Understanding Tax: A Guide

Total tax report
Northumbrian Water Group
July 2024

NWG
living water

Foreword from our Chief Financial Officer

Our vision is to be the national leader in the provision of sustainable water and wastewater services.

Our Purpose is caring for the essential needs of our communities and environment, now and for generations to come. We do this by providing reliable and affordable water and wastewater services for our customers. We make a positive difference by operating efficiently and investing prudently, to maintain a sustainable and resilient business.

Contributing to society through tax payments is a cornerstone of our responsibility. These taxes play a crucial role in financing essential public services, investing in our local communities and delivering public infrastructure. Building trust with our customers, colleagues, and stakeholders is paramount to us. That's why we are dedicated to paying our fair share of taxes and helping you understand how we handle taxes and the big impact we have through them. We promise to report our taxes in a clear way so everyone knows what's going on and we can be held accountable for it.

Our approach to tax

We handle our taxes as seriously and responsibly as we handle every other part of our business, in line with our commitment to corporate responsibility. We only take tax positions that make sense and follow the law, and if we need help understanding, we ask trustworthy professionals to keep us on track.
If we can receive any tax benefits or incentives available under the law, we will do so as long as it's in line with what the law is meant for. We aim to have an open and positive relationship with HMRC regarding all tax matters, keeping them informed about important transactions and developments in our business. Any communication with HMRC is done professionally and respectfully.

We hope you find this report informative.

Matt Williams
Chief Financial Officer
July 2024

Purpose of this report and summary of the taxes we pay

The purpose of this report is to provide information about the various taxes we pay to collect and complement the tax disclosures made in our **Annual Report and Financial Statements**. It also explains how we comply with our **Tax Strategy**.

We employ just over 3,400 people and together, we provide water and sewerage services to almost 4.4 million people. Every day we supply 1.1 billion litres of water. With that comes a significant level of investment in the form of both operating costs and capital expenditure.

We pay and collect taxes that arise from these transactions, and they can be summarised into these broad categories:

- **Corporation tax paid**
  An amount we pay on our taxable profits, less any refunds we get for overpayments in previous years.

  Taxable profits are how much money we make before we pay tax. We start with the profit number we see in the financial statements but then we make some adjustments. A key adjustment for us is depreciation - how much the value of buildings or equipment goes down over time. Instead of counting that as a loss, we add it back to the profit number. Then, we claim something called "capital allowances" instead. These are tax deductions that businesses can get for spending money on certain things. By making these adjustments, we get a more consistent picture of how much money the company is making that is subject to taxes. Corporation tax is used by the government to fund national services such as the NHS, education, defence, and welfare as examples.

Capital expenditure is when a company spends money to buy things that will help it in the long run, like new equipment for a factory, office repairs or acquiring software for business operations.

- **Business rates paid**
  A form of tax that we pay on the commercial buildings we occupy such as our water treatment works, wastewater treatment works and support buildings. Business rates contribute to local and central government revenue and help fund services such as education, waste management, and infrastructure.

- **Employment taxes (paid and collected)**
  Consisting of National Insurance Contributions (NIC), which are paid by employers and by employees, Pay As You Earn (PAYE) which is paid by employees, and The Apprenticeship Levy which is paid by employers. As an employer of over 3,400 people the amount we collect from employees and the amount we pay directly to HMRC is an important contribution to the tax authorities. Employment taxes play a crucial role in financing social welfare programs and public services while also making sure our people receive benefits, such as pensions and healthcare.

- **Environmental taxes (paid)**
  Including Climate Change Levy (CCL), a tax on the energy we use, Carbon Price Support (CPS), a tax on how much carbon is in the fuels we use to generate electricity, Landfill Tax, a tax on the amount of waste we dispose of at landfill sites, and Vehicle Excise Duty, also known as road tax which includes higher rates for vehicles with higher CO2 emissions.

  Environmental taxes contribute to the UK's efforts to mitigate climate change, reduce pollution, and transition to a more sustainable economy and so this is an area where our leading efforts to restore and regenerate the environment is rewarded through lower taxes. You can read more about our environmental commitments in our **Environment Strategy**.

- **Indirect taxes (paid and collected)**
  Value Added Tax (VAT) is an indirect tax charged on goods and services, which are either bought from our suppliers or sold to our customers. The provision of water and wastewater services are zero-rated (i.e. the rate of VAT is 0%) for most of our customers, so generally customers do not incur additional costs for VAT on their water bills.

