INTRODUCTION
This Directors' report is prepared in accordance with the provisions of the Companies Act 2006 and regulations made thereunder. It comprises pages 58 to 76 and 99 to 101 as well as the following matters which the Board considers are of strategic importance and, as permitted by legislation, has chosen to include in the strategic report rather than the Directors' report:

- risk management systems (page 51 of the strategic report)
- likely future developments of the Company (page 17 of the strategic report)
- important post-balance sheet events (note 45 of the notes to the financial statements)
- all matters relating to sustainability, which include details of the Group's carbon emissions (page 45 of the strategic report) and information relating to employee involvement (page 50) of the strategic report, as well as the disclosure below).

In addition, the Directors' report includes the following disclosures (and any other disclosures) which are incorporated by reference:

- financial risk management (note 3 of the notes to the financial statements)
- financial instruments (notes 2(o) and 18 of the notes to the financial statements).

BOARD OF DIRECTORS
The Directors in office as at the date of this report (all of whom served during the year) are named on pages 60 and 61. In addition, Ken Harvey, the previous Chairman, and Gerard Connell, the previous Senior Independent Director, served during the year until their retirement from the Board on 31 July 2015.

FINANCIAL RESULTS AND DIVIDEND
The Directors recommend a final dividend of 23.12p per ordinary share to be paid on 2 September 2016 to shareholders on the register on 8 July 2016, making a total dividend for the year of 33.58p, the cost of which will be £138.5 million, resulting in a transfer to reserves of £13.6 million. The strategic report on pages 18 to 25 analyses the Group's financial results in more detail and sets out other financial information.

DIRECTORS' INSURANCE AND INDEMNITIES
The Directors have the benefit of the indemnity provisions contained in the Company's Articles of Association ('Articles'), and the Company has maintained throughout the year Directors' and officers’ liability insurance for the benefit of the Company, the Directors and its officers. The Company has entered into qualifying third party indemnity arrangements for the benefit of all its Directors in a form and scope which comply with the requirements of the Companies Act 2006 and which were in force throughout the year and remain in force.

EMPLOYMENT POLICIES AND EMPLOYEE INVOLVEMENT
The Group has a culture of continuous improvement through investment in people at all levels within the Group. The Group is committed to pursuing equality and diversity in all its employment activities including recruitment, training, career development and promotion and ensuring there is no bias or discrimination in the treatment of people. In particular, applications for employment are welcomed from persons with disabilities, and special arrangements and adjustments as necessary are made to ensure that applicants are treated fairly when attending for interview or for pre-employment aptitude tests. Wherever possible the opportunity is taken to retrain people who become disabled during their employment in order to maintain their employment within the Group. Information regarding the Group's workplace policies is provided on page 48.

The Board has a diversity policy and encourages gender diversity in particular. Further details of the Board’s diversity policy are set out in the report of the Nomination Committee on page 74, and information regarding the diversity of the workforce is provided on page 50.

Employees are consulted regularly about changes which may affect them either through their trade union-appointed representatives or by means of the elected staff council which operates in South West Water for staff employees.

These forums, together with regular meetings with particular groups of employees, are used to ensure that employees are kept up to date with the business performance of their employer and the financial and economic factors affecting the performance of the Group. The Group also cascades information monthly to all employees to provide them with important and up to date information about key events and to obtain feedback from them. Further information about employment matters relating to the Group is set out on pages 48 to 50 of the strategic report.

The Group encourages share ownership among its employees by operating an HM Revenue & Customs approved Sharesave scheme and Share Incentive Plan. Following shareholder approval at the 2014 AGM, these were amended to provide for the increased savings limits approved by government. At 31 March 2016 around 44% of the Group’s employees were participating in these plans.

HUMAN RIGHTS AND ANTI-SLAVERY
The Group is fully supportive of the principles set out in the UN Declaration of Human Rights, and the Group Ethics Policy outlines the high standards of employment practice with which everyone in Pennon Group is expected to comply. The Group also supports the International Labour Organization’s core conventions for the protection and safety of workforces wherever they may be throughout the Group.

The Group’s commitment to ensuring the human rights of its employees are not infringed extends to those of its suppliers. Supplier codes of conduct are in place to ensure that people are treated fairly and with respect and dignity.
In addition, following appropriate due diligence we have put in place policies and procedures to assess, monitor and reduce the risk of modern slavery and human trafficking occurring in our businesses and supply chains. Risk assessments of any high risk supply partners have been completed by Viridor, South West Water and Bournemouth Water to ensure compliance with the Modern Slavery Act across the Group and we are in the process of drafting our anti-slavery and human trafficking web-based statement for the financial year 2016/17. This will be available at www.pennon-group.co.uk in due course.

RESEARCH AND DEVELOPMENT
Research and development within the Group involving water and waste treatment processes amounted to £0.1 million during the year (2014/15 £0.1 million).

OVERSEAS BRANCHES
The Company has no overseas branches.

PENNON GROUP DONATIONS
No political donations were made or political expenditure incurred and no contributions were made to a non-EU political party (2014/15 nil).

