

Registered no: 02366661 (England and Wales)

**Thames Water Utilities Limited**

Annual report and financial statements

For the year ended 31 March 2011

# Annual report and financial statements for the year ended 31 March 2011

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## **Directors and Advisors at 31 March 2011**

### **Directors**

Sir Peter Mason KBE (Chairman)  
M W Baggs  
E Beckley  
R Blomfield-Smith  
M W Braithwaite  
C R Deacon  
G I W Parsons  
A F C DeP Santos  
D J Shah OBE  
S F Shine OBE  
M S W Stanley  
R E Verrion

### **Independent non-executive directors**

Dame D M Hutton CBE  
M J Pavia  
E C Richards

### **Registered auditor**

KPMG Audit Plc  
Chartered Accountants  
15 Canada Square  
London  
E14 5GL

### **Company Secretary & registered office**

J E Hanson  
Clearwater Court  
Vastern Road  
Reading  
Berkshire  
RG1 8DB

# Thames Water Utilities Limited

## Chairman's introduction

This has been another very successful year for Thames Water. The Company's operational performance has been excellent and the Company has again invested over £1bn to renew ageing assets and continue the improvements in the Company services to a growing number of customers. This level of investment will continue for at least the next 3 years.

In this period, good progress has been made on the major projects at the five main sewage treatment works discharging to the tidal River Thames. These, along with the Lee Tunnel, which will intercept the largest sewage overflow in London, will provide a long term improvement to the water quality of London's major rivers.

Looking further ahead, the Company has successfully completed the first phase of its public consultation on the much longer and more complex Thames Tunnel, which is being designed to intercept a further 34 unsatisfactory sewage overflows. While continuing with the design and consultation processes, the Company is giving high priority to working with the Government and Water Services Regulation Authority ("Ofwat") on establishing appropriate delivery and funding mechanisms for this immense project.

I am particularly pleased to report that the Company has achieved its leakage target for the fifth successive year, despite one of the coldest starts to a winter on record. This is significant because leakage from cast iron pipes, which are widespread in London, increases dramatically as temperatures fall. The management team has considerably increased the resources devoted to detecting and fixing leaks as early as October and made further increases as temperatures fell and remained low.

The Company is proud to have once again provided its customers with the highest quality drinking water from any major supplier; pleased that customer complaints fell by 6.7% during the year; and encouraged by a further year during which all of its 349 sewage treatment works have maintained 100% compliance with environmental standards.

The Company's financial performance has, in all the circumstances, been satisfactory. Despite cost pressures from inflation at almost 5%, efficiencies have limited the rise in operating costs to 3.4%. Turnover has been almost the same as 2010, with real increases in prices largely balanced out by reduced demand for water from metered customers choosing to use less water. Static turnover, increased operating expenditure and higher depreciation have led to a fall in operating profit of 10.6% to £600.2m.

The Company's draft Water Resources Management Plan met with mixed reviews in the year. It was encouraging that the plans for the next 15 years received broad endorsement but disappointing that the longer term aspects were not approved at this stage. There is more work to do in considering a wider range of potential long term supply and demand options. This will be concluded in time for the next plan.

The Company continues to be fully and positively engaged in the many consultations currently taking place with regard to the future structure and regulation of the industry. There is considerable opportunity through this work to improve efficiency and quality of services to customers. Throughout these discussions, it is encouraging to note the understanding of all stakeholders that for a company like Thames Water, with an annual investment programme of over £1bn, the raising of finance at an attractive cost is a significant challenge but a key deliverable. Maintaining investors' confidence can only be achieved through efficient delivery of the capital programme underpinned by a stable and transparent regulatory environment.

# Thames Water Utilities Limited

## Chairman's introduction

During the year Willem Smit completed his term as a Non Executive Director and I thank him for his valuable contribution. We have also welcomed Dame Deirdre Hutton CBE and Ed Richards as additional Non Executive Directors, bringing wide experience and a valuable external perspective.

This has in many ways been a particularly challenging year for the Company and I want to record my thanks to all the people in Thames Water for their outstanding performance in the period.

A handwritten signature in black ink, appearing to read 'P. Mason', with a horizontal line underneath.

**Sir Peter Mason KBE**

Chairman

9 June 2011

# Thames Water Utilities Limited

## Chief Executive Officer's Business review

The following business review forms part of the Directors' report.