The VAT we pay to our suppliers is mainly incurred at the standard rate being 20%. That means we can make a VAT reclaim from HMRC. Insurance premium tax (IPT) is another indirect tax and this is imposed on our general insurance policies that we pay for, such as vehicle insurance, commercial insurance, and buildings insurance.

- **Regulatory service fees (paid)**
  We hold licences with the Environment Agency that allow us to take water from the natural environment – we treat this and supply clean, clear and great tasting drinking water to our customers. We also hold permits with the Environment Agency to allow us to discharge treated water back into the environment in a controlled manner.

We have calculated our total tax contribution by combining the taxes paid together with those we collect and remit on behalf of the Government.

Leading in good business practices

As a large company, we are subject to HMRC's Business Risk Review+. We have been assessed as 'low risk,' the lowest rating possible on a scale that includes low, medium, medium-high, and high risk.

For the third successive year, we were the only water company awarded the Good Business Charter, supported by the Confederation of British Industry and the Trades Union Congress.

This involves demonstrating good practice against a series of key components, including employment practices, environmental responsibility, fair tax, and procurement.

We publish a range of information about our services and performance, and financial statements. This helps to assure our customers and stakeholders that we're delivering what they've told us they need and want from Northumbrian Water and Essex & Suffolk Water.

It's important that we have robust assurance arrangements to make sure this information is accurate, clear, and transparent. This is essential to building and maintaining a high level of trust and confidence with our customers and stakeholders.

We have a requirement under our Instrument of Appointment and Ofwat's Regulatory Accounting Guidelines, for the Regulatory Financial Statements in the Annual Performance Report to be externally audited. This covers appointed business taxation.

You can read more about assurance **here**.

Our total tax contribution

We have calculated our total tax contribution by combining the taxes paid together with those we collect and remit on behalf of the Government.

We had a very small corporation tax payment this year of £2.9m which is explained on **page 6**.

Tax paid +	Tax collected =	Total tax contribution
These are taxes paid directly to the tax authorities or other government bodies, including employer NICs, business rates, environmental taxes, IPT and abstraction licences.	These are taxes generated by our operations but are not a direct cost to us. We collect these taxes and pay them on to the tax authorities or other government bodies.	**This is the total value of taxes that we are responsible for, being the sum of all the taxes paid and collected.**

