to shareholders and other stakeholders if they have concerns which it would be inappropriate to raise through the conventional channels of Chairman, CEO or the other Executive Directors.

The role of Executive Directors

The Executive Directors are the CEO, COO and CFO. The role of the CEO is set out above.

The COO is responsible, working closely with the CEO and CFO, for the delivery of the project through the main works contractors and the Alliance.

The CFO manages the Company's finances, including financial planning, management, accounting and control processes and treasury, in order to deliver the capital programme effectively, manage ongoing operations and ultimately protect shareholder value. The CFO is also responsible for delivering the Company's information systems strategy.

Board Leadership, Transparency and Governance

Board Composition

The Board is chaired by Sir Neville Simms, an independent Non-Executive Director, and includes three Executive Directors and eight other Non-Executive Directors, four of whom represent the current shareholders and four of whom are independent.

The Shareholders' Agreement entered into at licence award contains legally binding commitments to maintain an independent board and ensure the Company can make strategic and risk management decisions. The Board considers that the independent Non-Executive Directors are independent in character and judgement and is satisfied that there are no relationships or circumstances which are likely to affect, or could appear to affect, the independent Non-Executive Directors' independence.

The Board believes that it has the right combination of Executive Directors, Shareholder Directors and independent Non-Executive Directors, to ensure that no individual or small group can dominate the Board's decision making. Independent Non-Executive Directors (including the Chairman) form the largest single group on the Board, in compliance with Ofwat's corporate governance principles.

Appointments

There were three resignations and one appointment since 'licence award', as set out blow. Biographies of all the Directors in place at the year-end can be found on pages 39 to 43.

Director	Role	Appointment	Resignation
Norman Patrick Mitchell	Solicitor, initial company formation	21/04/2015	01/05/2015
David Wyles	Solicitor, initial company formation	24/04/2015	01/05/2015
Sir Neville Simms	Independent Non-Executive Director	19/08/2015	
Richard Morse	Independent Non-Executive Director	19/08/2015	
Anne Baldock	Independent Non-Executive Director	19/08/2015	
Mark Fairbairn	Independent Non-Executive Director	19/08/2015	
Michael Queen	Independent Non-Executive Director	19/08/2015	
Jaroslava Korpanec	Non-Executive Shareholder Director	01/05/2015	
Andrew Freeman	Non-Executive Shareholder Director	01/05/2015	17/03/2016
Alistair Ray	Non-Executive Shareholder Director	01/05/2015	
Gavin Tait	Non-Executive Shareholder Director	01/05/2015	
Moira Turnbull-Fox	Non-Executive Shareholder Director	17/03/2016	
Andy Mitchell	Executive Director	19/08/2015	
Mark Corben	Executive Director	19/08/2015	
Mark Sneesby	Executive Director	19/08/2015	

The Nominations Committee considers the desired experience and competencies of new Non-Executive Directors and reports these criteria to the Board before a decision is taken. During the year, the Board appointed one Non-Executive Director, Moira Turnbull-Fox, to replace Andrew Freeman as the DIF Shareholder Director.

All of the independent Non-Executive Directors were appointed on licence award for a three-year term. Each has confirmed that they are able to allocate sufficient time to the Company to discharge their responsibilities effectively. The independent Non-Executive Directors' terms and conditions of appointment are available for inspection upon request to the Company Secretary.

The Board (including the Company Secretary) has four women (from a total of 13), representing 31% of the total. The Executive Committee has two women from a total of nine members, representing 22% of the total. The Company's diversity policy, objectives and progress to date are set out in the Performance Review section of this Annual Report.

Conflicts of Interest

The Shareholders' Agreement and the Company's Articles of Association set out a process for identifying and managing actual or perceived conflicts of interest. The Company Secretary requests that all Directors complete a Declaration of Interest Form every six months and Directors are expected to raise any potential, actual or perceived conflicts as soon as they arise, so the Board can consider them at the next available opportunity. The Company Secretary holds a register of all declared interests and conflicts.

Development

On appointment to the Board and Committees, all Directors receive an induction tailored to their individual requirements. The induction, which is designed and arranged by the Head of Human Resources in consultation with the Chairman, includes meetings with Directors, senior management and key external advisors, to assist Directors in building a detailed understanding of how the Company works and the key issues it faces. Directors are also encouraged to visit construction/work sites, to see the Company's operations first hand. The Chairman periodically reviews and agrees with each Director their training and development needs. During the period, the Board received regular detailed presentations and updates from both staff and external advisors on specific topics, including engineering and system operations, consenting, NEC3 contracts, regulation, disclosure and governance. These sessions ensure that Non-Executive Directors have the knowledge and understanding of the business and the external legal and regulatory environment relevant to the Company to enable them to contribute effectively at Board meetings. All Board members participate in Company-wide HSSE training, as well as suitable training for site visits.

Information and Support

The Executive Directors regularly update the Board and Shareholders on key matters. Both the Board and its Committees have access to independent professional advice at the Company's expense, where it is necessary to discharge their responsibilities as Directors.

The Company Secretary advises the Chairman on all corporate governance matters.

Board Evaluation

An annual review of the performance of the Board and its Committees was conducted during the financial year by the Chairman and Company Secretary. This included meetings with the Shareholder Directors, the independent Non-Executive Directors and the Executive Directors. The Chairman and Company Secretary recorded the outcomes of the evaluation meetings and are working with the Chief Executive Officer to implement the agreed actions.

Going forward, it is intended that the annual review of Board and Committee performance will be externally facilitated every three years, in compliance with the Code. In other years, the review will be conducted at the end of the financial year, with each Director and Committee Chair completing a questionnaire issued by the Chairman of the Board and prepared by the Company Secretary. The roles, responsibilities and functions set out in the relevant terms of reference will be used in the process. The Chairman will report to the Board on the outcome of all Board and Committee reviews, with the analysis of the questionnaire providing topics on which to base a productive Board discussion. The evaluation process will capture agreed outcomes and clear timescales for implementation.

Board Leadership, Transparency and Governance

Board Committees

Board Committee Structure with each Board Committee chaired by an independent Non-Executive Director.

The Board has established six Board Committees, which are described in more detail in this section. The Committees' terms of reference are described in the following sections of this report. The Committees meet regularly during the year in accordance with an agreed schedule.

All Non-Executive Directors are permitted to attend Committee meetings, in addition to the Committee members. Each of the Committees has terms of reference, which have been approved by the Board. Each Committee's terms of reference and performance are reviewed by the Board each year, to ensure that the Committees operate effectively. The Board approves any changes to the terms of reference. The Chairs of each Committee provide regular updates to the Board on the Committee's work. Minutes of the Committee meetings are available to all Directors on a secure electronic portal.

Directors' attendance at Board and Committee meetings for the period from licence award on 24 August 2015, when the Board was formed, to year end, is summarised in the Table below.

	Board	Audit Committee	Risk Committee	HSSE Committee	Treasury Committee	Nominations Committee	Remuneration Committee
Total meetings held in period	9	2	1	1	3	1	3
Attendance by Director:							
Sir Neville Simms	9			1		1	3
Richard Morse	9	2	1		3	1	3
Anne Baldock	9	2			3	1	3
Mark Fairbairn	9		1	1	3		
Michael Queen	9	2	1		3		
Jaroslava Korpanec	9	2	1		3	1	2
Alistair Ray	9		1		3	1	3
Gavin Tait	8			1	3		3
Andy Mitchell	9	2	1	1	2		3
Mark Corben	9	2	1	1	3		
Mark Sneesby	8	2	1	1			
Attendance by Director appointed during the period:							
Moira Turnbull-Fox	1				1		1
Attendance by Director who resigned during the period:							
Andrew Freeman	7	1		1	1	1	

Note:
Whilst the Executive Directors are not formal members of the Board Committees, they are invited to attend the majority of meetings.

Board Leadership, Transparency and Governance
Board Committees

Committee members' attendance is set out in the attendance table on page 49.

AUDIT COMMITTEE

Membership of the Audit Committee 2015/16
Richard Morse (Chair)
Anne Baldock
Michael Queen
Jaroslava Korpanec
Andrew Freeman (resigned March 2016)
Moira Turnbull-Fox (appointed March 2016)

The Audit Committee reviews and reports to the Board on all matters relating to financial reporting, including the Company's published financial and regulatory statements, interim reports and related documents. It also reviews the role and independence of the auditors; the internal audit function; and the Company's overall compliance record. A majority of members of the Audit Committee are independent Non-Executive Directors.

The Audit Committee has prepared a separate report, which is presented on pages 58 to 63 of this report.

RISK COMMITTEE

Membership of the Risk Committee 2015/16
Mark Fairbairn (Chair)
Richard Morse
Michael Queen
Jaroslava Korpanec
Alistair Ray

The Risk Committee reviews and reports to the Board on risk management and internal control, including the determination of the nature and extent of the principal risks the Company faces. Details of our principal risks can be found in the Risk Management section. The Company also has an executive-level risk committee (the Executive Risk Committee), chaired by the CFO, which considers risk management matters in detail on a monthly basis. In a full financial year, the Risk Committee would be expected to meet at least three times or otherwise as required.

The Board Risk Committee is responsible for:

- overseeing the development, implementation and maintenance of the Company's overall risk management framework and its risk appetite, strategy, principles and policies, to ensure they are in line with emerging regulatory, corporate governance and industry best practice;
- reviewing the principal risks facing the Company, including those that would threaten its business model, future performance, solvency and liquidity, and making recommendations to the Board regarding formal sign-off of those principal risks set out within the Annual Report;
- reviewing the Company's systems of planning and internal control, to ensure they are adequate and in line with any guidelines published by Ofwat and revised from time to time;
- overseeing the Company's risk exposures, risk/return and proposed improvements to the Company's risk management framework;
- facilitating the effective contribution and involvement of Non-Executive Directors and aiding their understanding of risk issues and the Company risk management framework;
- providing input to the Remuneration Committee on the alignment of remuneration to risk performance;
- reviewing new risk principles and policy or material amendments to them recommended by the CEO and CFO, for approval by the Board;
- overseeing adherence to risk principles, policies and standards and any action taken resulting from material policy breaches across the Company, based upon reports from the CEO;
- reviewing the adequacy of the Company risk function's resources, and its authority and standing within the Company;
- reviewing co-ordination between the Company risk function and the external auditors;
- providing reports to the Board as appropriate; and
- periodically reviewing and updating its own terms of reference to reflect best practice, requesting Board approval for all proposed changes and, at appropriate intervals, evaluating its own performance against the terms of reference.

HEALTH, SAFETY, SECURITY AND ENVIRONMENT COMMITTEE (HSSE)

Membership of the HSSE Committee 2015/16
Mark Fairbairn (Chair)
Sir Neville Simms
Jaroslava Korpanec
Gavin Tait

The Company is committed to recognising HSSE standards and the use of best practice. The Company acknowledges that effective HSSE performance comes from the top and that members of the Board have both collective and individual responsibility for HSSE. Accordingly, the Board has established a Board level HSSE Committee to regularly review, develop and oversee consistent policy, standards and procedures for managing HSSE risks to the Company's business. The Company also has an executive-level HSSE committee, chaired by the COO, which considers HSSE matters in detail on a monthly basis. In a full financial year, the HSSE Committee would be expected to meet at least twice or otherwise as required. The HSSE Committee is responsible for:

- reviewing the HSSE strategy and objectives and recommending them to the Board;
- providing advice, assistance, recommendations and reports to the Board as required, to facilitate the Board's understanding, reviewing and monitoring of the Company's implementation of its HSSE strategy, including:
  - best practice comparator(s)
  - legal compliance
  - interface issues with stakeholders
  - third party and general public protection on site, abutting the site or off site (but resulting from programme delivery)
  - any issues and concerns raised by authorities, including proposals to address them, and
  - HSSE risk mitigation strategies;
- reviewing the Company's Integrated Management Systems relating to HSSE, to ensure legal compliance;
- analysing trends, including:
  - audits, inspections and safety tours carried out
  - third party audits carried out
  - non-compliance report analysis
  - incident and near miss analysis
  - reaction time and close out, and
  - occupational health analysis;
- reviewing and approving significant Company actions relating to HSSE;
- reviewing incident investigation reports and the close out of resulting actions for all incidents involving fatalities and any other serious incident as the Committee sees fit; and
- reviewing the Company's security policy, procedure and strategy.

NOMINATIONS COMMITTEE

Membership of the Nominations Committee 2015/16
Sir Neville Simms (Chair)
Anne Baldock
Michael Queen (appointed June 2016)
Richard Morse
Jaroslava Korpanec
Alistair Ray
Andrew Freeman (resigned March 2016)
Moira Turnbull-Fox (appointed March 2016)

The Nominations Committee, led by the Chairman of the Board, is responsible for Board recruitment, composition, evaluation and succession planning. A majority of members of the Nominations Committee are independent Non-Executive Directors.

The Nominations Committee is responsible for:

- regularly reviewing the structure, size and composition of the Board, including skills, knowledge, experience and diversity, and making recommendations to the Board with regard to any changes;
- considering succession planning for Directors and other senior executives, taking into account the challenges and opportunities facing the Company, and the skills and expertise needed on the Board in the future;

Board Leadership, Transparency and Governance
Board Committees

Committee members' attendance is set out in the attendance table on page 49.

- evaluating, before the Board makes any appointment, the balance of skills, knowledge, experience and diversity on the Board and, in the light of this evaluation, preparing a description of the role and capabilities required for a particular appointment. In identifying suitable candidates the Nominations Committee shall:
  - use open advertising or the services of external advisers to facilitate the search;
  - consider candidates from a wide range of backgrounds; and
  - consider candidates on merit and against objective criteria, with due regard for the benefits of diversity on the Board, including gender, and taking care that appointees have enough time available to devote to the position;
- requiring existing Directors to disclose any other business interests that could result in a conflict of interest;
- reviewing the results of the Board performance evaluation that relate to the composition of the Board; and
- reviewing annually the time required from Non-Executive Directors and using the results of the performance evaluation to assess whether the Non-Executive Directors are spending enough time to fulfil their duties.

The Nominations Committee also makes recommendations to the Board concerning:

- succession plans for both Executive and Non-Executive Directors and in particular for the key roles of Chairman and CEO;
- membership of the Audit and Remuneration Committees, and any other Board committees as appropriate, in consultation with the Chair of those Committees;
- the re-appointment of any Non-Executive Director at the conclusion of their specified term of office, having given due regard to their performance and ability to continue to contribute to the Board in the light of knowledge, skills and experience required; and
- any matters relating to the continuation in office of any Director at any time, including the suspension or termination of service of an Executive Director as an employee of the Company, subject to the provisions of the law and their service contract.

In a full financial year, the Nominations Committee would be expected to meet at least once or otherwise as required.

REMUNERATION COMMITTEE

Membership of the Remuneration Committee 2015/16
Anne Baldock (Chair)
Sir Neville Simms
Richard Morse
Mark Fairbairn (appointed June 2016)
Jaroslava Korpanec
Alistair Ray
Andrew Freeman (resigned March 2016)
Moira Turnbull-Fox (appointed March 2016)

The Board Remuneration Committee ensures that the Company's remuneration policy is designed with the Company's long-term success in mind and that performance-related elements are transparent, stretching and rigorously applied. A majority of members of the Remuneration Committee are independent Non-Executive Directors. The Remuneration Committee has prepared a separate report, which is presented on pages 64 to 71 of this report.

TREASURY COMMITTEE

Membership of the Treasury Committee 2015/16
Michael Queen (Chair)
Anne Baldock
Mark Fairbairn
Richard Morse
Jaroslava Korpanec
Alistair Ray
Gavin Tait
Andrew Freeman (resigned March 2016)
Moira Turnbull-Fox (appointed March 2016)

The Treasury Committee reviews and reports to the Board on the Company's Treasury Policy, treasury strategies and financial strategy. The Company also has an executive-level Funding and Financing Committee, chaired by the CFO, which considers treasury and regulatory matters in detail on a monthly basis. In a full calendar year, the Treasury Committee would be expected to meet at least three times or otherwise as required.

The Board Treasury Committee is responsible for:

- reviewing the Treasury Policy and presenting it to the Board for approval;
- reviewing the treasury strategies that support the implementation of the Treasury Policy and presenting them to the Board for approval;
- reviewing the annual Treasury business plan and presenting it to the Board for approval;
- monitoring Treasury performance;
- reviewing the result of the annual ratings process and any potential developments that may affect the Company's credit rating;
- approving any funding, hedging or investment contemplated in the approved Business Plan that is above the limits in the SoDA for individuals;
- reviewing and presenting to the Board any prospectus or other listing document required in relation to the issuance of any capital markets instruments or any formal information memorandum in relation to borrowing by any member of the Group that is not part of the approved Business Plan;
- reviewing and presenting to the Board any material change, amendment or variation to any of the Company's financing arrangements or any request for any waiver thereunder; and
- monitoring compliance with financial covenants set out in various legal agreements.