### Business review

#### Introduction

Unless otherwise stated, all current year data included in this review is for the year ended 31 March 2011 ("2011").

#### Nature of business

#### Background

The Company is the largest supplier of water and provider of sewerage services in the UK, based on the number of customers served. It is one of 10 companies currently holding appointments as water and sewerage undertakers<sup>1</sup> in England and Wales, with a further 11 companies holding appointments as water only undertakers.

In total, the area served by the Company occupies approximately 13,331 km<sup>2</sup> and encompasses more than 9% of the area of England and Wales. This includes London and extends as far as Cirencester in the west, Dartford in the east, Banbury in the north and Haslemere in the south. This area has a population of about 14m people, which represents nearly a quarter of the total population of England and Wales. In approximate terms, the Company supplies 3.6m properties (just over 8.7m people) with water, and collects sewage from 5.1m properties (about 13.8m people), including 97% of households in its sewerage region.

The Annual Performance Report 2011, which incorporates the Corporate Responsibility Report, does not form part of this report. It provides further information regarding the Company's regulatory and operational performance and is available on the Company's dedicated website: [www.thameswater.co.uk/cr](http://www.thameswater.co.uk/cr)

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<sup>1</sup> A company that has been appointed to provide water and/or sewerage services to customers in England and Wales is known as an "undertaker". The Company's Instrument of Appointment - usually referred to as "the Licence" - was issued by the Secretary of State for the Environment in August 1989

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Highlights

This was the first year of the new AMP, which has been financially challenging for the Company. However the Company has achieved its key regulatory outputs, and outperformed the Final Determination ("FD") by almost £13m.

Other achievements include:

- Delivering over £1bn of investment in the year.
- Customer complaints fell by 6.7% (2010: 14.0%).
- Staging the water industry's first Health and Safety Excellence Awards for the main contractors carrying out the work on the Company's 2010-15 investment programme.
- Meeting the Company's water-efficiency target; Ofwat set a goal of saving 4Mld by encouraging water-wise behaviour by customers. The Company saved 5Mld.
- Opening mainland UK's first desalination plant at Beckton in East London so that 1m people when needed can be supplied with high-quality tap water taken from brackish water in the tidal River Thames.
- Meeting the Company's annual leakage target despite the coldest start to a winter in 100 years, and delivering 100% security of water supply to all its customers.
- Maintaining the Company's drinking water quality performance at the high level of 99.97% compliance.
- Agreeing terms to build Europe's first reactor to make premium-grade phosphate fertiliser, derived from struvite deposits on pipes at Slough sewage works.
- Reducing emissions by 11% on 1990 levels, despite serving 3m more customers today than 20 years ago, and becoming the first UK utility to be re-accredited with the Carbon Trust Standard.
- Continuing focus on meeting customers needs including further reduction of 182 properties at risk of sewer flooding.
- Continued investment in the London Tideway Improvements programme to clean up the River Thames: £675m of upgrades to London's five main sewage works and the £635m Lee Tunnel, to stop sewage overflows to the River Lee, a tributary of the Thames.
- Running a six-week unbilled customer amnesty to encourage people who use water but do not receive a bill to come forward. This amnesty resulted in more than 1,300 new accounts being set up, making it fairer on paying customers.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Financial results

#### Financial Key Performance Indicators (KPIs)

Performance Measure	The Company			The regulated business		
	Year to 31 March 2011  £m	Year to 31 March 2010  £m	% Change	Year to 31 March 2011  £m	Year to 31 March 2010  £m	% Change
Turnover	<b>1,623.1</b>	1,623.8	-%	<b>1,600.0</b>	1,593.1	0.4%
Operating expenditure <sup>2</sup>	<b>629.6</b>	609.2	3.4%	<b>627.1</b>	604.8	3.7%
Operating profit <sup>3</sup>	<b>600.2</b>	671.1	10.6%	<b>598.1</b>	689.5	13.3%
Total capital expenditure (see note 9) <sup>4</sup>	<b>1,006.6</b>	754.1	33.5%	<b>1,003.0</b>	763.0	31.5%

The following commentary is in respect of the Company.