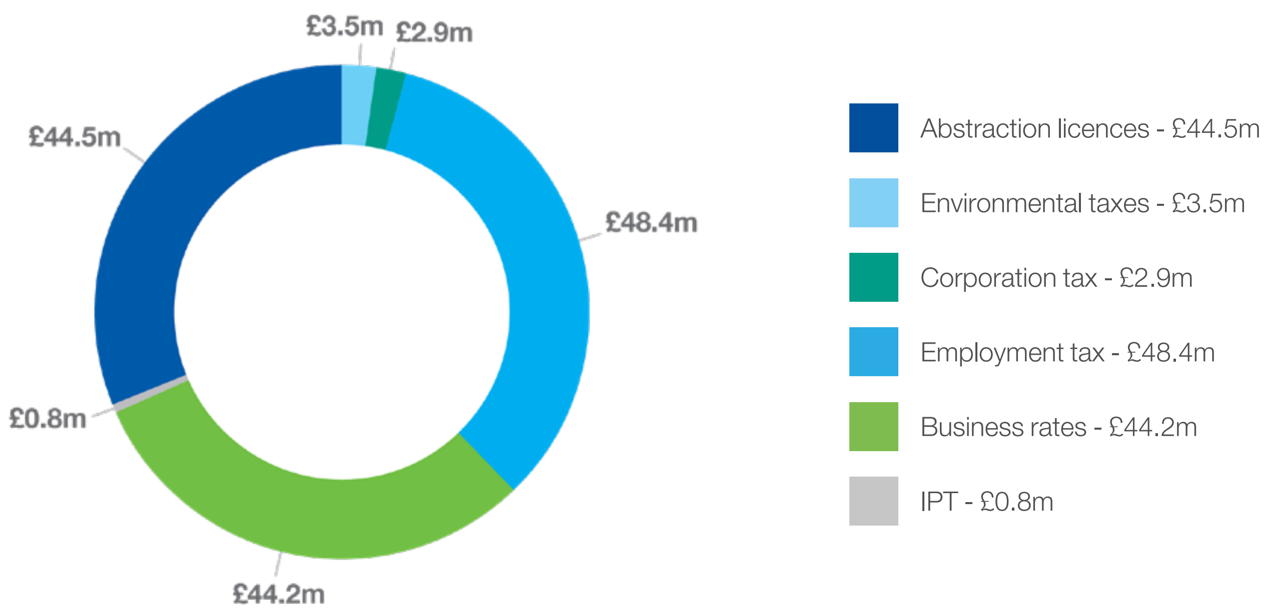
Group revenue
£918.9m

Loss before tax
£1.2m

Tax paid
£111.8m

Tax collected
£32.5m

Total tax contribution
£144.3m



Tax in our Financial Statements

Most of the taxes that we pay such as employers NIC, business rates, environmental taxes, IPT and abstraction licences are included in our Operating costs line within the Income Statement, shown below. The Taxation line specifically refers to corporation tax, which is charged on our taxable profits. Taxable profits are how much money we make before we pay tax, but then we make the adjustments, as explained earlier on **page 3**. Taxable profits are then subject to UK corporation tax at the current rate of 25%.

Allowable deductions

The biggest adjustments we make to our loss before tax are in relation to how much we spend on fixed assets, such as buildings, machinery and equipment, and over the last few years there have been some changes to rules on how these adjustments are calculated.

After Covid-19, the UK Government wanted to encourage businesses to invest in certain capital assets like equipment or machinery. They introduced a special rule called the 'super deduction' for two years until March 31, 2023. This rule let companies deduct 130% of their spending on these assets from their taxable profits.

Later, they replaced the 'super deduction' with something called the 'expensing regime.' With this new rule, companies can deduct 100% of the cost of certain big purchases upfront from their taxable profits.

We make use of available incentives, such as the super deduction, and the expensing regime as outlined in our **Tax Strategy**.

The new rules about how we can deduct the cost of big purchases mean we don't have to pay any corporation tax for the year ended March 31, 2024 for the main part of the group. This is because we've spent a lot of money on assets that qualify for this deduction. The good thing is, we get to take this deduction sooner than we would have before. Even though we don't have to pay tax now, we'll have to record it through something called deferred tax, which means accounting for assets where tax relief has been given earlier or later than it has gone through our financial statements.

We have to pay our corporation tax in advance of knowing what the final profit or loss for the group is, which means sometimes we have to pay more or sometimes we get a refund once the final calculations are done. We overpaid corporation tax in previous years so during this year we got a refund of £19.7m.

We also have another part of the group which isn't included in the results below. This relates to two water treatment works in Scotland. We don't need to spend as much annually on capital assets in these business as they are still quite new, which means we don't get the same tax relief. We paid corporation tax of £2.9m for these businesses.

Consolidated Income Statement*

for the year ended 31 March 2024

	Note	2024 £'m	2023 £'m
Continuing operations			
Revenue	2	918.9	861.2
Operating costs	3	(685.7)	(638.7)
Operating profit		**233.2**	**222.5**
Finance costs	7	(236.8)	(278.2)
Finance income	7	2.4	2.1
Net finance costs		(234.4)	(276.1)
Loss before taxation		**(1.2)**	**(53.6)**
Taxation	8a	(0.5)	21.5
Loss for the year attributable to the shareholder of the Company		**(1.7)**	**(32.1)**

*Consolidated Northumbrian Water Limited

Corporation tax challenges arising from the digital era

In December 2021, the Organisation for Economic Co-operation and Developments (OECD) introduced new rules called Pillar Two Model Rules. These rules aim to set a minimum global corporation tax rate of 15%. This is to tackle concerns that big multinational companies aren't paying their fair share of taxes because they shift profits around to different countries with low rates of corporation tax. Then, in December 2022, the OECD released transitional safe harbour rules. These are temporary measures meant to make things easier for countries that don't pose as much of a tax risk.

In 2023, the UK put into effect the Pillar Two top-up tax rules, which means they made them into law. These rules started being used from 1 January 2024.

As a big company making over €750 million in total revenue, we're affected by these new tax rules. This means we have to calculate how much tax we're paying in each country we do business in, and if it's less than 15%, we have to pay extra tax to make up the difference.

We don't expect to pay extra tax for our operations in any of the countries where we do business. That's because those countries fall under the OECD transitional safe harbour rules, which the UK has also adopted.

For more details on our finances **go to our website**.

Conclusion

In conclusion, this guide highlights our commitment to transparency and our significant contribution to public finances through taxes. Our total tax contribution reflects our role as a responsible business and our dedication to supporting the economic and social well-being of the communities in which we operate.

We are proud of our contribution and the positive impact it has on society, enabling public services and infrastructure that benefit everyone.

We remain dedicated to maintaining the highest standards of compliance and ethical conduct in all our tax related activities.

Thank you for taking the time to read our tax guide. We value your interest and trust in our company.

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