Tideway launches its Vision and Values to staff in April 2015

Board Leadership, Transparency and Governance
Relationship with Shareholders

OUR OWNERS

The Company is owned by a consortium of investors. Further information on our equity investors and their equity interests as at July 2016 are as summarised in the table below.

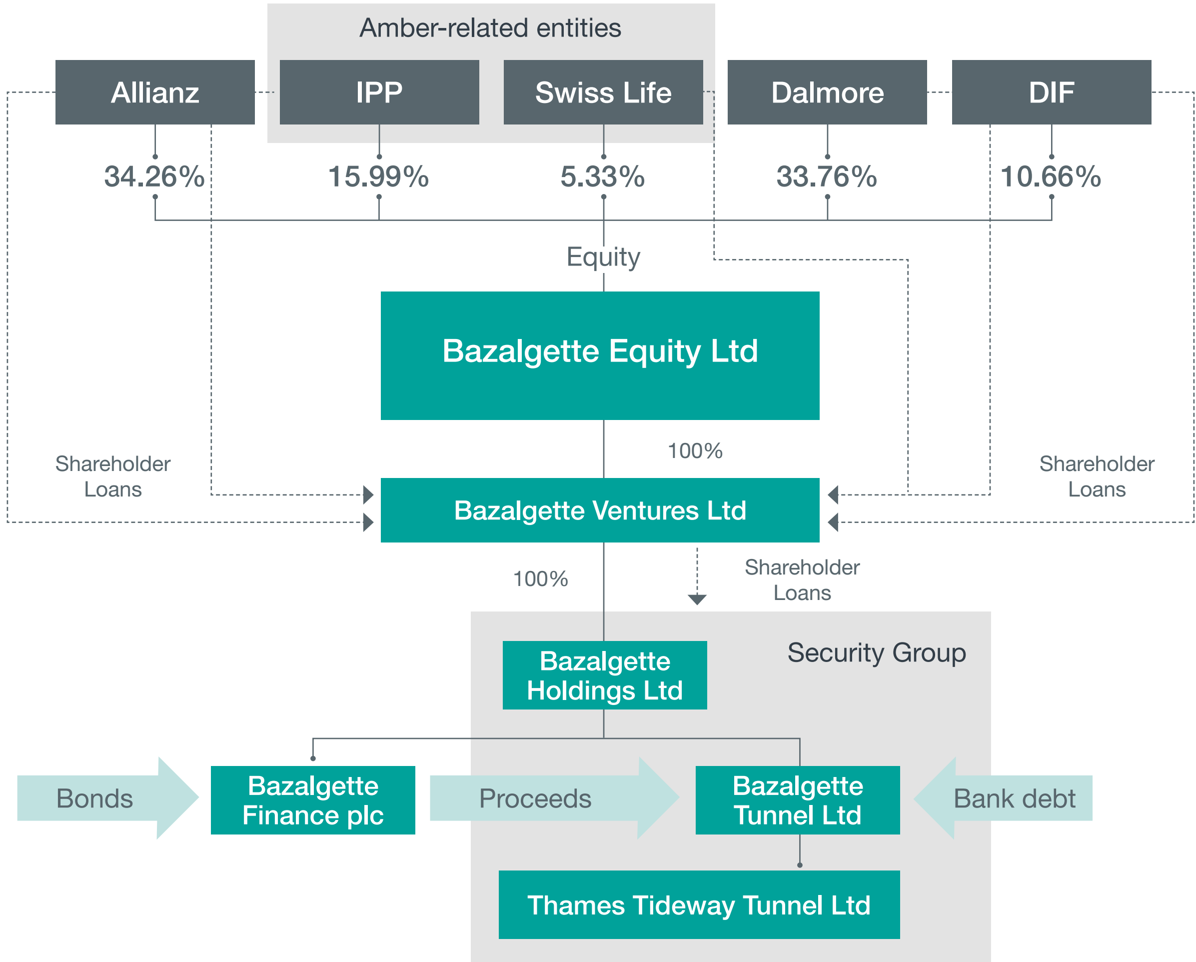
Shareholder and Shareholding	Description
Allianz Infrastructure Luxembourg I S.a.r.l. 34.26%	The Allianz Group is a leading global financial services group, active in insurance and asset management. It has assets under management in excess of €1.8 trillion and a market capitalisation of over €65bn. The investment in the Company is funded from the balance sheets of various Allianz Group insurance companies, with over 60% coming from the German life insurance business.
Dalmore Capital 14 GP Limited 33.76%	Dalmore is an independent fund manager based in London, with over £1.7bn of investors' funds under management. For the purpose of investment in the Company, Dalmore has established a single purpose fund which has secured commitments from some of the UK's leading pension funds, as well as from a number of European infrastructure investors.
IPP (Bazalgette) Limited 15.99% Bazalgette (Investments) Limited 5.33% (Both Amber related entities)	Amber is a developer, financial adviser and manager of infrastructure projects. It looks after funds for more than 2,000 public and private sector investors, and has assets under management of c. £5bn. It manages four infrastructure funds, including International Public Partnerships Limited (IPP), which is listed on the London Stock Exchange and has a market capitalisation of over £1.5bn. Amber manages the IPP and Swiss Life Holding AG (Swiss Life) investments in the Company, which are respectively held through IPP (Bazalgette) Limited and Bazalgette (Investments) Limited. Swiss Life is the largest life insurance company in Switzerland, with a market capitalisation of c. CHF 7bn.
DIF Bid Co Limited (UK) 10.66%	DIF is an independent fund management company with c. €3.2bn of funds raised. Through five investment funds, DIF invests in high-quality infrastructure assets that generate long-term, stable cash-flows, including Public Private Partnership projects (PPP/PFI/P3), renewable energy projects and other core infrastructure projects in Europe, North America and Australia. DIF Management Holding BV directly or indirectly owns and/or manages all of the DIF entities in the corporate structure above Bazalgette Equity Limited. DIF Management UK Limited is the topmost UK company in the DIF corporate structure. The source of DIF's share of equity funding for the project comprises long term pension fund, insurance and fund of funds investors.

The Company's Board includes five independent Non-Executive Directors (including the Chairman), which means that independent Directors are the largest single group on the Board. These appointments, together with the reserved matters requiring Board approval (see pages 56 to 57), help ensure that the Board is independent, in control of its business and able to operate sustainably.

The Shareholders' Agreement entered into on licence award contains legally binding commitments to maintain an independent Board and ensure the Company can make strategic and risk management decisions. The Shareholder Directors are the primary conduit by which the Board interacts with the shareholders and understands their views, both individually and collectively. The Shareholder Directors attend Board and Committee meetings (often supported by other investor representatives as observers). In addition, regular meetings and calls take place between independent and Executive Board members, involving one or more Shareholder Directors, which are a useful, less formal communication channel.

TIDEWAY GROUP STRUCTURE

Bazalgette Tunnel Limited is part of a group of companies. Its immediate parent company is Bazalgette Holdings Limited, which is in turn wholly owned by Bazalgette Ventures Limited, and its ultimate holding company is Bazalgette Equity Limited.



Structure of the Tideway group of companies.

Each shareholder controlling 10% or more of the ordinary shares of Bazalgette Equity Limited and loan notes of Bazalgette Ventures Limited is entitled to appoint one Director to the Boards of Bazalgette Equity Limited, Bazalgette Ventures Limited and Bazalgette Holdings Limited. Each shareholder controlling 20% or more of the ordinary shares of Bazalgette Equity Limited and loan notes of Bazalgette Ventures Limited is entitled to appoint a second Director to the Boards of Bazalgette Equity Limited, Bazalgette Ventures Limited and Bazalgette Holdings Limited.

Each shareholder controlling 20% or more of the ordinary shares of Bazalgette Equity Limited and loan notes of Bazalgette Ventures Limited is entitled to appoint one Observer to the Board of Bazalgette Tunnel Limited. Each shareholder controlling 30% or more of the ordinary shares of Bazalgette Equity Limited and loan notes of Bazalgette Ventures Limited is entitled to appoint a second Observer to the Board of Bazalgette Tunnel Limited. The Observers are entitled to attend Board and Committee meetings and to speak with the permission of the Chairman of the Board, but are not entitled to vote.

Board Leadership, Transparency and Governance *Continued*

SHAREHOLDER RESERVED MATTERS

There are a limited number of matters reserved by the Board for approval by shareholders. As set out in the tables below, these matters require the approval of shareholders holding either 75% or 90% of the Company's equity. Although these matters are reserved to the Shareholders, the Board would expect to express a view to the Shareholders before any decisions were taken.

Shareholder and shareholding	Description
General corporate	General corporate matters relating to the issue of any shares in any Tideway group company.
Incurring of commitments, liabilities etc.	Incurring of commitments, liabilities etc. unless contemplated by the annual Business Plan or Budget.
Acquisitions or disposals	Disposals, acquisitions and capital expenditure over £50 million or not contemplated by the annual Business Plan or Budget.
Accounts, auditor	The change of the company accounting reference date, the removal or appointment of auditor and any change to the accounting policies except where required as a consequence of a change in IFRS, GAAP or law.
Manner of carrying on business	Entering into or materially changing a material contract to the extent not contemplated by the annual Business Plan or Budget. Substantial alteration in the nature of the business or cessation of the business. Approval of or making amendments to the Project Licence, Business Plan or Budget, which would result in additional expenditure or indebtedness over £50 million. Entering into any guarantee in excess of £50 million. The appointment or removal of an Executive Director to the Board, as recommended by the Nominations Committee. The conduct of litigation and claims involving any Tideway group company where the potential liability may exceed £50 million. Any material submission or application to Ofwat, whether pursuant to the licence or otherwise. Any request that Ofwat refer a matter to the Competition and Markets Authority. The submission of any material tax claim, disclaimer, election or consent. The issuances or withdrawal of notices pursuant to the Government Support Package. The replacement of a Main Works Contractor, System Integrator or Project Manager during the Construction Period. The appointment of a Tideway representative to the Liaison Committee and any voting in relation to material variations to the scope of the project. The approval of or entry into a related party transaction.

Shareholder and shareholding	Description
Partnership, joint venture or other agreement	Entering into any partnership, JV or other profit sharing agreement in excess of the materiality threshold.
Articles and board composition	A change to the articles, acting contrary to the articles and a change to the Board composition requirements in the Shareholders' Agreement.
Share denomination	Any consolidation or re-denomination of any shares.
Share redemptions or buybacks	The redemption or purchase by Bazalgette Equity Limited, Bazalgette Ventures Limited or Bazalgette Holdings Limited of any share or the reduction of its share capital or any uncalled or unpaid liability in respect thereof, capital redemption reserve or share premium account.
Winding-up or liquidation	Any proposal for the winding-up or liquidation of Bazalgette Equity Limited, Bazalgette Ventures Limited or Bazalgette Holdings Limited.
Control of Bazalgette Equity Limited, Bazalgette Ventures Limited and Bazalgette Holdings Limited	Any arrangement whereby the directors no longer determine the general policy, scope of activity and operation or major decisions of Bazalgette Equity Limited, Bazalgette Ventures Limited and Bazalgette Holdings Limited.
Paying up of share capital or debentures	The paying up of any share capital or debenture or debenture stock of Bazalgette Equity Limited, Bazalgette Ventures Limited or Bazalgette Holdings Limited by way of capitalisation or application of any profits or reserves.
Schemes or arrangement and demergers	The proposal of any compromise or arrangement within the meaning of section 895 of the Companies Act 2006 or any arrangement pursuant to which Bazalgette Equity Limited, Bazalgette Ventures Limited or Bazalgette Holdings Limited is to make a distribution of the kind described in section 1075 of the Corporation Tax Act 2010.

Audit Committee Report

PURPOSE OF THE COMMITTEE

The Audit Committee's (the Committee) Terms of Reference include all matters covered by the Code. The Committee's main responsibilities are to examine any matters relating to the Company's financial affairs and to provide effective oversight and governance of the Company's internal control and risk management processes. The Committee's primary functions are shown below:

Function	Responsibilities
Financial and regulatory reporting	• To review, and challenge where necessary, the actions and judgements of management in relation to the Company's financial statements, operating and financial review, interim reports, half-yearly accounts, preliminary announcements and related formal statements before submission to, and approval by, the Board, and before clearance by the auditors. Particular attention should be paid to: • critical accounting policies and practices, and any changes in them; • decisions requiring significant elements of judgments; • the extent to which the financial statements are affected by any unusual transactions in the year and how they are disclosed; • the clarity of disclosures; • significant adjustments resulting from the audit; • the going concern assumption; • compliance with accounting standards; and • compliance with other legal requirements. • To review, and challenge where necessary, the actions and judgements of management, in relation to the Company's regulatory accounts before submission to, and approval by, the Board. • To review, and challenge where necessary, the actions and judgements of management, in relation to the Company's Risk and Compliance Statement before submission to, and approval by, the Board. • To review and challenge where necessary the actions and judgements of management, in relation to the Company's Compliance Certificate and Investor Report, before submission to and approval by the Board. • To review, and challenge where necessary, the actions and judgements of management, in relation to the Company's material financial and regulatory submissions to the Liaison Committee or any other external stakeholder, including but not limited to, those submissions which relate to any Remedy Event, Failure Event, Default or Trigger Event under the Financing Documents and Government Support Package. • To consider other topics, as defined by the Board.

Function	Responsibilities
Internal control and risk management	• To review the Company's procedures for detecting fraud and whistleblowing and ensure the arrangements are in place by which staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting, financial control or any other matters. • To review management's and the internal auditor's reports on the effectiveness of the systems for internal financial control, financial reporting and risk management. • To monitor the integrity of the Company's internal financial controls. • To review the statement in the Annual Report and accounts on the Company's internal controls and risk management framework. • To assess the scope and effectiveness of the systems established by management to identify, assess, manage and monitor financial and non-financial risks.
Internal audit	• To monitor and review the effectiveness of the Company's internal audit function, in the context of its overall risk management system. • To approve the appointment and removal of the Head of Internal Audit. • To review and assess the annual internal audit plan. • To review reports from the internal auditor to the Audit Committee. • To review and monitor the Executive Directors' reaction to the findings and recommendations of the internal auditor. • To meet the Head of Internal Audit at least once a year, without the Executive Directors being present, to discuss the remit and any issues arising from the internal audits carried out. • To ensure the Head of Internal Audit is given the right of direct access to the Chairman of the Board and to the Audit Committee.

Audit Committee Report
Continued

Function	Responsibilities
External audit	• To consider and make recommendations to the Board in relation to the appointment, re-appointment and removal of the Company's external auditor. The Audit Committee shall oversee the selection process for a new auditor and, if an auditor resigns, the Audit Committee shall investigate the issues leading to this and decide whether any action is required. • To review and monitor the external auditor's independence, objectivity and the effectiveness of the audit process, which shall include a report from the external auditor on its own quality procedures. • To oversee the relationship with the external auditor including (but not limited to): • recommendations on its remuneration, whether fees for audit or non-audit services, and that the level of fees is appropriate to enable an adequate audit to be conducted; • approval of its terms of engagement, including any engagement letter issued at the start of each audit and the scope of the audit; • satisfying itself that there are no relationships (such as family, employment, investment, financial or business) between the auditor and the Company (other than in the ordinary course of business); • monitoring the auditor's compliance with relevant ethical and professional guidance on the rotation of audit partner, the level of fees paid by the Company compared to the overall fee income of the firm, office and partner and other related requirements; and • seeking to ensure co-ordination with activities of the internal auditor. • To meet regularly with the external auditor, including once at the planning stage before the audit and once after the audit at the reporting stage. The Audit Committee shall meet the external auditor at least once a year, without the Executive Directors being present, to discuss the auditor's remit and any issues arising from the audit. • To review and approve the annual audit and ensure that it is consistent with the scope of the audit engagement. • To review the findings of the audit with the external auditor. This shall include: • a discussion of any major issues which arose during the audit; • any accounting and audit judgements. • levels of errors identified during the audit; and • the effectiveness of the audit. • To review the management letter and management's response to the auditor's findings and recommendations. • To develop and implement a policy on the supply of non-audit services by the external auditor, taking into account any relevant ethical guidance on the matter.

Function	Responsibilities
Compliance, whistleblowing and fraud	• To review the adequacy and security of the Company's arrangements for its employees and its contractors to raise concerns, in confidence, about possible wrongdoing in financial reporting or other matters. The Audit Committee shall ensure that these arrangements allow proportionate and independent investigation of such matters and appropriate follow-up action; • To review the Company's regulatory compliance; • To review the Company's procedures for detecting fraud; and • To review the Company's systems and controls for the prevention of bribery and receive reports on non-compliance.

The Committee's Terms of Reference are reviewed at least annually and referred to the Board for approval. A copy is available on the Company's website.

REVIEW OF THE YEAR

The Committee met twice in the seven-month period to 31 March 2016 and reported all of its activities to the Board. In a full calendar year, the Audit Committee would be expected to meet at least three times or otherwise as required.