#### Turnover

Turnover remained broadly in line with prior year at £1,623.1m (2010: £1,623.8m). Whilst reflecting real increases in price ('K'), (see page 103), as agreed with Ofwat, together with increases linked to the Retail Price Index ("RPI"), turnover remained in line with last year largely as a result of lower metered consumption reflecting the Company's customers' wise use of water.

#### Operating expenditure

Whilst the Company has continued its emphasis on driving operating efficiencies and ensuring the delivery of its regulatory outputs, operating costs have increased by 3.4% to £629.6m (2010: £609.2m). This year on year increase is largely due to inflation (RPI has averaged nearly 5%) together with increased bad debt provisioning resulting from the impact of the economic downturn, higher business rates and additional costs associated with the coldest start to winter for 100 years. Despite these cost pressures the Company has still managed to deliver efficiencies to hold the year on year increase to just 3.4%.

#### Operating profit

As a result of static turnover, increased operating expenditure, as explained above, and an increase in depreciation of £49.8m (14.5%) reflecting the significant capital investment over recent years, operating profit has fallen by 10.6% to £600.2m (2010: £671.1m).

<sup>2</sup> Operating expenditure: operating costs, excluding depreciation and the Infrastructure Renewals Charge ("IRC").

<sup>3</sup> Operating profit: turnover less operating costs for the Company but including profit on sale of assets for the regulated business.

<sup>4</sup> Total capital expenditure: total expenditure on tangible fixed assets including contributions received, see note 9 to the financial statements. Regulatory capital expenditure, in addition includes maintenance non infrastructure income.



# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Capital expenditure

2011 has been a successful year for capital delivery with the Company investing over £1bn and completing all of its capital regulatory outputs within the first year of Asset Management Period 5 ("AMP5"). This is a great start to the new AMP and a solid platform to deliver the Company's required investment programme of nearly £5bn over the regulatory period.

### Treasury policy

The Company's treasury operations are managed centrally by a small specialist team, which operates with the delegated authority of, and under policies approved by, the Board of Directors. The treasury function does not act as a profit centre and does not undertake any speculative trading activity. The key objectives of the funding strategy are defined by the regulatory regime within which the Company operates and are intended to ensure that it meets all funding related requirements under the terms of its Licence. This includes maintaining cash reserves and access to undrawn committed bank facilities sufficient to fund at least 12 months net cash flow (as discussed on page 23 - Company dividend policy - extends this to a 15 month period) and to maintain an investment grade credit rating (see "Debt financing" section below) as set out in Condition F of the Licence.

A key objective of treasury policy is to ensure compliance with financial covenants, including interest cover and gearing ratios; maintain liquidity and a balanced debt maturity profile, and ensure that at least 85% of the interest cost within the Securitisation Group, (being Thames Water Utilities Holdings Limited, the Company, Thames Water Utilities Finance Limited, Thames Water Utilities Cayman Finance Holdings Limited and Thames Water Utility Cayman Finance Limited) is based on either fixed or RPI-linked interest rates.

### Financial risk management

The Company has an Executive Team ("the Executive"), which receives regular reports from all areas of the business to enable prompt identification of financial and other risks so that appropriate actions can be taken.

The operation of the Treasury function is governed by policies and procedures, which set out guidelines for the management of interest rate risk and foreign exchange risk and the use of financial instruments. Treasury policy and procedures are incorporated within the financial control procedures of the Company.

The Company's operations expose it to a variety of financial risks that include the effects of changes in debt market prices, price risk, liquidity risk, interest rate risk and exchange rate risk.

Derivative financial instruments, including cross currency swaps, interest rate swaps and forward currency contracts are employed to manage the interest rate and currency risk arising from the primary financial instruments used to finance the Company's activities. Matching of assets and liabilities in foreign currencies is also applied wherever practicable. The Company actively maintains a broad portfolio of debt, diversified by source and maturity and designed to ensure the Company has sufficient available funds for operations.

The Company is exposed to commodity price risk, especially energy price risk, as a result of its operations. The Company aims to manage its risk by fixing contract prices where possible.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Financing

The Company had committed facilities in place with a syndicate of relationship banks to the value of £1,175m; all of which were undrawn at 31 March 2011. In addition, due to pre-funding activity undertaken in the final quarter of the year, the Company had £776m of cash on short-term deposit. This cash balance together with undrawn facilities will provide the Company with the necessary liquidity to fund the operation of the business for at least the next fifteen months.