PURCHASE OF OWN ORDINARY SHARES
The Company has authority from shareholders to purchase up to 10% of its own ordinary shares (as renewed at the Annual General Meeting in 2015), which was valid as at 31 March 2016 and remains currently valid. No purchases were made during the year. As at 1 April 2015, 389,515 shares were held in treasury, with a nominal value of £158,533 and representing 0.1% of issued share capital. 379,159 treasury shares representing 0.09% of issued share capital as at 1 April 2015 were reissued during the year under the Company’s employee share schemes for proceeds of £2.5 million.

DISCLOSURES REQUIRED BY PUBLICLY TRADED COMPANIES
The following disclosures are made pursuant to Part 6 of Schedule 7 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 and Rule 7.2.6.R of the UK Listing Authority’s Disclosure and Transparency Rules (DTR).

As at 31 March 2016:

a) Details of the Company’s issued share capital, which consists of ordinary shares of nominal value 40.7 pence each, are set out in note 33 to the financial statements on page 160. All of the Company’s issued shares are fully paid up, rank equally in all respects and are listed on the Official List and traded on the London Stock Exchange. The rights and obligations attaching to the Company’s shares, in addition to those conferred on their holders by law, are set out in the Company’s Articles, copies of which can be obtained from Companies House in the UK or by writing to the Group Company Secretary at the Company’s registered office;

b) There are no restrictions on the transfer of issued shares of the Company or on the exercise of voting rights attached to them, except where the Company has exercised its right to suspend their voting rights or to prohibit their transfer following the omission of their holder or any person interested in them to provide the Company with information requested by it in accordance with Part 22 of the Companies Act 2006 or where their holder is precluded from exercising voting rights by the Financial Conduct Authority’s Listing Rules or the City Code on Takeovers and Mergers. There are no persons with special rights regarding control of the Company. No shares issued under the employee share schemes have rights with regard to control of the Company that are not exercisable directly by the employees;

c) Details of significant direct or indirect holdings of securities of the Company are set out in the shareholder analysis on page 174. The Company is not aware of any agreements between shareholders which may result in restrictions on the transfer of securities or on voting rights;

d) The Company’s rules about the appointment and replacement of Directors are contained in the Articles and accord with usual English company law provisions. The powers of Directors are determined by UK legislation and the Articles in force from time to time. Changes to the Articles must be approved by the Company’s shareholders by passing a special resolution;

e) The Directors have the power to make purchases of the Company’s own shares in issue as set out above. The Directors also have the authority to allot shares up to an aggregate nominal value of: (i) £55,765,009 (such amount to be reduced by any shares allotted or rights granted under (ii) below in excess of £55,765,009); and (ii) £111,530,018 by way of a rights issue (such amount to be reduced by any shares allotted or rights granted from (i)) above), which was approved by shareholders at the 2015 Annual General Meeting (AGM). In addition, shareholders approved a resolution giving the Directors a limited authority to allot shares for cash other than pursuant to the Company’s employee share schemes and the scrip dividend alternative;

f) There are a number of agreements which take effect, alter or terminate upon a change of control of the Company following a takeover bid, such as bank loan agreements, eurobond documentation, hybrid capital securities documentation, private placement debt and employees’ share plans. This may result in certain funding agreements being altered or repaid early. The impact on employees’ share plans is not considered significant; and

g) There are no agreements between the Company and its Directors or employees providing for compensation for loss of office or employment that occurs because of a takeover bid.

GOING CONCERN
Having considered the Group’s funding position and financial projections the Directors have a reasonable expectation that the Group has adequate resource to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the financial statements.
STATEMENT OF DIRECTORS’ RESPONSIBILITIES

The Directors are responsible for preparing the annual report, the Directors’ remuneration report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the Group and Company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union.

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 the Company and of the profit or loss of the Group for the year.

In preparing these financial statements the Directors are required to:

- select suitable accounting policies and then apply them consistently
- make judgements and accounting estimates which are reasonable and prudent
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements.

The Directors confirm that they have complied with the above requirements in preparing the financial statements.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company’s transactions, and disclose with reasonable accuracy at any time the financial position of the Group and the Company; and enable them to ensure that the financial statements and the Directors’ remuneration report comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the International Accounting Standards (IAS) Regulation. They are also responsible for safeguarding the assets of the Group and the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Each of the Directors, whose names and functions are listed on pages 60 and 61, confirms that, to the best of his or her knowledge:

i) The financial statements, which have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Group and of the Company.

ii) The strategic report (pages 4 to 55) and the Directors’ report (pages 99 to 101) include a fair review of the development and performance of the business during the year and the position of the Company and the Group at the year end, together with a description of the principal risks and uncertainties they face.

iii) Following receipt of advice from the Audit Committee, that the annual report, taken as a whole, is fair, balanced and understandable, and provides the information necessary for the shareholders to assess the Group’s performance, business model and strategy.

The Directors are responsible for the maintenance and integrity of the Company’s website www.pennon-group.co.uk. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

STATEMENT AS TO DISCLOSURE OF INFORMATION TO THE AUDITOR

i) So far as each of the Directors in office at the date of the signing of the report is aware, there is no relevant audit information of which the Company’s auditor is unaware; and

ii) each of the Directors has taken all the steps each Director ought to have taken individually as a Director in order to make himself or herself aware of any relevant audit information and to establish that the Company’s auditor is aware of that information.

The Directors’ report consisting of pages 58 to 76 and 99 to 101 was approved by the Board on 24 May 2016.

By Order of the Board

Helen Barrett-Hague
Group Company Secretary
24 May 2016