As the Company was newly formed, the Audit Committee considered the following items:

- the Audit Committee terms of reference;
- the appointment of external auditors;
- the formation of the internal audit function;
- the appropriateness of the accounting policies;
- the approach to compliance and assurance; and
- the approach to annual reporting.

Membership and attendance

As at 31 March 2016, the Committee was chaired by Richard Morse, who is an independent Non-Executive Director, and comprised two additional independent Non-Executive Directors (Michael Queen and Anne Baldock) and two Shareholder Directors (Jaroslava Korpanec and Moira Turnbull-Fox). The Company Secretary is the secretary to the Audit Committee meetings.

Details of the Committee members' experience can be found in their biographies on pages 39 to 43.

All of the Directors of the Company have the right to attend the Committee meetings. The Company's Head of Internal Audit attends all meetings. The external auditor, KPMG, attended parts of meetings, to present the approach to the annual audit and the overall audit findings.

Significant Matters considered by the Committee in respect of the 2016 Financial Statements

As the Company was newly formed, the Audit Committee considered a range of significant issues in relation to the financial statements. These issues tended to relate to judgements and accounting estimates that management made in preparing the financial statements. In addition, as this was the Company's first year, the Committee considered the appropriateness of the accounting policies adopted for the period to 31 March 2016. For the period ended 31 March 2016, the Committee reviewed the following key areas:

- Analysis of accounting and tax considerations, in particular whether lease accounting was the most appropriate accounting framework during the construction period. Management has taken some external advice which helped conclude that lease accounting was most appropriate, as the Company controls the tunnel asset and that the project agreements contain a lease for accounting.
- Going concern – the Committee reviewed the evidence that supports the assumption that the accounts can be prepared on a going concern basis and in making the statement in the Directors' Report that the Company is a going concern. This included a review of the Company's liquidity, cash flows and exposure to financial, strategic and operational risks.

Audit Committee Report
Continued

Key stakeholders meeting regularly at the Thames Tideway Tunnel Forum

- Compliance with accounting standards and other legal requirements.

Internal control, risk and compliance

The Company has established an internal audit function that reviews the effectiveness of the Company's risk management and internal control system throughout the year, to ensure its adequacy. The Committee ensures that the Company achieves this through internal review, challenge and by considering the following:

- The adequacy of the Company's system of internal control, through the reports received from Internal Audit, management's response to the issues raised and their timely resolution.
- The control-related findings presented by the external auditor during its audit of the financial statements.
- The Company's approach to assurance, with its main requirements such as its licence, consents, financial obligations and other legal requirements.
- The overall assurance of the Annual Report and Accounts.
- The review of minutes from the Compliance Assurance and Review Group, which is chaired by the CEO and challenges relevant staff on compliance with key project obligations.
- The Company's approach and underlying process to assure the Board in relation to the Risk and Compliance Statement which is required in the Annual Report, under the licence granted by Ofwat.
- The policies and procedures in place to prevent, detect and investigate fraud.

Confidential reporting procedures and whistleblowing

As a newly formed company, the Company has sought to establish a culture of transparency and in implementing that it has developed a confidential whistleblowing policy and procedure for all staff. This has been widely advertised throughout the Company. It covers a wide range of areas where malpractice may occur, such as health and safety, fraud, bribery, money laundering and other human resource related matters. Staff are encouraged to deal with any matters of concern with line management first. Where this is not appropriate, the Company has set up a confidential whistleblowing reporting process with Crimestoppers.

The Head of Internal Audit acts as the Whistleblowing Officer, to monitor, investigate and report to the Committee on any concerns raised and the resulting outcome.

Internal Audit

The Company employs an independent Internal Audit team to carry out a number of risk-based reviews, giving the Committee assurance on the adequacy of the internal controls. The Head of Internal Audit is independent and reports functionally to the Chief Financial Officer but directly to the Chairman of the Audit Committee. The Head of Internal Audit regularly meets the Chairman of the Audit Committee without Executive Management being present.

To ensure Internal Audit's independence and effectiveness, the Committee reviewed, challenged and approved:

- the Internal Audit function's policy and strategy;
- the programme of work;
- the adequacy of the team's resources and skills;
- the reports received from the Head of Internal Audit outlining areas of weakness, including the adequacy of management's responses and the actions undertaken; and
- progress against the approved programme of work.

Through this monitoring, the Committee considers that Internal Audit is independent and effective.

Auditor appointment, independence and objectivity

During the year, the Committee approved the appointment and remuneration of the external auditor, KPMG, for the external audit of the financial statements and regulatory audit work for the period ended 31 March 2016. The fees for audit and non-audit services are reported on page 63.

During the period, the Committee considered:

- KPMG's planned approach to the audit of the financial statements;
- KPMG's execution of the audit approach, including its assessment of key accounting issues, audit judgements and audit adjustments required;
- the issues identified and management's response to the report covering internal control weaknesses identified during the external audit;
- KPMG's arrangements to identify, manage and report its own conflicts of interests;
- KPMG's independence and objectivity;
- the extent and impact on KPMG's independence, approval and quality of non-audit services carried out for the Company; and
- the arrangements for the day-to-day management of the audit relationship.

The Committee considers and approves the fees and activities for non-audit services carried out by KPMG. For the year ended 31 March 2016, the fees paid to KPMG for non-audit services were:

Fees paid to KPMG for non-audit services	£'000
Non-audit services (tax and accounting)	£55
Revenue Statement	£17

The Chairman of the Audit Committee has met with the KPMG engagement partner, to discuss matters without Executive management being present. The Committee concluded that it is satisfied with the independence of the auditor and the overall quality of the external audit process.

This report was approved by the Board of Directors on 21 June 2016.

Richard Morse
Chairman of the Audit Committee
at 31 March 2016

Remuneration Committee Report

STATEMENT BY THE CHAIR OF THE REMUNERATION COMMITTEE

On 24 August 2015, Tideway began operating as an independent regulated water company. For the period prior to that date the organisation operated as part of Thames Water. The Remuneration Committee's role and membership changed during this time. Whilst part of Thames Water, the Thames Tideway Tunnel Remuneration Committee carried out significant work to put in place proposed remuneration structures and strategies for the future organisation. With the creation of the new company, we have begun to develop these strategies to appropriately reflect Tideway's strategic drivers and targets.

The compensation detailed in this report is for the period from 24 August 2015 to 31 March 2016. The source data for standards of performance are held in company records.

Anne Baldock
Remuneration Committee Chair

Membership	Responsibilities
Anne Baldock Sir Neville Simms Richard Morse Jaroslava Korpanec (from August 2015) Alistair Ray (from August 2015) Gavin Tait (from August 2015) Andrew Freeman (from August 2015 to March 2016) Moira Turnbull-Fox (from March 2016) Mark Fairbairn (from June 2016)	• Set the remuneration policy for all Executive Directors and the Company's Chairman, including pension rights and any compensation payments. • Recommend and monitor the level and structure of remuneration for senior management. • Set and review the ongoing appropriateness and relevance of the remuneration policy. • Commission external benchmarking to obtain reliable, up-to-date information about remuneration in other companies of comparable scale and complexity. • Recommend the design of, and determine targets for, any performance-related pay schemes operated by the Company and recommend the total annual payments made under such schemes. • Recommend the policy for, and scope of, pension arrangements for each Executive Director and other designated senior executives. • Ensure that contractual terms on termination, and any payments made, are fair to the individual and the Company, that failure is not rewarded and that the duty to mitigate loss is fully recognised. • Oversee any major changes in employee benefits structures throughout the company.
Attendees	**Terms of reference**
The CEO attends the meetings for all business other than that relating to his own remuneration. Independent advisors attend meetings by invitation. The Head of HR or nominated deputy acts as Secretary to the Committee.	The Committee's full terms of reference have been approved by the Board and can be found on our website.

REMUNERATION POLICY REPORT

The Company's remuneration policy reflects the complexity and significance of one of Europe's largest infrastructure projects. We base annual bonuses on a combination of individual and key project milestones and company performance, to incentivise and reward success. As 2015/16 was a transitional year, there was no formal long-term incentive plan (LTIP) in place and the Company granted a deferred bonus, to recognise the Executive Directors' significant achievement during the year. Willis Towers Watson is appointed to provide salary and benefits benchmarking and consultancy to the Company.

Full details of each component of the Executive Directors' remuneration and the way remuneration was calculated, applicable for the period 24 August 2015 to 31 March 2016, are shown in the tables below.

Base salary	
Purpose and strategy	Fixed element to attract and retain Directors of the appropriate calibre, to reflect the organisation's size, complexity and external market competition.
Operation	Reviewed annually in April and normally fixed for 12 months. There is no right to an annual increase. Increases are based on: • individual performance; • internal and external comparators; and • market conditions.
Opportunity	Base salary increases are reviewed in the context of increases across the Company and will usually be in line with average increases. The Remuneration Committee will consider differences to this for the following reasons: • increase in scope or responsibility, including a promotion; • external market data showing that the salary is not competitive; and • the Remuneration Committee considering there to be a risk of not attracting or retaining executives.
Performance metrics	The individual's performance, external market and internal relativities will determine the salary level.

Remuneration Committee Report
Continued

Annual bonus	
Purpose and strategy	Incentivises and rewards performance against annual targets, which support the Company's strategic direction.
Operation	Annual targets included health, safety and wellbeing, regulatory compliance, customer value, shareholder return and project milestones, as well as individual targets. Targets are set annually by the Remuneration Committee and notified to the Board. The Committee approves the assessment of achievement and recommends it to the Board. All bonuses are discretionary and can be removed or adjusted at the Committee's discretion.
Opportunity	Maximum bonus opportunities are: CEO – 70%; CFO – 50%; COO – 50% Awards for 2015/16 were: CEO – 64%; CFO – 46%; COO – 46% The weighting of annual targets across each section were as follows:
Performance metrics	(see table below)

	Peformance measure		Weighting for 2015/16	Average achievement 2015/16
Overall company objectives 25%	Health, Safety and Wellbeing	Deliver transformational health, safety and wellbeing performance	6.25%	5.56%
	Regulatory compliance	Deliver good regulatory relationships and ensure full regulatory compliance	6.25%	6.25%
	Customer value	Deliver value for money to Thames Water customers, by timely and efficient delivery	6.25%	5.78%
	Shareholder return	Provide a reasonable return on the investments made by the private sector	6.25%	6.13%
Additional Executive Director objectives 50%	Finance plan	Ensure effective implementation, management and support of the proposed financing plan approved by the Board.	10.00%	10.00%
	Project milestones	Ensure contractors are on site and works commenced by March 2016, such that spend, and forecasts of milestones and spend, will be no less than that shown in the schedule relied upon by investors in making their bid	20.00%	20.00%
	Revised schedule	Agreed revised schedule of works (time and costs), which in turn will de-risk the programme	20.00%	17.40%
25%	Personal objectives	Achievement of personal objectives	25.00%	20.00%
		Total % of bonus pool	100.00%	91.12%

Annual bonus	
Performance metrics *Continued*	Regulatory compliance, health, safety and wellbeing, customer value and shareholder return are equally weighted and these targets are shared with all staff. Project milestones are linked to key project deliverables. The revised schedule targets refer to the agreement of an improved delivery programme with our Alliance partners. The finance plan details operational delivery of the financing plan. The Remuneration Committee has discretion to reduce the bonus to zero if there is a significant health and safety or regulatory breach. Personal objectives were a combination of strategic, project and development measures to support the creation of the new Company and delivery of the project.

In-service benefits	
Purpose and strategy	Ensures the overall package is competitive and supports the recruitment and retention of Directors.
Operation	Executive Directors receive benefits in line with market practice, which include car allowance, medical insurance and life insurance. Other benefits dependent on individual circumstances could include travel, accommodation or relocation allowances.
Opportunity	Benefits are determined at an appropriate level based on external market data and, in the case of other benefits, personal circumstances.
Performance metrics	Not applicable.

Retirement benefits	
Purpose and strategy	Ensures the overall package is competitive, within the pensions and taxation parameters, to provide post-employment benefits.
Operation	Executive Directors are eligible to participate in the Company's defined contribution pension scheme.
Opportunity	The Executive Directors have a fully portable Self Invested Personal Pensions.
Performance metrics	Not applicable.

Remuneration Committee Report
Continued

EXPLANATION OF PERFORMANCE METRICS CHOSEN

Tideway became a new independent regulated water company on 24 August 2015. Prior to licence award we developed Company and personal goals, to incentivise and reward the Executive Directors to successfully create the Company and manage critical milestones related to setting up and appointing the main works contractors and delivering pre-construction milestones.

Company targets, relating to regulatory compliance, health, safety and wellbeing, customer value and shareholder return were given a 50% weighting in calculating the potential bonus payment. In October 2015, the Board agreed to add three targets relating to 2015/16 project milestones, the revised schedule and the financing plan. We gave these additional targets a 50% weighting, reducing the original Company objectives and personal objectives to 25% each. This recognised the importance of reducing the cost and time of the project, to ensure value for money for Thames Water bill payers and less disruption to local communities during construction. Individual targets focus on all areas of the Company and project delivery, including community and stakeholder engagement, leadership, governance and employee engagement.

Deferred bonus

In lieu of a formal LTIP for 2015/16, the Remuneration Committee agreed to carry forward the deferred bonus scheme implemented when the project was part of Thames Water. This scheme applies only to the CEO, CFO and COO.

Deferred bonus	
Purpose and strategy	Reward and retention incentive, to recognise outstanding delivery in lieu of a formal LTIP.
Operation	Maximum Bonus opportunities are: CEO – 40% CFO – 30% COO – 30% Awards for 2015/16 were: CEO – 37% CFO – 28% COO – 28%
Performance Metrics	The deferred bonus was based on agreed milestones and project objectives for 2015/16. Payment is deferred until May 2017. The Remuneration Committee has discretion to reduce the deferred bonus to zero for health and safety or regulatory breaches.

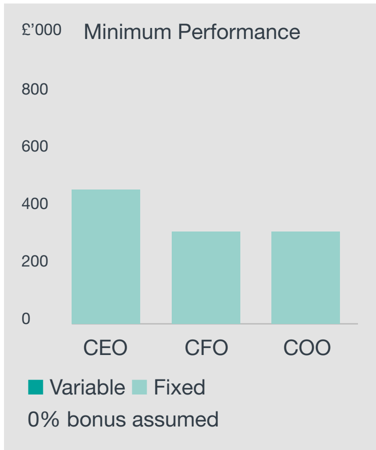
Tagets	Objectives	Weighting
Health, Safety and Wellbeing	Deliver transformational health, safety and wellbeing performance	12.50%
Regulatory compliance	Deliver good regulatory relationships and ensure full regulatory compliance	12.50%
Customer value	Deliver value for money to Thames Water customers, by timely and efficient delivery	12.50%
Shareholder return	Provide a reasonable return on the investments made by the private sector	12.50%
Finance plan	Ensure effective implementation, management and support of the proposed financing plan brought forward by shareholders	10.00%
Project milestones	Ensure contractors are on site and works commenced by March 2016, such that spend and forecasts of milestones and spend, will be no less than that shown in the schedule relied upon by investors in making their bid	20.00%
Revised schedule	Agreed revised schedule of works (time and costs), which in turn will de-risk the programme	20.00%

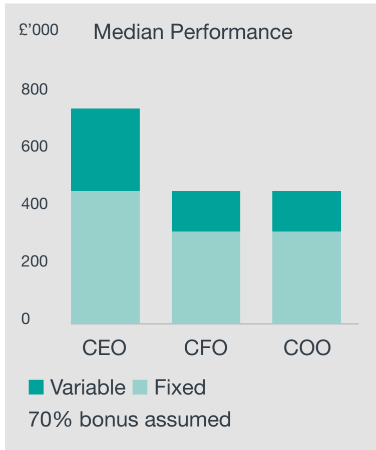
REMUNERATION SCENARIOS FOR EXECUTIVE DIRECTORS

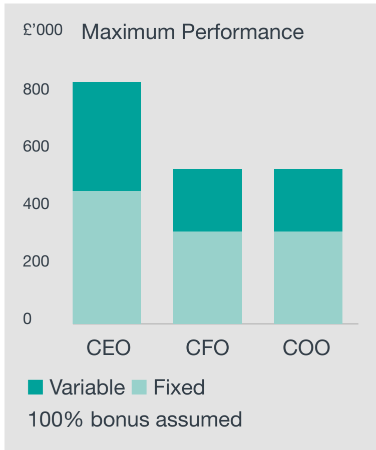
We have made the following assumptions in preparing the illustrations of potential remuneration for Executive Directors:

	Fixed pay	Annual bonus	Deferred bonus
Minimum performance	Fixed elements of remuneration are base salary, benefits and pension.	0 – 60%	0 – 60%
Median performance	Individual performance would be expected to have a positive impact on base salary – see pay and conditions for other employees	61 – 80% of potential annual bonus achieved	61 – 80% of potential deferred bonus achieved
Maximum performance		81 – 100% of potential annual bonus achieved	81 – 100% of potential deferred bonus achieved

The charts below show the relative split of remuneration between fixed (base salary, benefits and pensions) and variable elements (annual and deferred bonus) for each Director under the three scenarios described above.







Remuneration Committee Report
Continued

Non-Executive Director fees	
Purpose and strategy	Non-Executive Directors receive only a fee, which is set at a level that reflects market conditions and is sufficient to attract individuals with appropriate skills, knowledge and experience. The Chair and Deputy Chair receive enhanced fees for additional responsibilities. Non-Executive Directors representing shareholders do not receive fees from the Company.
Operation	Fees are reviewed either every year, on the change of responsibilities or the appointment of new Non-Executive Directors. The Board determines the remuneration of the Non-Executive Directors within the limits set in the Articles of Association.
Opportunity	Non-Executive Directors do not receive annual bonuses, benefits or pension contributions. Fees are based on the level of fees paid to Non-Executive Directors on the boards of comparable companies and the time commitment expected.

CONTRACTS

The Executive Directors have employment contracts with six months' notice on either side. The Directors who held office during the period are listed on page 46 of the Corporate Governance report.

The Independent Non-Executive Directors have service contracts with three months notice on either side. Details of their appointment to the Board can be found on page 46 of the corporate governance report.

REMUNERATION

Period ended 31 March 2016[1]	Base salary and fees £'000	Taxable benefits £'000	Annual bonus £'000	Deferred bonus £'000	Pension contribution[2] £'000	Total £'000
Andy Mitchell	215	8	138	80	43	484
Mark Corben	157	6	72	44	24	303
Mark Sneesby	157	7	72	44	5	285
Sir Neville Simms	166					166
Richard Morse	56					56
Anne Baldock	33					33
Mark Fairbairn	33					33
Michael Queen	33					33

Notes

1. Directors pay presented in this table covers the period from licence award on 24 August 2015 to the 31 March 2016.

2. Pensions include cash allowances paid in lieu of company contributions to the following directors: Andy Mitchell (£32,167), Mark Corben (£23,219).

The table shows the total remuneration earned by each Director in 2015/16. Annual and deferred bonuses were earned in line against targets detailed on pages 66 and 68. There are no comparators for the previous year, as the organisation was not previously trading. Fees for the Independent Non-Executive Directors have been set in line with the policy described, and were last reviewed in August 2015.

PAY AND CONDITIONS FOR OTHER EMPLOYEES

Whilst Tideway is a regulated independent water company, we recognise that a number of unique characteristics influence our remuneration strategy, not least that we are implementing one of Europe's largest infrastructure projects. We therefore have an element within the overall compensation structure, which is designed to ensure that the Company remains an employer of choice and to attract and retain appropriate skills, experience and talent. It is important for the project's success, and in particular candidates for new roles, that we offer an attractive overall compensation package.

We apply this compensation strategy consistently across all employees, from junior members of staff through to the senior management team, with the same principles of fairness and equity, as detailed below:

- Remuneration packages reflect the complexity and significance of one of Europe's largest infrastructure projects.
- Reward is based on total compensation, meaning base, bonus and benefits.
- Future increases in base pay are merit based, with no right to annual increases – though an annual review will take place.
- Bonuses are discretionary, based on a combination of individual and company performance, and are a key part of the package to incentivise and reward project success.
- Pensions will be contributory into a defined contribution scheme, with contributions in line with market practice.
- All employees have a base level benefits package (covering holidays, pension, life insurance and private medical cover). Additional benefits are provided based on job level (such as car allowances and enhanced pension) or personal circumstances (such as relocation allowance).

In January 2016, the Remuneration Committee agreed the following changes to improve the attractiveness of the overall compensation and benefits package;

- annual holiday allowance increased to 30 days;
- private medical insurance (single cover) for all employees (previously only for senior professionals and above); and
- annual bonus participation for those not previously eligible.

Tideway has no collective agreements in place and increases are determined based on an individual's performance, internal and external relativities. We carry out external benchmarking each year, to review market changes in remuneration. The first employees of Thames Tideway Tunnel Ltd (which was part of Thames Water) joined in May 2014, with the first salary increases awarded in October 2015 for individuals who had been with Thames Tideway Tunnel Ltd for 12 months or more. The overall salary increase pot was 3%. Future annual increase reviews will take place in April each year.

The Remuneration Committee takes into account the same criteria for the annual pay award for employees when considering any increase to base pay for Executive Directors. All employees who are eligible for an annual bonus share the same Company-wide targets and have individual objectives set in the same way as those of the Executive Directors.

RECRUITMENT REMUNERATION POLICY

We use the policy detailed above when deciding on the overall remuneration package for externally-recruited Directors. If necessary, to facilitate the hiring of individuals of the right calibre and experience, the Committee has the discretion to include other components outside of the policy.

Anne Baldock
Chair of the Remuneration Committee
21 June 2016

Directors' Report

The Directors present their report and the audited Group and Company financial statements of Bazalgette Tunnel Limited ("the Company") for the 11-month period ended 31 March 2016

Ownership and relationship with associated Companies

Bazalgette Tunnel Limited is owned by a consortium of UK-led investors. These investors include Dalmore Capital 14 GP Limited, Allianz Infrastructure Luxembourg I S.a.r.l, IPP (Bazalgette) Limited, Bazalgette (Investments) Limited and DIF Bid Co Limited (UK). Further information on our equity investors and their equity interests are set out on pages 54 to 55 of the Corporate Governance report.

Principal activities

The Group's business is to design, build and maintain the Thames Tideway Tunnel. A full explanation of the Group's principal activities is set out on pages 16 to 17 of the Strategic report.

Corporate Governance

Full disclosure on the Group's Corporate Governance activities is set out on pages 37 to 57 of the Corporate Governance report and is incorporated by reference into this Directors' report. Further details can also be found online at www.tideway.london

Financial results and dividends

Following the Group's accounting policies, all costs that meet the capitalisation criteria are capitalised and all income received is recognised as deferred income. This accounting treatment is expected to continue throughout the construction phase. The accounting policies are set out on pages 84 to 86 of the Financial Statements.

The Company and the Group recorded £nil profit for the 11-month period ended 31 March 2016. The detailed financial results of the Group are set out in the Financial Review within the Strategic report on pages 32 to 33. The Company did not pay any dividends in the 11-month period ended 31 March 2016.

During the period, £8.3m of shareholder loan interest was accrued on the shareholder loan notes. At 31 March 2016, £7.4m of the accrued shareholder loan interest had been paid and £0.9m rolled up within the shareholder loans. The shareholder loan notes bear an interest rate of 8%, with maturity on 30 September 2064. Further details of the shareholder loan notes are set out on note 12 of the Financial Statements.

Financial risk management

Full disclosure on the Group's financial risk management is set out on page 93 of the financial statements.

Directors

The Directors who held office during the period are listed on page 46 of the Corporate Governance report.

Directors' Indemnities

The Group has had in place Directors and Officers Liability insurance for the period.

Employees

The Group has 108 employees as at 31 March 2016. These are all employed by Thames Tideway Tunnel Limited which the Company has access to via the Management Services Agreement with Thames Tideway Tunnel Limited. The Company does not employ any staff directly. Details relating to the Group's employment policies and values are set out on pages 27 to 28 of the Strategic Report.

Greenhouse gas emissions

The Group's approach to identifying and reducing its greenhouse gas emissions is set out in the Strategic report on page 31.

Charitable and political donations

The Group made charitable donations totalling £500. Details of the Group's charitable partnerships are set out on pages 30 to 31 of the Strategic report. The Group did not make any political donations or incur any political expenditure during the year.

Payment to suppliers

Settlement terms are agreed with suppliers as part of the contract terms and the Company's policy is to pay in accordance with these terms. Other creditors are paid in accordance with invoice terms.

The Group, along with its Main Work Contractors, has signed up to the Fair Payment Charter. The Charter applies to all construction contracts with the aim of helping to create a more collaborative culture and ensure a strong, resilient and sustainable supply chain. The Charter's ambition for 2025 is that the construction industry's standard payment terms are 30 days and that retentions are no longer withheld.

The creditor days for the period ending 31 March 2016 are approximately 18 days.

Events occurring after the reporting period

Details of any events occurring after the reporting period are included in note 20 of the financial statements.

Going concern

The Directors believe, after due careful enquiry, that the Company and Group have sufficient resources to continue in operational existence for the foreseeable future and, therefore, consider it appropriate to adopt the going concern basis in preparing the 2016 financial statements.

Disclosure of information to auditor

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

Other information

An indication of likely future developments in the business and particulars of significant events which have occurred since the end of the financial year have been included in the Strategic Report on page 29.

Auditor

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

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

The Directors are responsible for preparing the Annual Report and the group and parent company financial statements in accordance with applicable law and regulations. Company law requires the directors to prepare group and parent company financial statements for each financial year. Under that law they have elected to prepare the group and the parent company financial statements in accordance with IFRSs as adopted by the EU and applicable law. Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and parent company and of their profit or loss for that period. In preparing each of the group and parent company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the group and the parent company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent company's transactions and disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect fraud and other irregularities.

The Directors have decided to prepare voluntarily a Directors' Remuneration Report in accordance with Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 made under the Companies Act 2006, as if those requirements were to apply to the Company. The Directors have also decided to prepare voluntarily a Corporate Governance Statement, as if the company were required to comply with the Listing Rules and the Disclosure Rules and Transparency Rules of the Financial Conduct Authority in relation to those matters.

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

We consider the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

A Mitchell
Director

The Point
37 North Wharf Road
London
W2 1AF
21 June 2016

Registered company number is 09553573

A guided tour through London's sewers

Long Term Viability Statement

The UK Corporate Governance Code requires company directors to state whether they have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over a long-term period.

In order to assess the long-term viability of the Company, the Board has taken a number of steps. It has:

- identified the most appropriate period over which to make the assessment;
- evaluated the Company's current position and future prospects; and
- considered the potential impact of principal risks over the period and, where appropriate, undertaken analysis of the potential financial impact under a suitable set of sensitivities.

The Board considers that it is most appropriate to assess the Company's viability over the eight-year period to the expected handover of the tunnel to Thames Water in 2024, under the programme schedule consistent with the regulatory baseline. This period aligns with the Company's planning horizon, as well as with the life of most of the risks facing the Company, as by the date of handover we will have retired the majority of the risks relating to constructing and financing the tunnel. The Board is not aware of any specific relevant factors that would affect this statement beyond this period and therefore has no reason to believe the Company will not be viable over a longer period. However, for the reasons set out above, the Board considers it reasonable to assess the Group's viability to 2024 for the purposes of this statement.

The viability of the Company has been assessed taking into account Tideway's business and financing plans, which are prepared as part of an annual planning process. These plans are consistent with the Company's performance since Ofwat granted its licence in August 2015 and with its financial position at the end of the financial year. The plans and projections we prepare as part of our corporate planning process consider the Group's committed funding and liquidity position, our forecast future funding requirements, the stability provided by our regulatory framework and the Government Support Package, key financial metrics, and our credit ratings.

Where appropriate during the course of the year, we conduct sensitivity analysis on our financial model to stress-test the resilience of the Group and its business model to the potential impact of the Group's principal risks, or a combination of those risks. For the purposes of this assessment of long-term financial viability, we have considered the likely impact of each principal risk on the company's viability, taking into account the availability and effectiveness of risk mitigation plans and the measures we could realistically take to avoid or reduce the impact or occurrence of the underlying risks. In considering the likely effectiveness of such actions, we take into account the Board's regular monitoring and review of risk management and internal control systems.

The Board confirms that its assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency and/or liquidity, and which are set out in the Risk Management section on pages 22 to 25, was robust.

A number of scenarios have been modelled to assess the potential impact of the principal risks, with many of the risks modelled as delays to delivery and/or cost overruns. Forecast RPI, financing costs and the speed of revenue collection have been sensitised as appropriate. We have also carried out sensitivities on the execution of the Group's financing plan.

The outcome of the sensitivities has been assessed considering a range of different financial ratios. In all downside scenarios modelled, ratios are robust and in excess of minimum requirements under the Company's financing covenants.

In reaching its conclusion, the Board has assumed that there will not be changes to the current regulatory framework or impact from the result of the referendum on the UK's membership of the European Union that will impact the Company's viability, and that financing will be available to Tideway over the period covered by the analysis.

A range of assurance activities have been undertaken, which the Board considers provide a robust degree of assurance over the analysis. This long-term viability statement has been reviewed by KPMG as part of the statutory audit. The Board considers that this combination of internal and external assurance activities means that checks have been carried out by parties with the appropriate skills and knowledge.

On the basis of the robust assessment of our principal risks, and on the assumption that we manage or mitigate them in the ways disclosed, the Board's review of the business plan and other matters considered and reviewed during the year, and the results of our sensitivity analysis and assurance described above, the Board has a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the period to the expected handover date in 2024.

Financial Statements

For the 11-month period ended 31 March 2016
Registered number 09553573

78 Independent Auditor's Report

80 Financial Statements

84 Notes to the Financial Statements

Kristiana Thomas, a yoga instructor and stand-up paddle boarder from Buckinghamshire, combines her life's passions on the Thames in west London. She is part of a growing community of enthusiasts taking to the river to enjoy this new sport.

Financial Statements
Independent Auditor's Report

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF BAZALGETTE TUNNEL LIMITED ONLY

Opinions and conclusions arising from our audit

1 Our opinion on the financial statements is unmodified

We have audited the financial statements of Bazalgette Tunnel Limited for the period ended 31 March 2016 set out on pages 80 to 94. In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 March 2016 and of the Group's result for the period then ended;
- the group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and 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.

2 Our assessment of risks of material misstatement

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

Completeness and existence of capitalised costs and creditors - costs £161.2 million, creditors £28.4 million

Refer to page 78 (Audit Committee Report), pages 84 to 86 (accounting policy) and pages 87 to 94 (financial disclosures)

- ***The risk*** - The Group has a substantial capital programme which has been agreed with the Water Services Regulation Authority ('Ofwat') and therefore incurs significant annual expenditure in relation to the construction of the wastewater infrastructure asset. All costs incurred are capitalised as assets under construction. Due to the significance of these costs, their completeness and existence is considered a significant risk, in particular the inclusion of purchases around the year end in the correct period.
- ***Our response*** - Our procedures included testing controls over the authorisation of invoices from main works contractors as well as other purchase invoices. We inspected the content of a sample of invoices around the year end to consider the timing of work performed and therefore appropriate recognition of costs in the year. We also inspected a sample of invoices received during the year to assess the existence of amounts capitalised.

We also considered the adequacy of the group's disclosures in this area.

Current and deferred tax charges - £nil

Refer to page 78 (Audit Committee Report), page 86 (accounting policy) and page 89 (financial disclosures)

- ***The risk*** – Tax accounting is an area of complexity. The current and deferred tax treatment in the period, dependent upon the judgement that the terms under which the wastewater infrastructure asset will be leased upon completion, which are already set, will be classified as a finance lease, is an area of judgement for the group. There is also a risk that the tax authorities will challenge the tax consequences of that accounting treatment and therefore that the tax accounting in the current year is inappropriate.
- ***Our response*** – Our procedures included considering the appropriateness of the expected future accounting treatment as a finance lease, in line with the current accounting requirements and any expected future changes to those requirements. With the help of our tax specialists we critically assessed the group's judgements in relation to the resultant tax consequences with reference to the relevant tax law. We also considered the adequacy of the Group's disclosures in this area.

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

Materiality for the Group financial statements as a whole was set at £1.5m, determined with reference to a benchmark of gross expenditure in the year, of which it represents 0.93%.

We reported to the Audit Committee any corrected or uncorrected identified misstatements exceeding £75,000, in addition to other identified misstatements that warranted reporting on qualitative grounds. Of the Group's two components, we subjected both to audit for group reporting purposes, The audit work on all components was performed by the group audit team. The component materialities ranged from £1,000 to £1.1m, having regard to the mix of size and risk profile of the Group across the components.

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

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

- the part of the Directors' Remuneration Report which we were engaged to audit has been properly prepared in accordance with Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 made under the Companies Act 2006, as if those requirements were to apply to the company; and
- 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.

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

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

- the directors' statement of long term viability on page 75, concerning the principal risks, their management, and, based on that, the directors' assessment and expectations of the Group's continuing in operation over the eight years to 2024; or
- the disclosures in the financial statements concerning the use of the going concern basis of accounting.

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

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

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

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

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

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

- the directors' statements, set out on pages 72 to 73, in relation to going concern and longer-term viability; and
- the part of the Corporate Governance Statement the Annual Report relating to the company's compliance with the eleven provisions of the 2014 UK Corporate Governance Code specified for our review.

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

Scope and responsibilities

As explained more fully in the Directors' Responsibilities Statement set out on page 73, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate. This report is made solely to the company's members as a body and is subject to important explanations and disclaimers regarding our responsibilities, published on our website at www.kpmg.com/uk/auditscopeukco2014b, which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

John Luke (Senior Statutory Auditor)
for and on behalf of KPMG LLP,
Statutory Auditor
Chartered Accountants
15 Canada Square,
London, E14 5GL
30 June 2016

Financial Statements

GROUP INCOME STATEMENT

For the 11 month period ended 31 March 2016

	Note	2016 £m
Net Operating Costs	4	–
Operating result		**–**
Net financing costs	5	–
Profit on ordinary activities before tax		**–**
Taxation	6	–
Result for the period		**–**

GROUP STATEMENT OF OTHER COMPREHENSIVE INCOME

For the 11 month period ended 31 March 2016

	2016 £m
Result for the period	–
Other comprehensive income for the period	–
Total comprehensive income for the period attributable to owners of the Company	**–**

GROUP AND COMPANY STATEMENT OF FINANCIAL POSITION

At 31 March 2016

	Note	2016 Group £m	2016 Company £m
Non-current assets			
Property, plant and equipment	8	161.2	161.2
Trade and other receivables	9	54.9	54.9
		216.1	216.1
Current assets			
Trade and other receivables	9	25.3	25.3
Cash and cash equivalents	10	112.9	112.9
Short-term deposits	10	17.5	17.5
		155.7	155.7
Total assets		**371.8**	**371.8**
Current liabilities			
Trade and other payables	11	(28.4)	(28.4)
		(28.4)	(28.4)
Non-current liabilities			
Borrowings	12	(205.1)	(205.1)
		(205.1)	(205.1)
Total liabilities		**(233.5)**	**(233.5)**
Net assets		138.3	138.3
Equity attributable to equity holders of the parent			
Share capital	13	138.3	138.3
Total equity		**138.3**	**138.3**

Notes 1 to 20 form an integral part of these financial statements

These financial statements were approved by the Board of Directors on 21 June 2016 and were signed on its behalf by:

M Corben
Director

Company registered number: 09553573

Financial Statements
Continued

GROUP AND COMPANY STATEMENT OF CHANGES IN EQUITY

	Share capital £m	Total equity £m
Balance at 21 April 2015	**–**	**–**
Profit or loss	–	–
Other comprehensive income	–	–
Total comprehensive income for the period	**–**	**–**
Transactions with owners recorded directly in equity:		
Issue of ordinary shares	138.3	138.3
Total contributions by, and distributions to, owners	**138.3**	**138.3**
Balance at 31 March 2016	**138.3**	**138.3**

GROUP AND COMPANY CASHFLOW STATEMENTS

For the 11 month period ended 31 March 2016

	Note	Group 2016 £m	Company 2016 £m
Cash flows from operating activities before working capital movements		**–**	**–**
Increase in trade and other receivables	9	(80.2)	(80.2)
Increase in trade and other payables	11	28.4	28.4
Cash used in operations		**(51.8)**	**(51.8)**
Net cash used in operating activities		**(51.8)**	**(51.8)**
Cash flows used in investing activities			
Construction of infrastructure asset		(160.3)	(160.3)
Short-term deposits		(17.5)	(17.5)
Net cash used in investing activities		**(177.8)**	**(177.8)**
Cash flows from financing activities			
Proceeds from the issue of share capital	13	138.3	138.3
Proceeds from shareholder loans		207.4	207.4
Repayment of shareholder loan principal		(3.2)	(3.2)
Net cash from financing activities		**342.5**	**342.5**
Net increase in cash and cash equivalents during the period		**112.9**	**112.9**
Cash and cash equivalents at 21 April 2015	10	–	–
Cash and cash equivalents at 31 March 2016	10	**112.9**	**112.9**

Financial Statements
Notes to the financial statements

1 ACCOUNTING POLICIES

Basis of preparation

Bazalgette Tunnel Limited (the "Company") is a company incorporated on 21 April 2015 and domiciled in the UK. The accounting policies set out below have been applied consistently to all periods presented in these Group and parent Company financial statements.

The Bazalgette Tunnel Group comprises the Company and Thames Tideway Tunnel Limited (TTT). The Group financial statements consolidate those of the Company and its subsidiary (together referred to as the "Group").

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

The Group and the Company financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU ("Adopted IFRSs").

Where items are sufficiently significant by virtue of their size or nature, they are disclosed separately in the Financial Statements in order to aid the reader's understanding of the Group and the Company's financial position.

In the process of applying the Group's accounting policies, the Group is required to make certain judgements, estimates and assumptions that it believes are reasonable based on the information available. The Directors consider that the significant judgements made in the application of these accounting policies that have significant effect on the financial statements and estimates and a risk of material adjustment to the carrying amounts in the next year are as follows:

Impairment – In assessing the recoverable value of the Thames Tideway Tunnel asset, the Directors are required to make judgements around the assumptions used to calculate the recoverable amount. The assumptions include RPI, for which an average of independent forecasts is used.

Basis of consolidation

Subsidiaries

Subsidiaries are entities controlled by the Group. The Group controls an entity when it 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. In assessing control, the Group takes into consideration potential voting rights that are currently exercisable. The acquisition date is the date on which control is transferred to the acquirer. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Measurement convention

The financial statements are prepared in accordance with the historical cost accounting convention except where adopted IFRSs require an alternative treatment.

Property, plant and equipment

Recognition and measurement

Property, plant and equipment comprises assets under the course of construction and fixtures and fittings.

Additions to assets under construction represent the capitalised costs of project expenditure by the Group.

The construction phase of the Thames Tideway Tunnel project commenced in 2015 and is expected to be completed at the System Acceptance date. During the construction phase of the project, expenditure which is directly attributable to bringing the Thames Tideway Tunnel asset into its working condition for its intended use will be capitalised within assets under construction. The Directors consider that the Group is constructing one asset, that being the Thames Tideway Tunnel, and do not consider there to be other individual assets under construction.

The Directors consider all expenditure in the period ended 31 March 2016 to have met the capitalisation criteria. Assets under construction are measured at cost less any accumulated impairment losses.

Land and Property acquired for the Thames Tideway Tunnel project is not included in the Statement of Financial Position because all acquisitions are made by Thames Water.

Depreciation

Assets under construction are not depreciated. Fixtures and fittings are depreciated over 5 years.

Intangible assets

Intangible assets represent software assets that were transferred to the Group on the acquisition of TTT.

Software costs are measured at cost less accumulated amortisation and accumulated impairment charges.

Amortisation is capitalised on a straight-line basis over the estimated useful life of the assets from the date they are available for use, unless such assets' lives are indefinite.

Borrowing costs

Borrowing costs that are directly attributable to the acquisition, construction or production of qualifying assets are added to the cost of those assets, until such time that those assets are ready for their intended use. A qualifying asset is defined as an asset that necessarily takes a substantial period of time to get ready for its intended use or sale, a substantial period of time interpreted as being greater than one year.

Impairment

The Directors consider assets under construction to consist of a single asset, the Thames Tideway Tunnel. As such, impairment is considered in the context of the whole asset under construction as opposed to review of individual components.

The carrying value of the Group's asset under construction is reviewed at each reporting date, to determine whether there is objective evidence the asset is impaired. The Directors consider the asset to be impaired if the forecast carrying value of the asset at System Acceptance exceeds the forecast recoverable value of the asset at System Acceptance.

For other financial and non-financial assets, the Group reviews the individual carrying amount of those assets to determine whether there is any indication of impairment in those assets. If any such impairment exists, the recoverable amount of the asset is calculated in order to determine the extent of any impairment loss. Impairment losses are recognised in the Income Statement.

Revenue and bad debt risk

The Group's revenue for each financial year is determined by arrangements set out in its licence granted by Ofwat. During the construction period of the Thames Tideway Tunnel, the primary component of revenue is the regulated return on the Company's Regulated Capital Value (RCV). The Company's Allowed Revenue is notified to Thames Water, which bills and collects this revenue from its wastewater customers and passes this through to BTL. Through the construction period, revenue is deferred as the services associated with this revenue will not be delivered until System Acceptance. Revenue is accrued in the period it has been earned, if it has not been invoiced by BTL to Thames Water. Revenues that have been invoiced and collected from Thames Water are treated as an advance payment liability.

In determining the accrued revenue earned in the period, the Directors consider the value of revenues that will not be recovered through bad debt risk and subsequently the accrued revenue in the Statement of Financial Position is adjusted to reflect this.

Invoiced revenues reflect the actual cash collected by Thames Water from its customers and as such the bad debt risk is considered to be very low.

Employee benefits

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which the Company pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are capitalised in the period which services are rendered by employees.

Other employee benefits

Other short and long-term employee benefits are measured on an undiscounted basis and are recognised as an expense over the period in which they accrue.

Provisions

A provision is recognised in the Statement of Financial Position when the Group has a present legal or contractual obligation as a result of a past event, which can be reliably measured and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are recorded at management's best estimate of the consideration required to settle the obligation at the Statement of Financial Position date.

Operating leases

Payments made under operating leases are capitalised in assets under construction on a straight-line basis over the term of the lease, provided they meet the capitalisation criteria for assets under construction.

Financial instruments

Financial assets and liabilities within the scope of IAS 39 Financial Instruments: Recognition and Measurement ("IAS 39") are classified as non-derivative financial instruments. Non-derivative financial instruments comprise trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables.

The Company determines the classification of financial instruments at initial recognition and evaluates this designation at each financial year end. ›

The initial and subsequent measurement of financial instruments depends on their classification as follows:

Trade and other receivables
Trade and other receivables are recognised initially at fair value. Subsequent to initial recognition they are measured at amortised cost.

Cash and cash equivalents
Cash and cash equivalents comprise cash at bank and in hand balances and short-term deposits with a maturity at acquisition of three months or less. Cash equivalents are readily convertible to a known amount of cash and subject to an insignificant risk of change in value.

Short-term cash deposits disclosed in the Statement of Financial Position comprise cash deposited with a maturity of greater than three months on acquisition, a fixed interest rate and which do not constitute cash equivalents under IAS 7 'Statement of cash flows'.

Interest-bearing borrowings
Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost.

Taxation
Tax on the profit or loss 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 directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years. Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse using tax rates enacted or substantively enacted at the reporting date. A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets and liabilities are disclosed net to the extent that they relate to taxes levied by the same tax authority and the Company has the right of set off.

Recently issued accounting standards

The following new and revised IFRSs will be applicable in future periods, subject to endorsement by the EU, and have not been applied by the Group in these financial statements. The adoption of these standards is not expected to have a material effect on the Group's financial statements.

- IFRS 9 Financial Instruments (effective date 1 January 2018).
- IFRS 15 Revenue from Contract with Customers (effective date 1 January 2018).
- IFRS 16 Leases (effective date 1 January 2019).
- Investment Entities: Applying the Consolidation Exception – Amendments to IFRS 10, IFRS 12 and IAS 28 (effective date 1 January 2016).
- IFRS 14 Regulatory Deferral Accounts (effective date 1 January 2016).
- Recognition of Deferred Tax Assets for Unrealised Losses – Amendments to IAS 12 (effective date 1 January 2017).
- Disclosure Initiative – Amendments to IAS 7 (effective date 1 January 2017).

2 ACQUISITIONS OF SUBSIDIARIES

Acquisitions in the current period

On 24 August 2015, the Group acquired all of the ordinary shares in TTT Limited for £1, satisfied in cash. The company provides services to BTL under a Management Services Agreement. These services largely constitute the employment cost of business functions within the Group. These employment services are recharged to BTL at zero mark up. In the 7 months to 31 March 2016, the subsidiary contributed net profit of £nil to the consolidated result for the year. If the acquisition had occurred on the first day of the accounting period, there would have been no change to the Group result. The Group has concluded that no fair value adjustments were required to the assets and liabilities acquired.

The acquisition had the following effect on the Group's assets and liabilities.

	Book value £m	Fair value adjustments £m	Recognised values on acquisition £m
Acquiree's net assets at the acquisition date:			
Intangible assets	0.3	–	0.3
Tangible assets	0.1	–	0.1
Trade and other receivables	1.0	–	1.0
Trade and other payables	(1.4)	–	(1.4)
Net identifiable assets and liabilities	**–**	**–**	**–**
Cash price paid			–
Total consideration			**–**

No goodwill has arisen on the acquisition.

3 AUDITOR'S REMUNERATION

	2016 £'000
Audit of these financial statements	55
Audit of subsidiary financial statements	2
Regulatory reporting fees	37
Other non-audit services	60
	154

All of these fees have been capitalised.

Financial Statements
Notes continued

4 EMPLOYEE COSTS

The average number of persons employed by the Group (including Directors) during the period ended 31 March 2016 was 87. The aggregate payroll costs of these persons were as follows:

	2016
	£m
Wages and salaries	4.8
Social security costs	0.5
Contributions to defined contribution plans	0.3
Capitalised into asset under construction	(5.6)
	–

Directors' remuneration is disclosed within the Directors' Remuneration section of this Annual Report.
The Group operates a single defined contribution pension plan, which is open to all employees of the Group.

5 FINANCE INCOME AND EXPENSE

	£m
Finance income	
Interest income	(0.4)
Finance costs	
Interest expense on borrowings	8.3
Financing fees	0.5
Capitalised finance interest and expenses into asset under construction	(8.4)
Net finance costs	**–**

6 TAXATION

	£m
Total current tax	–
Total Income Statement tax expense	–
Reconciliation of effective tax rate	
Profit before tax	–
Profit before tax using the UK corporation tax rate of 20%	–

Unrecognised deferred tax assets

Deferred tax assets of £1.6m in relation to carried forward losses have not been recognised due to uncertainty around the recoverability of these losses against future taxable profits.

7 INTANGIBLE ASSETS

Intangible assets comprised the following at 31 March 2016:

	Note	Software costs £m	Total £m
Cost			
At 21 April 2015		–	–
Acquired through business combinations	2	0.3	0.3
Balance at 31 March 2016		0.3	0.3
Accumulated amortisation			
At 21 April 2015		–	–
Amortisation		(0.3)	(0.3)
Balance at 31 March 2016		(0.3)	(0.3)
Net book value at 31 March 2016		**–**	**–**
Net book value at 21 April 2015		**–**	**–**

Financial Statements
Notes continued

8 PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment comprised the following at 31 March 2016.	Note	Fixtures and fittings £m	Asset under construction £m	Total £m
Cost				
At 21 April 2015		—	—	—
Additions		—	161.2	161.2
Acquired through business combinations	2	0.1	—	0.1
Balance at 31 March 2016		0.1	161.2	161.3
Accumulated depreciation				
At 21 April 2015		—	—	—
Depreciation charge for the year		(0.1)	—	(0.1)
Balance at 31 March 2016		(0.1)	—	(0.1)
Net book value at 31 March 2016		**—**	**161.2**	**161.2**
Net book value at 21 April 2015		**—**	**—**	**—**

Asset under construction

During the construction phase of the project, which commenced in 2015 and which is expected to be completed at System Acceptance, all expenditure which is directly attributable to bringing the Thames Tideway Tunnel asset into its working condition for its intended use will be capitalised. All expenditure in the period ended 31 March 2016 is considered to have met this requirement. The amount of net borrowing costs capitalised during the period was £7.9m with a capitalisation rate of 100%.

9 TRADE AND OTHER RECEIVABLES

	Group 2016 £m	Company 2016 £m
Trade receivables	1.7	1.7
Accrued income	8.6	8.6
Other receivables	5.5	5.5
Prepayments	64.4	64.4
	80.2	**80.2**
Non-current assets	**54.9**	**54.9**
Current assets	**25.3**	**25.3**

Accrued income of £8.6m relates to revenue earned in the period ended 31 March 2016 that has not been invoiced to Thames Water as at the Statement of Financial Position date. Prepayments include £39.8m in relation to the Government Support Package.

10 CASH AND CASH EQUIVALENTS

	Group 2016 £m	Company 2016 £m
Cash and bank balances	0.1	0.1
Cash equivalents	112.8	112.8
Cash and cash equivalents per cashflow statement	**112.9**	**112.9**

Cash equivalents comprise short-term deposits and investments in money market funds with an original maturity of three months or less. The carrying value of cash and cash equivalents approximates their fair value. Short-term deposits with a maturity of greater than 3 months are shown separately on the Statement of Financial Position. At the Statement of Financial Position date these totalled £17.5m.

11 TRADE AND OTHER PAYABLES

	Group 2016	Company 2016
Current	£m	£m
Accrued expenses	19.6	19.6
Deferred income	8.8	8.8
	28.4	**28.4**

Deferred income of £8.8m represents revenue that is deferred until System Acceptance, as the services associated with this revenue will not be delivered until this date.

12 BORROWINGS

This note provides information about the contractual terms of the Group's interest-bearing loans and borrowings, which are measured at amortised cost. For more information about the Group's exposure to interest rate risk, see note 14.

	Group 2016 £m	Company 2016 £m
Non-current liabilities		
Shareholder loan notes	205.1	205.1
	205.1	**205.1**

The principal economic terms and conditions of outstanding borrowings are:

	Currency	Nominal interest rate	Maturity date	Carrying value 2016 £m
Borrowings measured at amortised cost				
Shareholder loan notes (principal):	**GBP**	**8%**	**2064**	**205.1**

13 CAPITAL AND RESERVES

Share capital

Allotted, called up and fully paid Ordinary shares of £1 each	Ordinary shares
On issue at 21 April 2015	–
Issued for cash	138,258,754
On issue at 31 March 2016	**138,258,754**

The holders of ordinary shares are entitled to receive distributions as declared from time to time and are entitled to vote at meetings of the Company, in line with the details of the Shareholders agreement. Further information on the role of the shareholders is outlined in the Corporate Governance report.

14 FINANCIAL RISK MANAGEMENT

The key objective of the Group's financing principles is to deliver efficient financing and financial risk management, which minimises the Group's cost of debt and supports the investment grade credit rating. The Group manages its financial risks in line with the classification of its financial assets and liabilities in the Group's Statement of Financial Position and related notes. The Group's management of specific risks is dealt with as follows:

Liquidity risk

Liquidity risk is the risk that the Group will not be able to fund its capital expenditure programme on a timely basis or service its debt. The Group's exposure to liquidity risk is considered low, as the Group's shareholders committed funding at licence award of £1.3bn backed by letters of credit. The equity and loans provided by shareholders will be substantially invested before the business is expected to enter a position of net debt at the end of 2018.

The Group has a £1bn revolving credit facility (RCF) which does not expire until 2025. At the Statement of Financial Position date, this facility was undrawn.

The Secretary of State for Environment, Food and Rural Affairs, through the Government Support Package, has committed to provide certain financial support during the construction period. Such support is available in exceptional circumstances and includes the Market Disruption Facility, providing BTL with up to £500 million debt facility for use where it is unable to issue debt in the debt capital markets as a result of market disruption.

Credit risk

Credit risk is the risk of financial loss to the Group if a counterparty to a financial instrument fails to meet its contractual obligations. The Treasury Policy limits application of funds through concentration limits and minimum rating requirements. The Financing Documents include minimum rating requirements for lenders under the RCF. At the Statement of Financial Position date, there were no significant concentrations of credit risk.

Interest rate risk

The Group does not have any exposure to interest rate risk on its financial liabilities, as the only interest bearing financial instruments are fixed rate shareholder loan notes. The effective interest rate of these borrowings is disclosed in note 12.

The Group's finance strategy defines long-term objectives for the management of interest rate risk, in addition to compliance with the hedging policies contained in the Government Support Package and financing documentation. These include, amongst other things, restrictions on over hedging and requirements as to the amount of the Group's debt which bears a fixed or index-linked rate of interest. The Group will seek to pre-finance debt to reduce exposure to increases in interest rates.

Inflation risk

The Group is exposed to changes in the Retail Price Index (RPI), through its Regulated Capital Value (RCV) and revenue. A sustained period of low or negative inflation as measured by RPI would reduce returns to shareholders. The Group's proposed financing strategy includes raising a high proportion of index-linked debt, which will ensure that interest costs and principal move in line with RPI and therefore offset any reductions in revenue and RCV that result from lower inflation.

Capital managements

The capital structure of the Group consists entirely of shareholder equity and borrowings from the shareholders through loan notes. The Group currently has no external borrowings. The Group has been assigned a corporate family credit rating of Baa1 by Moody's and with regards to the RCF, BBB+ by Fitch.

Financial Statements
Notes continued

15 OPERATING LEASES
The Group has entered into non-cancellable operating leases in respect of buildings. The future minimum rentals payable under non-cancellable operating lease rentals are as follows:

	2016 £m
Less than one year	5.4
Between one and five years	4.6
More than five years	–
	10.0

16 CONTINGENT LIABILITIES
There are a number of uncertainties surrounding the Group including potential claims, which may affect the financial performance of the Group. Where claims are possible but not probable, or unquantifiable, such claims are treated as contingent liabilities. Contingent liabilities are not recognised in the Statement of Financial Position, but are monitored to ensure that should a possible obligation become probable and a transfer of economic benefits to settle an obligation can be reliably measured, then a provision for the obligation is made. The assessment is there were no contingent liabilities at the balance sheet date.

17 CONTINGENT ASSETS
The majority of the Group's works contracts are based on a target cost mechanism under which over or underspends on target are shared with the contractor. As a result, it is possible that a cash inflow to the Group may occur in the future. Where amounts due to the Group are not virtually certain, they are treated as contingent assets and not recognised in the Statement of Financial Position as an asset. The assessment is there were no contingent assets at the balance sheet date.

18 RELATED PARTIES
Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note.

Amounts outstanding on borrowings from the immediate parent company, Bazalgette Holdings Limited, are disclosed in note 12.

19 ULTIMATE PARENT COMPANY AND PARENT COMPANY OF LARGER GROUP
The Company is a wholly owned subsidiary of Bazalgette Holdings Limited. The Company's ultimate controlling parent is Bazalgette Equity Limited which is also the largest group in which the Company is consolidated. Copies of the consolidated accounts for the Bazalgette Equity Group are available from the Company Secretary at The Point, 37 North Wharf Road, London, W2 1AF.

Investments in subsidiaries

Company	Thames Tideway Tunnel Limited
Country of incorporation	UK
Class of shares held	Ordinary
Ownership 2016	100%

The subsidiary has the same period end as the Company.

20 EVENTS OCCURRING AFTER THE REPORTING DATE
The European Investment Bank has provided a £700m long-term loan, expected to be drawn from 2018 in index-linked form. The Group has put in place a bond issuance platform and priced bond issues of £350m. Further detail is provided in the Financing section of the Performance Review on page 29.

The Lee Tunnel in its final stages of construction

Regulatory Reporting

98 Introduction

98 Regulatory Annual Performance Report

110 Transfer Pricing Information

111 Risk and Compliance Statement

112 Condition K Reporting

113 Other Reporting Requirements

115 Data Assurance Summary

115 Auditor's Report

119 Glossary

Stephen Shipley, from Surbiton, is a commercial manager at Tideway, working in the team progressing the western section of the Thames Tideway Tunnel. An enthusiast for the river and its pubs, he joined project colleagues and other volunteers to rebuild the eroding banks of Chiswick Eyot, an island in the Thames.

Regulatory Reporting

INTRODUCTION

Tideway has included its regulatory reporting requirements within the Annual Report and Accounts rather than produce a separate report. We believe this approach provides stakeholders with information in a simple, consistent and accessible way to support their trust and confidence in the Company.

Tideway faces a number of annual reporting requirements driven by its licence, and by guidance from the economic regulator, Ofwat. These requirements are summarised in Ofwat's Information Notice 15/18, "Expectations for company annual performance reporting 2015-16",[1] and set out in more detail in Ofwat's Regulatory Accounting Guidelines (RAGs) and Tideway's licence.

This section contains the main items of regulatory information: the annual performance report, a statement on transfer pricing, risk and compliance statement, statements on the sufficiency of Tideway's resources and a data assurance summary. Where regulatory reporting requirements have been addressed in earlier sections of the report, these are summarised in the table on pages 113 to 114.

REGULATORY ANNUAL PERFORMANCE REPORT

This section contains information on Tideway's financial position and performance in 2015/16 that is relevant from a regulatory perspective.

Tideway is a wholesale company with specific regulatory arrangements. This means that its regulatory reporting is different from other water companies. Tideway has agreed with Ofwat that it will publish a set of tables that includes some standard tables and some that are unique. The table below summarises the differences between Tideway's annual performance report and those produced by other water companies.

As well as the difference in the suite of tables, the numbers within this Regulatory Annual Performance Report look different in many ways from those reported by other water companies. Features of the data reported below include:

- Tideway capitalises costs that meet the capitalisation criteria for assets under construction and revenue is reported as deferred income during the construction phase. There are therefore no entries in the income statement other than in relation to interest (see notes to Table 1A). Allowed Revenue is reported in Table 5A.
- In 2015/16, Tideway did not have any third-party debt. It does, however, have shareholder loans. In line with the RAGs, the shareholder loans are reported as debt within the net debt metric in tables 1E and 4H. Tideway has a separate net debt metric in its licence which is used for the financing cost adjustment and which excludes shareholder loans.
- Tideway's regulatory capital value was zero at licence award. On 31 March 2016, it was £151.3m in March 2016 prices.

Section	Relevance and approach
1	Standard Industry Tables. Relevant to Tideway. Tables 1A-1E shown on pages 99 to 105.
2	Standard Industry Tables. Table 2D includes some elements that are relevant to Tideway and is shown on page 106. Other tables, such as 2B (Totex analysis – wholesale) and 2C (Operating cost analysis – retail), are not relevant to Tideway as they relate to elements of financial reporting that are not applicable.
3	Standard Industry Tables. Not relevant to Tideway as it relates to performance commitments made at the last periodic review. This review does not apply to Tideway.
4	Standard Industry Tables. Most are not relevant to Tideway as they relate to different segments of the water and sewerage business and elements of financial reporting that are not applicable. Table 4H (Financial metrics) is relevant to Tideway and is reported on page 107. Table 4I is not relevant to Tideway for 2015/16 reporting as it did not have any financial derivatives during the 2015/16 financial year. This table will be included in future years if the situation changes.
5	This section contains tables that are unique to Tideway, covering revenue analysis, expenditure analysis, Alliance Agreement payments, and a note on the financing cost adjustment element of Tideway's allowed revenue calculation.

1. *http://www.ofwat.gov.uk/wp-content/uploads/2015/12/prs_in1518annualperformancereport.pdf*

1A – Income statement

For the period ended 31 March 2016

				Adjustments			
Line description		Units	Statutory	Differences between statutory & RAG definitions	Non appointed	Total adjustments	Total appointed activities
1	Revenue	£m	–	–	–	–	–
2	Operating costs	£m	–	–	–	–	–
3	Other operating income	£m	–	–	–	–	–
4	Operating profit	£m	–	–	–	–	–
5	Other income	£m	–	–	–	–	–
6	Interest income	£m	–	0.414	–	0.414	0.414
7	Interest expense	£m	–	(8.290)	–	(8.290)	(8.290)
8	Other interest expense	£m	–	–	–	–	–
9	Profit before tax and fair value movements	£m	–	(7.876)	–	(7.876)	(7.876)
10	Fair value gains/(losses) on financial instruments	£m	–	–	–	–	–
11	Profit before tax	£m	–	(7.876)	–	(7.876)	(7.876)
12	UK Corporation tax	£m	–	–	–	–	–
13	Deferred tax	£m	–	–	–	–	–
14	Profit for the year	£m	–	(7.876)	–	(7.876)	(7.876)

Notes to line items:

6 & 7: Differences between statutory and RAG definitions relate to interest capitalised under IAS 23 Borrowing Costs. These are required to be shown in the Income Statement for regulatory reporting and therefore generate a loss for the period of £7.876m.

14: As explained in the Financial Performance Review (pages 32-33), all costs which meet the capitalisation criteria for assets under construction will be capitalised and revenue is reported as deferred income during the construction phase. The statutory accounts Income Statement result for the period is £nil.

Regulatory Reporting

1B – Statement of comprehensive income

For the period ended 31 March 2016

	Line description	Units	Statutory	Adjustments: Differences between statutory & RAG definitions	Adjustments: Non appointed	Adjustments: Total adjustments	Total appointed activities
1	Profit for the year	£m	–	(7.876)	–	(7.876)	(7.876)
2	Actuarial gains/(losses) on post employment plans	£m	–	–	–	–	–
3	Other comprehensive income	£m	–	–	–	–	–
4	Total Comprehensive income for the year	£m	–	(7.876)	–	(7.876)	(7.876)

For details on the adjustments see notes to table 1A

1C – Statement of financial position

For the period ended 31 March 2016

	Line description	Units	Statutory	Adjustments: Differences between statutory & RAG definitions	Adjustments: Non appointed	Adjustments: Total adjustments	Total appointed activities
A	**Non-current assets**						
1	Fixed assets	£m	161.229	(7.876)		(7.876)	153.353
2	Intangible assets	£m	–	–	–	–	–
3	Investments – loans to group companies	£m	–	–	–	–	–
4	Investments – other	£m	–	–		–	–
5	Financial instruments	£m	–	–	–	–	–
6	Retirement benefit assets	£m	–	–	–	–	–
7	Total non-current assets	£m	161.229	(7.876)	–	(7.876)	153.353

1C – Statement of financial position

For the period ended 31 March 2016

	Line description	Units	Statutory	Adjustments: Differences between statutory & RAG definitions	Adjustments: Non appointed	Adjustments: Total adjustments	Total appointed activities
B	**Current assets**						
8	Inventories	£m	–	–	–	–	–
9	Trade & other receivables	£m	97.674	–	–	–	97.674
10	Financial instruments	£m	–	–	–	–	–
11	Cash & cash equivalents	£m	112.877	–	–	–	112.877
12	Total current assets	£m	210.551	–	–	–	210.551
C	**Current liabilities**						
13	Trade & other payables	£m	–	–	–	–	–
14	Capex creditor	£m	(28.390)	–	–	–	(28.390)
15	Borrowings	£m	–	–	–	–	–
16	Financial instruments	£m	–	–	–	–	–
17	Current tax liabilities	£m	–	–	–	–	–
18	Provisions	£m	–	–	–	–	–
19	Total current liabilities	£m	(28.390)	–	–	–	(28.390)
20	Net current assets/(liabilities)	£m	182.161	–	–	–	182.161

Regulatory Reporting

1C – Statement of financial position *(continued)*

For the period ended 31 March 2016

	Line description	Units	Statutory	Adjustments: Differences between statutory & RAG definitions	Adjustments: Non appointed	Adjustments: Total adjustments	Total appointed activities
D	**Non-Current liabilities**						
21	Trade & other payables	£m	–	–	–	–	–
22	Borrowings	£m	(205.131)	–	–	–	(205.131)
23	Financial instruments	£m	–	–	–	–	–
24	Retirement benefit obligations	£m	–	–	–	–	–
25	Provisions	£m	–	–	–	–	–
26	Deferred income – G&Cs	£m	–	–	–	–	–
27	Preference share capital	£m	–	–	–	–	–
28	Deferred tax	£m	–	–	–	–	–
29	Total non-current liabilities	£m	(205.131)	–	–	–	(205.131)
30	Net assets	£m	138.259	(7.876)	–	(7.876)	130.383
E	**Equity**						
31	Called-up share capital	£m	138.259	–	–	–	138.259
32	Retained earnings & other reserves	£m	–	(7.876)	–	(7.876)	(7.876)
33	Total Equity	£m	138.259	(7.876)	–	(7.876)	130.383

Notes to line items:

1. All the costs included in Fixed Assets are on an accruals basis. This differs from the Annual Actual Project Spend in Table 5B, which is on a cash basis.
9. The regulatory accounts include £97.7m of Trade and other receivables. This includes current and non-current trade debtors, prepayments, accrued income and short-term deposits. Under IFRS, the Statement of Financial Position splits the £97.7m between £54.9m of Non-current assets (being amounts due after more than one year) and £42.8m of Current assets. Current assets includes £17.5m of short-term deposits with a maturity of greater than 3 months.

1D – Statement of cash flows

For the period ended 31 March 2016

	Line description	Units	Statutory	Adjustments: Differences between statutory & RAG definitions	Adjustments: Non appointed	Adjustments: Total adjustments	Total appointed activities
A	**Statement of cash flows**						
1	Operating profit	£m	–	–	–	–	–
2	Other income	£m	–	–	–	–	–
3	Depreciation	£m	–	–	–	–	–
4	Amortisation – G&Cs	£m	–	–	–	–	–
5	Changes in working capital	£m	(51.784)	–	(0.530)	(0.530)	(52.314)
6	Pension contributions	£m	–	–	–	–	–
7	Movement in provisions	£m	–	–	–	–	–
8	Profit on sale of fixed assets	£m	–	–	–	–	–
9	Cash generated from operations	£m	(51.784)	–	(0.530)	(0.530)	(52.314)
B							
10	Net interest paid	£m	–	(7.014)	–	(7.014)	(7.014)
11	Tax paid	£m	–	–	–	–	–
12	Net cash generated from operating activities	£m	(51.784)	(7.014)	(0.530)	(7.544)	(59.328)

Regulatory Reporting

1D – Statement of cash flows *(continued)*

For the period ended 31 March 2016

				Adjustments			
	Line description	Units	Statutory	Differences between statutory & RAG definitions	Non appointed	Total adjustments	Total appointed activities
C	**Investing activities**						
13	Capital expenditure	£m	(160.296)	7.014	0.530	7.544	(152.751)
14	Grants & Contributions	£m	–	–	–	–	–
15	Disposal of fixed assets	£m	–	–	–	–	–
16	Other	£m	(17.500)	–	–	–	(17.500)
17	Net cash used in investing activities	£m	(177.796)	7.014	0.530	7.544	(170.251)
18	Net cash generated before financing activities	£m	(229.580)	–	–	–	(229.580)
D	**Cash flows from financing activities**						
19	Equity dividends paid	£m	–	–	–	–	–
20	Net loans received	£m	204.198	–	–	–	204.198
21	Cash inflow from equity financing	£m	138.259	–	–	–	138.259
22	Net cash generated from financing activities	£m	342.457	–	–	–	342.457
23	Increase (decrease) in net cash	£m	112.877	–	–	–	112.877

Notes to line items:

10. The net interest paid of £7.014m includes £7.356m of interest paid, partly offset by £0.342m of interest received. The difference of £0.862m between the £7.014m of net interest paid and the £7.876m net interest within the Income Statement (table 1A) is £0.933m of rolled up interest (see note to Table 1E) partly offset by £0.071m of interest receivable accrual.

5 & 13. The non-appointed adjustment of £0.530m reflects expenditure by the Company on behalf of Thames Water. The adjustment reduces the investing activities (capital expenditure) in the period, recognising these are not allowable spend for the Company. The Company has been reimbursed by Thames Water for these costs after the year end.

13. The £160.296m of capital expenditure represents cash outflows for the asset under construction.

16. The £17.500m represents the short-term deposits with a maturity of greater than 3 months.

22. The £342.457m of net cash generated from financing activities reflects funds received from the shareholders. This was in the form of £204.198m of net shareholder loans received and £138.259m of equity.

1E – Net debt analysis

at 31 March 2016

			Interest rate risk profile			
Line description		Units	Fixed rate	Floating rate	Index linked	Total
1	Borrowings (excluding preference shares)	£m	(205.131)	–	–	(205.131)
2	Preference share capital	£m				–
3	Total borrowings	£m				(205.131)
4	Cash	£m				112.877
5	Short term deposits	£m				17.500
6	Net debt	£m				(74.754)
7	Gearing	%				(49.40)
8	Adjusted gearing	%				0.00
9	Full year equivalent nominal interest cost	£m	(16.410)	–	–	(16.410)
10	Full year equivalent cash interest payment	£m	(16.410)	–	–	(16.410)
	Indicative interest rates					
11	Indicative weighted average nominal interest rate	%	8.00	–	–	–
12	Indicative weighted average cash interest rate	%	8.00	–	–	–

Notes to line items:

1. The borrowings of £205.131m are shareholder loans and include £204.198m of net loans received (Table 1D) and £0.933m of rolled up interest.

7. As the Company was not part of the 2014 Periodic Review process, it does not have an RCV determined at the Final Determination. Therefore the gearing calculation is based on the RCV at 31 March 2016 (in table 5B).

8. Adjusted gearing is the ratio of senior net indebtedness to RCV. The Company has no outstanding senior net indebtedness. As it has cash and cash equivalents, the senior net indebtedness figure, and hence adjusted gearing, would in principle be negative. However, for the purposes of its reporting in relation to its financial covenants, as per the terms of its financing documents, the Company reports gearing of zero.

Regulatory Reporting

2D - Historic cost analysis of fixed assets — wholesale & retail

For the period ended 31 March 2016

	Line description	Units	Wholesale		Retail		Total
			Water	Wastewater	Household	Non Household	
	A Cost						
1	At 1 April 2015	£m	–	–	–	–	–
2	Disposals	£m	–	–	–	–	–
3	Additions	£m	–	153.447	–	–	153.447
4	At 31 March 2016	£m	–	153.447	–	–	153.447
	B Depreciation						
5	At 1 April 2015	£m	–	–	–	–	–
6	Disposals	£m	–	–	–	–	–
7	Charge for the year	£m	–	(0.094)	–	–	(0.094)
8	At 31 March 2016	£m	–	(0.094)	–	–	(0.094)
9	Net book amount at 31 March 2016	£m	–	153.353	–	–	153.353
10	Net book amount at 1 April 2015	£m	–	–	–	–	–

Notes to line items:

All. For the purposes of completing table 2D, Tideway has classified all of its activities as falling within the wholesale wastewater segment. This approach reflects that Tideway is constructing a single asset, the Thames Tideway Tunnel, which will be used solely for sewage collection activities. The company has no direct relationship with customers and carries out no activities that could be classified as retail. The approach to this table therefore aligns both to the general principles set out in Regulatory Accounting Guideline 2.05, including those of transparency and causality, and with the definitions of wholesale activities set out in Regulatory Accounting Guideline 4.05.

7. The depreciation charge for the period of £0.094m reflects depreciation for fixtures & fittings which were acquired through the combination of Thames Tideway Tunnel Limited into the Bazalgette Tunnel Limited Group. This amount does not appear in the regulatory or statutory income statements as for the purpose of producing these statements, depreciation is capitalised.

9. The net book amount of £153.353m aligns to the fixed assets value on the statement of financial position (table 1C).

4H – Financial metrics

For the period ended 31 March 2016

	Line description	Units	Metric
1	Net debt	£m	(74.754)
2	Regulated equity	£m	76.557
3	Regulated gearing	%	(49.40)
4	Post tax return on regulated equity	%	(20.57)
5	RORE (return on regulated equity)	%	n/a
6	Dividend yield	%	n/a
7	Retail profit margin – Household	%	n/a
8	Retail profit margin – Non household	%	n/a
9	Credit rating	n/a	Baa1
10	Return on RCV	%	0.00
11	Dividend cover	dec	n/a
12	Funds from operations (FFO)	£m	(7.014)
13	Interest cover (cash)	dec	0.05
14	Adjusted interest cover (cash)	dec	0.05
15	FFO/Debt	dec	0.09
16	Effective tax rate	%	0.00
17	Free cash flow (RCF)	£m	(7.014)
18	RCF/capex	dec	0.05
19	Revenue (actual)	£m	0.00
20	EBITDA (actual)	£m	0.00

Regulatory Reporting

	Line description	Units	Statutory
21	Proportion of borrowings which are fixed rate	%	100.00
22	Proportion of borrowings which are floating rate	%	–
23	Proportion of borrowings which are index linked	%	–
24	Proportion of borrowings due within 1 year or less	%	–
25	Proportion of borrowings due in more than 1 year but no more than 2 years	%	–
26	Proportion of borrowings due in more than 2 years but no more than 5 years	%	–
27	Proportion of borrowings due in more than 5 years but no more than 20 years	%	–
28	Proportion of borrowings due in more than 20 years	%	100.00

Notes to line items:

1 & 3. As shown in table 1E, Tideway's borrowings per the RAGs exceed its cash and short-term deposits, and hence it has a net debt position. Applying the line definitions specified by Ofwat results in negative figures for net debt in line 1 (which is taken directly from table 1E), and hence regulated gearing in line 3.

2 & 3. As the Company was not part of the 2014 Periodic Review process, it does not have an RCV determined at the Final Determination. Therefore the regulated equity and regulated gearing are calculated based on the RCV at 31 March 2016 (in table 5B).

5. The calculation of return on regulated equity (RORE) is n/a as the Company was not part of the PR14 process and does not have a base RORE set at Final Determination.

6 & 11. As explained in the Financial Performance Review, there were no dividends paid or proposed during the period. Therefore all the dividend-based financial metrics are reported as n/a.

7 & 8. The retail profit margins are n/a as Tideway has no retail business.

9. The Company has been assigned a corporate credit rating of Baa1 by Moody's.

5A – Revenue analysis

For the period ended 31 March 2016

	£m	
	Year	Allowed Revenue
1	2015/16	11.2
2	2016/17	22.4

Notes:

1. As explained in the notes to Table 1A, the Company will recognise all revenue as deferred income during the construction phase.
2. Tideway's Allowed Revenue was first billed by Thames Water for the 2016/17 charging year, as this could only be calculated following the award of Tideway's licence in August 2015, but Tideway did not receive any payments from Thames Water in 2015/16.
3. As explained in the Financial Performance Review, the financial statements include revenue (as deferred income) of £8.8m, which is based on the latest estimate as of April 2016. This is lower than the £11.2m allowed revenue, reflecting the lower allowable project spend (see Table 5B). The impact on customers of any over- or under-recovery of revenue is mitigated via a reconciliation carried out in subsequent years.

5B – Expenditure analysis

For the period ended 31 March 2016

	£m, 2014/15 prices	2015/16
1.1	Annual Base Case Forecast	234.7
2.1	Total expenditure	209.8
3.1	Excluded Project Spend	60.6
4.1	Non-regulated expenditure	0.5
5.1	Annual Actual Project Spend	148.7
6.1	Variance from base case	(85.9)
7.1	Variance (%)	(36.6%)
	As at 31 March 2016	
8.1	RCV	148.7

	£m, outturn prices	2015/16
1.2	Annual Base Case Forecast	237.2
2.2	Total expenditure	212.1
3.2	Excluded Project Spend	61.3
4.2	Non-regulated expenditure	0.5
5.2	Annual Actual Project Spend	150.3
6.2	Variance from base case	(86.8)
7.2	Variance (%)	(36.6%)
	As at 31 March 2016	
8.2	RCV	151.3

Notes to line items:

1. Tideway's Annual Base Case Forecast, its annually profiled regulatory baseline, is included in its licence. The figure reported for each financial year is subject to defined inflationary adjustments, as set out in Appendix 1 of Tideway's licence. For the purpose of this report, the adjustment for 2015/16 has been applied using the inflation data at 18 April 2016. For this reason, the figures reported above differ from the £237.8m set out in the licence.
3. Excluded Project Spend includes certain specified categories of spending that are not included in Tideway's RCV. In 2015/16, Excluded Project Spend related primarily to Tideway's financing costs.
4. Non-regulated expenditure relates to activity that is neither Allowable nor Excluded Project Spend. In 2015/16, non-regulated expenditure relates to the £0.5m expenditure by the Company on behalf of Thames Water noted in Table 1D.
5. Annual Actual Project Spend is the total of Allowable Project Spend incurred by Tideway and verified by the ITA during the period from 24 August 2015 to 31 March 2016, inclusive. This amount becomes part of Tideway's RCV and drives its revenues.

6 & 7. In 2015/16, Annual Actual Project Spend was below the Annual Base Case Forecast due to lower costs on both direct and indirect costs and unutilised risk. The main reasons were due to the licence award date being delayed by three weeks and the slower than expected ramp up in resources. The Financial Performance Report sets out the 2015/16 expenditure (on an accruals basis) in more detail.

1-7. The tables above report expenditure in both outturn and 2014/15 prices. Except for RCV, figures in outturn prices are deflated to 2014/15 prices using financial year average RPI, consistent with Tideway's licence.

8. The tables above report RCV in 2014/15 prices and March 2016 prices. The outturn RCV differs from outturn Annual Actual Project Spend due to the difference between outturn and year-end prices.

5C – Alliance Agreement payments

For the period ended 31 March 2016

	£m, outturn prices	2015/16
1	Alliance Agreement payments received	–
2	Alliance Agreement payments made	–

Notes to line items:

1. Expenditure funded by Alliance Agreement payments received will be Excluded Project Spend and therefore excluded from the RCV.
2. An amount of £4.160m was accrued at 31 March 2016 for Alliance Agreement payments within the Financial Statements but no payments were made on or before 31 March 2016.

Regulatory Reporting

Financing cost adjustment

Tideway is required by Part A of Appendix 1 of its licence to report on:

- Net debt (as defined by the licence). In 2015/16 this was -£130.4m. This figure was calculated by taking Tideway's net debt figure of £74.8m and removing the £205.1m of shareholder loans, leaving a net cash figure. Shareholder loans are included in Tideway's net debt using the definitions in the Regulatory Accounting Guidelines but are not included in the net debt figure calculated in accordance with Tideway's licence.
- The basis of the calculation of the Financing Cost Adjustment and its component parts. This information is included in its annual Revenue Statement (see http://www.tideway.london/media/2236/tideway-2015-updated-revised-revenue-statement-submission-151215.pdf)

Disclosure of information to auditor[3]

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

TRANSFER PRICING INFORMATION

To demonstrate that it is operating at arm's length from other companies in the same group and that no cross-subsidies exist, Tideway is required by Regulatory Accounting Guideline 3.08 to disclose details of transactions with associated companies. The Tideway group structure is shown on page 55.

Service	Company	Turnover of associate	Terms of supply	Value
Shareholder loans	Bazalgette Holdings Ltd	–	The shareholder loans were included in the financing plan that was part of the bid that Tideway's owners made for the company. Bids were evaluated as part of the procurement process for the infrastructure provider against criteria that included the rate of return ('Bid WACC') required by bidders and the financial resilience of the proposed financing structure. Government and Ofwat were given sight of documents relating to the shareholder loans during the procurement process run by Thames Water. Ofwat's scrutiny of these documents informed its judgement that Tideway was fit and proper to hold a licence.	£205.1m outstanding

Notes:

3. This information is included in the Directors' Report for statutory purposes and is repeated here in line with Ofwat's requirement that companies make this statement within their annual performance reports.

Tideway's shareholder loans are made by an associated company, Bazalgette Holdings Limited, and are therefore a relevant transaction. The loan arrangement meets all regulatory requirements for transactions with associated companies. The information in the form required by Ofwat is shown on the previous page.

Other than arrangements under shareholder loans, the only transactions within the Tideway group were between Tideway and its subsidiary, Thames Tideway Tunnel Ltd (TTT). These transactions result from an administrative arrangement put in place to allow Tideway to be created; from an operational perspective, there is no distinction between Tideway and TTT. As a result, Ofwat has agreed that Tideway and TTT accounts can be reported on a consolidated basis. This means that there are no relevant transactions to be reported in relation to TTT.

RISK AND COMPLIANCE STATEMENT

This section relates to Tideway's compliance with its statutory, licence and regulatory obligations. For the purpose of the statements set out on page 112, Tideway has identified four sources of obligations. The following paragraphs explain Tideway's legal and regulatory framework and set out why this scope of obligations is considered appropriate:

- the project licence;
- a modified version of the Water Industry Act 1991, as amended;
- the "SIP Regulations";[4] and
- Project Specification Notice.

Tideway has a bespoke regulatory regime that builds on the arrangements applying to other water companies while reflecting its particular characteristics. As a consequence of the SIP Regulations, which were enacted specifically to allow the delivery of infrastructure projects such as the Thames Tideway Tunnel, Tideway is subject to a modified version (the "Modified WIA") of the main law that governs the water industry: the Water Industry Act 1991, as amended. The Modified WIA includes a limited number of duties that are identical to those of other water companies, such as a requirement to comply with reasonable requests for information by the Secretary of State or Ofwat, and a number of further requirements that are tailored to licensed infrastructure providers.

In addition to the requirements of the Modified WIA, and unlike other water companies, Tideway's activities are prescribed by a detailed Project Specification Notice that was issued by the Secretary of State on 4 June 2014, in accordance with the SIP Regulations. The Project Specification Notice sets out the scope of the Thames Tideway Tunnel, being its design, construction, testing, commissioning, financing, operation and maintenance.

Tideway has a licence, granted by Ofwat pursuant to the Modified WIA. The licence contains many conditions that are identical to the most up-to-date versions applying to other water companies, including those relating to ring-fencing, restrictions on the grant and enforcement of security, and disposals of land. The differences between Tideway's licence and those of other companies predominantly relate to the way in which it calculates and collects revenue, and to the fact that it has, and is expected to have, no direct relationship with wastewater customers.

For the purposes of the statements on page 112, Tideway defines its obligations as those contained in the Modified WIA, the SIP Regulations, the Project Specification Notice, and its licence. This scope captures the major regulatory and legal obligations applicable to Tideway that are specific to the Thames Tideway Tunnel or to the water industry. The risk and compliance statement therefore complements a number of other Tideway reporting practices, such as detailed quarterly reporting of project information to a Liaison Committee attended by representatives from Ofwat and Defra, and regular information sharing with the Independent Technical Assessor, Environment Agency and other sources of scrutiny. Collectively, ›

Notes:

4. The Water Industry (Specified Infrastructure Projects) (English Statutory Undertakers) Regulations 2013 (as amended by the Water Industry (Specified Infrastructure Projects) (English Statutory Undertakers) (Amendment) Regulations 2015) (the "SIP Regulations").

5. Statements in relation to customers and outputs required by Ofwat's risk and compliance statement guidance are not included here as they are not relevant to Tideway. (See page overleaf)

Regulatory Reporting

these practices help to ensure transparency and accountability regarding Tideway's compliance with its statutory, licence and regulatory obligations.

With regard to the above obligations, Tideway's Board confirms that: [5]

- The Company has a full understanding of, and is meeting, its obligations. Under the umbrella of its assurance policy, strategy and plan, Tideway has put in place a range of processes for ensuring compliance. In relation to Tideway's licence obligations, these processes include allocation of each obligation to an owner with the most relevant expertise within Tideway, quarterly reviews by the Regulation team, management reviews, and further review by a broader compliance and assurance group led by the CEO. Two internal audits of licence compliance took place during 2016. In relation to legal obligations, compliance is managed by Tideway's legal team. The team periodically verifies compliance with Tideway's obligations using guidance produced by external legal advisors. It also scrutinises procurements, particularly those of high value, to ensure compliance with the procurement regime applicable to Tideway.
- The Company has satisfied itself that it has sufficient processes and internal systems of control to fully meet its obligations. The Company is committed to continual improvement and as such we will continue to refine our processes to support ongoing compliance.
- The Company has appropriate systems and processes in place to allow it to identify, manage and review its risks. The steps being taken to manage or mitigate material identified risks are covered in the Risk Management section of the Strategic Report.

CONDITION K STATEMENT

Condition M 5.1 of Tideway's licence requires it to make an annual statement regarding the sufficiency of its non-financial resources in case of special administration.

The Tideway Board confirms that as at 31 March 2016, Tideway had available to it sufficient rights and resources other than financial resources so that if, at any time, a special administration order were to be made in relation to it, the special administrator would be able to manage Tideway's affairs, business and property in accordance with the purposes of the special administration order.

INFORMATION ON THE CONDITION K CERTIFICATE

Tideway has submitted a Condition K Certificate to Ofwat stating that in the opinion of its Board:

- Tideway will have available to it sufficient financial resources and facilities to enable it to carry on the Licensed Activities for at least the 12-month period following the date of submission.
- Tideway will have available to it sufficient management resources and systems of planning and internal control to enable it to carry on the Licensed Activities for at least the 12-month period following the date of submission.
- All contracts entered into between Tideway and any Associated Company include the necessary provisions and requirements in respect of the standard of service to be supplied to Tideway, to ensure that it is able to carry on the Licensed Activities.

Tideway has a range of processes that enable the Tideway Board to make the above statements. These include:

- Tideway's financing plan, annual budget, annual and long-term business plans and resource planners;
- Board oversight of these processes, in particular via Tideway's Audit Committee, which oversees systems of planning and internal control and overall regulatory compliance. The Board reviews financial resources and facilities and management resources on a monthly basis. A summary of the quarterly licence compliance review is provided to the Board through the monthly reporting process;
- scrutiny by Tideway's external auditor, KPMG, which is required to confirm that Tideway is a going concern;
- reviews by Tideway's legal team of all proposals for new or modified contracts with reference to regulatory obligations and the need to ensure appropriate standards of service; and
- a strong data assurance policy, strategy and plan based around the concept of 'three lines of defence' (see data assurance summary on page 115).

The outputs of the process underlying the Long Term Viability Statement (see page 75) give further comfort in relation to the above statements, by demonstrating Tideway's financial viability up to 2024.

OTHER REPORTING REQUIREMENTS

Tideway's Long Term Viability Statement is included on page 75. The Company believes that this statement is appropriate for both its statutory and regulatory accounts.

Sections 3 and 4 of RAG 3.08 require companies to make a number of further disclosures, in addition to those set out above. As explained in the table below, a number of these requirements are not relevant to Tideway. Where the requirements are relevant, they are included in the most relevant section of the Annual Report, as shown below.

Required Disclosure	Location in report	Notes
Description of the link between directors' pay and standards of performance, as required by section 35A of the WIA 1991	Remuneration report (pages 64 to 71)	
Statement on dividend policy for the appointed business (value and basis of dividend/ distribution)	Directors' report (page 72)	Tideway did not pay any dividends in 2015/16, though distributions were made under shareholder loan arrangements, in line with Tideway's distribution policy. Information on the distributions made is provided in the Directors' report.
Accounting policy note for price control segments.	N/A	As Tideway operates only within the sewerage segment, this requirement does not apply.
Note on revenue recognition	N/A	Section 3.6 of RAG 3.08 requires companies to report on revenue recognition. This requirement does not apply to Tideway, as none of the items contained within this requirement are relevant. Tideway has not reported any income statement revenue in 2015/16, either in the statutory accounts or regulatory annual performance report, and does not bill customers directly.
Note on capitalisation policy	Financial statements: contained within note 1 under "Property, plant and equipment: Recognition and measurement" (page 84)	The Directors consider all expenditure in the period ended 31 March 2016 to have met the capitalisation criteria.

Regulatory Reporting

Required Disclosure	Location in report	Notes
Note on bad debt policy	Financial statements: contained within note 1 (accounting policies) under "Accrued Revenue and bad debt risk" (page 85)	Tideway collects its revenue via Thames Water and does not bill customers directly, so its bad debt policies are different to those of other water and sewerage companies. Note 1 to the Financial Statements contains more information on the arrangements in place.
Statement on differences between statutory and RAG definitions	This section – see notes to table 1A (page 99)	Only difference relates to capitalisation of interest.
Narrative disclosures on performance	N/A	Outcome performance and totex are not part of the bespoke regulatory regime applying to Tideway. Tideway does not operate in the retail sector, so does not report retail performance figures. Tideway was not subject to 2014 price review and does not complete table 2I, so does not report a wholesale revenue control reconciliation. Current tax reconciliation is not relevant as Tideway did not pay any corporation tax in 2015/16.

DATA ASSURANCE SUMMARY

Tideway's Board, supported by the Audit Committee, places a high level of importance on assurance of company information. The Audit Committee has overseen the development of the Company's assurance policy and strategy, which has embedded the approach of the 'three lines of defence'. The first line of defence relates to business operations; the second line to oversight functions; and the third to independent audit.

The Company has applied the three lines of defence approach to assurance of data in the Annual Report and Accounts. The positive results of the assurance workstream have been shared with the Audit Committee. This has enabled the Audit Committee to assure the Board, in line with UK Corporate Governance Code requirements, that the 'Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy'.

Beyond the assurance provided by business operations (first line) and oversight functions (second line), the scope of independent assurance provided by KPMG and internal audit is set out below:

- KPMG audit of Statutory Accounts (including elements of the remuneration report); regulatory audit (covering tables 1A-1E and 2D and Condition K certificate) and an agreed-upon procedures review covering the remaining regulatory tables;
- KPMG review and report by exception ongoing concern, Long Term Viability Statement, corporate governance and the unaudited sections of the Annual Report and Accounts; and
- Internal audit of key financial and operational processes supporting the Annual Report and Accounts and of the licence compliance process.

The results of KPMG's two audits are covered by the opinions in the Annual Report and Accounts (pages 115 to 118).

The regulatory report was approved by the Board on the 21 June 2016 and was signed on their behalf by:

M. Corben
Director

Independent auditor's report (Regulatory Annual Performance Report – section 1 and 2 tables)

Independent auditor's report to the Water Services Regulation Authority (the "WSRA") and Directors of Bazalgette Tunnel Limited.

Opinion on the Annual Performance Report

In our opinion, the Annual Performance Report:

- fairly presents in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA and the accounting policies set out on pages 84 to 86 (including the accounting separation methodology), the state of the Company's affairs at 31 March 2016 and its profit and its cashflow for the year then ended; and
- has been properly prepared in accordance with Condition F, the Regulatory Accounting Guidelines and the accounting policies (including the accounting separation methodology).

Basis of preparation

Financial information other than that prepared on the basis of UK GAAP does not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in statutory financial statements prepared in accordance with the Companies Act 2006. The Annual Performance Report is separate from the statutory financial statements of the Company and has not been prepared under the basis of United Kingdom Generally Accepted Accounting Practice ("UK GAAP").

In forming our opinion on the Regulatory Accounting Statements within the Annual Performance Report, which is not modified, we draw attention to the fact that the Annual Performance Report has been prepared in accordance with Condition F, the Regulatory Accounting Guidelines, the accounting policies (including the accounting separation methodology) set out in the statement of accounting policies and under the historical cost convention.

The Regulatory Accounting Statements have been drawn up in accordance with Regulatory Accounting Guidelines with a number of departures from UK GAAP. A summary of the effect of these departures from Generally Accepted Accounting Practice in the Company's statutory financial statements is included in the tables within section 1.

Regulatory Reporting

What we have audited

The tables within the Company's Annual Performance Report that we have audited ("the Regulatory Accounting Statements") comprise:

- the regulatory financial reporting tables comprising the income statement (table 1A), the statement of comprehensive income (table 1B), the statement of financial position (table 1C), the statement of cash flows (table 1D) and the net debt analysis (table 1E) and the related notes; and
- the historical cost analysis of fixed assets for wholesale and retail (table 2D). In line with the Ofwat guidance issued on 27 May 2016, other section 2 tables have neither been presented nor audited.

The financial reporting framework that has been applied in their preparation comprises the basis of preparation and accounting policies set out in the notes to the Annual Performance Report.

In applying the financial reporting framework, the directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

We have not audited the Outcome performance table (table 3A), the additional regulatory information in tables 4A to 4I, or the bespoke information in tables 5A to 5C.

This report is made, on terms that have been agreed, solely to the Company and the WSRA in order to meet the requirements of Condition F of the Project Licence granted by the WSRA to the Company as infrastructure provider under section 17FA of the Water Industry Act 1991 (as has effect under paragraph 3(2) of Schedule 1 of the Water Industry (Specified Infrastructure Projects) (English Undertakers) Regulations 2013) ("the SIP Regulations") ("Condition F"). Our audit work has been undertaken so that we might state to the Company and the WSRA those matters that we have agreed to state to them in our report, in order (a) to assist the Company to meet its obligation under Condition F to procure such a report and (b) to facilitate the carrying out by the WSRA of its regulatory functions, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the WRSA, for our audit work, for this report or for the opinions we have formed.

Respective responsibilities of the WSRA, the Directors and Auditors

As explained more fully in the Statement of Directors' Responsibilities set out on page 73, the directors are responsible for the preparation of the Annual Performance Report and for their fair presentation in accordance with the basis of preparation and accounting policies. Our responsibility is to audit and express an opinion on the Regulatory Accounting Statements within the Annual Performance Report in accordance with International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)"), except as stated in the section on 'What an audit of the Annual Performance report involves' below, and having regard to the guidance contained in Audit 05/03 'Reporting to Regulators of Regulated Entities' issued by the Institute of Chartered Accountants in England and Wales. Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

What an audit of the Annual Performance Report involves

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

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

Opinion on other matters prescribed by Condition F

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

- proper accounting records have been kept by the appointee in line with paragraph 1.1 of Condition F; and
- the Regulatory accounting statements are in agreement with the accounting records and returns retained for the purpose of preparing the Annual Performance report.

Other matters

The nature, form and content of the Annual Performance Report is determined by the WSRA. It is not appropriate for us to assess whether the nature of the information being reported upon is suitable or appropriate for the WSRA's purposes. Accordingly, we make no such assessment. Our opinion on the Annual Report is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2016 on which we report, which are prepared for a different purpose. Our audit report in relation to the statutory financial statements of the Company (our 'statutory audit') was made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our statutory audit work was undertaken so that we might state to the Company's members those matters we are required to state to them in a statutory audit report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume responsibility for any other purpose or to any other person to whom our statutory audit report is shown or into whose hands it may come, save where expressly agreed by our prior consent in writing.

John Luke
For and on behalf of KPMG LLP
Chartered Accountants
15 Canada Square
London, E14 5GL
21 June 2016

Notes:

1. The maintenance and integrity of the Company's website is the responsibility of the directors and the maintenance and integrity of the Regulator's website is the responsibility of the Regulator; 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 Annual Performance Report since they were initially presented on the websites.
2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements and The Annual Performance Report may differ from legislation in other jurisdictions.

Regulatory Reporting

Independent auditor's report (Condition K Certificate) Report of KPMG LLP to Bazalgette Tunnel Limited ('the Company') and the Water Services Regulation Authority ('the WSRA') under Licence Condition F4.1

In accordance with the terms of our engagement letter dated 14 June 2016, we have examined the Company Condition K Certificate as defined in the licence, dated 21 June 2016 (the "Certificate") which is attached to this report and initialled for identification purposes, in conjunction with the completion of our audit of the Annual Performance Report of the Company for the year ended 31 March 2016.

Respective duties of directors and auditor

The directors of the Company have sole responsibility for the preparation of the Condition K Certificate – in accordance with Condition M5 of the licence. The Certificate is presented as set out in the Project Licence by the WSRA of the Company as an infrastructure provider under section 17FA of the Water Industry Act 1991 (as has effect under paragraph 3(2) of Schedule 1 of the Water Industry (Specified Infrastructure Projects) (English Undertakers) Regulations 2013) ("the SIP Regulations")).

As specified in our engagement letter dated 14 June 2016, it is our responsibility to review the Certificate and report to you whether we are aware of any inconsistencies between that Certificate and the Annual Performance Report and any information which we obtained in the course of our work as the Company's Auditor.

For the avoidance of doubt, our audit of the Annual Performance Report of the Company for the year ended 31 March 2016 was and is not directed towards meeting the requirements of the Company or the directors under the terms of the Condition. We have not carried out and will not carry out specific procedures designed to verify the substance of the matters certified by the directors of the Company. Our sole responsibility is to review the Certificate for consistency with our knowledge of the Company's financial affairs gained in the course of our normal audit work. Furthermore, we have not carried out any audit procedures on the Company since 21 June 2016, the date of our audit opinion on the Annual Performance Report of the Company for the year ended 31 March 2016.

This report is made solely to the Company as a body and the WSRA in accordance with the Regulatory Accounting Guidelines and other relevant material issued by the WSRA and the terms of our engagement with the Company. Our examination has been undertaken so that we might state to the Company and the WSRA those matters that we have agreed to state to them in our report 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 as a body, and the WSRA, for our report, or for the opinions we have formed. The terms of our engagement do not confer benefits on any other parties and exclude the application of the Contracts (Rights of Third Parties) Act 1999.

This report has been released to the Company and to the WSRA on the basis that it shall not be copied, referred to or disclosed, in whole (save for the Company's or the WSRA's own internal purposes) or in part, without our prior written consent. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company (and the WSRA) for our work, for this report, or for the opinions we have formed. (We will accept such responsibility to the WSRA on condition that the WSRA agrees in writing to the WSRA's Contract by signing the WSRA's Contract.)

Basis of our review

Our work consisted of an examination of the Certificate signed by the Directors, to determine whether there were any inconsistencies with our findings arising from the audit of the Annual Performance Report and any information which we obtained in the course of our work as the Company's Auditor.

Findings

In our opinion, nothing has come to our attention during the course of our audit work on the Annual Performance Report of the Company for the year ended 31 March 2016 that would indicate any inconsistencies, in all material respects, between the Certificate and the Annual Performance Report and any information which we obtained in the course of our audit work on the Annual Performance Report of the Company for the year ended 31 March 2016.

KPMG LLP
Chartered Accountants
15 Canada Square
London, E14 5GL

Glossary

Term	Definition
Community Liaison Working Groups	Stakeholder groups that Tideway has set up near the active construction sites, to engage and share information with local residents.
Consents	The permissions required from third parties (e.g. local authorities) for Tideway to deliver the project.
Employee Project Induction Centre programme	Tideway's compulsory Health Safety and Wellbeing training programme for every person working on the project.
Encompass diversity programme	Encompass is the Project's diversity forum and is open to all working on Tideway.
Handover	The point at which the tunnel is integrated into the wider sewer network, commissioning tests have been successfully completed and Thames Water has issued a handover certificate.
Licence	The licence granted to Tideway by Ofwat on 24 August 2015.
Main Works Contracts	The contracts between Tideway and the main works contractors to engineer, procure, construct and commission the three sections (West, Central and East) of the Thames Tideway Tunnel.
More by river	Tideway's strategy to enhance the use of the River Thames for logistics.
Regulatory Baseline	The baseline cost of delivering the tunnel of £3.1bn in 2014/15 prices, as set out in Tideway's licence.
Regulatory Capital Value (RCV)	The value of Tideway's capital base, as calculated in line with our licence.
Revenue Agreement	The agreement under which Thames Water collects revenue from its wastewater customers on Tideway's behalf.
Right Way	Tideway's approach to introducing transformational Health, Safety and Wellbeing.
Right Start	This is about getting the Health, Safety and Wellbeing basics right from the very start to help us avoid incident spikes often seen at the start of major projects.
System Acceptance	System Acceptance is the point at which the entire Thames Tideway Tunnel system is accepted to serve as part of TWUL's wastewater system.
Thames Skills Academy	The Port of London Authority's facility, supported by Tideway, to train new river workers.
Thames Water Works	Thames Water's activities, including enabling and interface works, which are necessary for the development and connection of the Thames Tideway Tunnel to the sewer network.
Tideway Alliance	The alliance between Tideway, Thames Water, the main works contractors and the system integrator, designed to incentivise collaborative working, realise synergies and share best practice.

Name & Registered Office:
Bazalgette Tunnel Limited,
The Point,
37 North Wharf Road,
Paddington,
London, W2 1AF

Company number: 09553573
Registered in England and Wales

Visit: **www.tideway.london**
Email: **info@tideway.london**

FSC
www.fsc.org
RECYCLED
Paper made from recycled material
FSC® C016486