### Debt financing

Debt financing is raised by the Company or through the Company's wholly owned subsidiary; Thames Water Utilities Cayman Finance Limited. Previously, debt had been raised through Thames Water Utilities Finance Limited; another wholly owned subsidiary.

Moody's Investor Service ("Moody's") rates Class A debt as issued by Thames Water Utilities Cayman Finance Limited, A3 long term with stable outlook. Moody's also issues a Corporate Family Rating for the Securitisation Group of companies, which stands at Baa1, reflecting the ability to issue Class B debt beyond 31 March 2011. Standard and Poor's Rating Services ("Standard and Poor's") rates Class A debt as issued by Thames Water Utilities Cayman Finance Limited at A- with a stable outlook. The Standard and Poor's rating was upgraded from BBB+ to A- on 19 April 2010, reflecting an improvement in the operating performance of the Company. Accordingly, the Company maintains an investment grade issuer credit rating in accordance with the requirements of its Licence.

In July 2010, Thames Water Utilities Cayman Finance Limited issued Class B bonds on behalf of the Company. This Class B debt is rated Baa3 by Moody's and BBB by Standard and Poor's. See note 16, page 59 for details of these bonds.

### Capital structure

Key features of the Company's capital structure are as follows:-

- All debt issued by the Securitisation Group is documented pursuant to a Common Terms Agreement as part of the Whole Business Securitisation entered into in August 2007.
- Until March 2010, all debt issued by the Securitisation Group was ranked in the same class ("Class A"). The ratio of Class A net debt to Regulated Capital Value ("RCV") within the Securitisation Group is limited to 75 %.
- Since 1 April 2010, the Company and the Securitisation Group has the option to issue Subordinated Debt ("Class B"). At the same time, there is an increase in the combined Class A and Class B (together "Senior") net Debt/RCV ratio to a maximum of 85 %.
- Each Obligor (the companies within the Securitisation Group) had entered into the Security Trust and Inter-creditor Deed ("STID") with the Security Trustee pursuant to which Thames Water Utilities Holdings Limited guarantees the obligations of each other Obligor under the finance documents and the Company and its wholly owned subsidiaries guarantee the obligations of each other under the finance documents, in each case to the Security Trustee.
- Following an event of default, the documents provide for an automatic 18 month standstill of the claims of the creditors that have entered into the STID.

### Covenant compliance

Under the terms of its finance documents, the Company is required to comply with various covenants such as interest cover and net debt to RCV. These covenants are measured and submitted to the Security Trustee semi-annually and involve both actual data and forecasts. The two main ratios are discussed further below:

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Covenant compliance (continued)

**Adjusted Interest cover ratio (trigger: 1.3x)<sup>5</sup>:** For the year to 31 March 2011 the ratio was 2.1x (2010: 2.1x). There has been no movement in the year.

**Senior Debt/RCV ratio (trigger: 85%)<sup>6</sup>:** At 31 March 2011 the ratio was 77.4% (2010: 68.3%). The movement in the ratio is due to two new class B bond issuances of £550m and £300m during the year.

There are other variations on these ratios on class A and Senior Debt, which the Company is also required to calculate to show compliance with its covenants. The Company is compliant with these ratios as at 31 March 2011.

### Key performance measures

The table below shows the Company's performance against its key performance measures, which with two exceptions all measures were achieved.

Key performance measures		Target	2011 Actual	Target achieved
<b>Customer Services levels</b>				
Inadequate pressure (DG2)	Properties	34	14	✓
Interruptions to supply (DG3)	Points	0.35	0.58	✗
Billing queries (DG6)	%	99.9	99.9	✓
Complaint handling (DG7)	%	99.6	99.6	✓
Meter reading (DG8)	%	99.7	99.7	✓
Abandoned rate (DG9)	%	7.5	5.1	✓
<b>Security of Supply</b>				
Security of supply score	Annual average	100	100	✓
Security of supply score	Critical period	99	100	✓
Leakage	Mld	674	665	✓
<b>Pollution incidents</b>				
Serious or significant pollution incidents	Number	0	10	✗
<b>Quality</b>				
Water quality mean zonal compliance	% (2010 calendar)	99.97	99.97	✓
Sewage works compliance	% (All measures)	100	100	✓
<b>Serviceability</b>				
Water non-infrastructure (process)		Stable	Stable	✓
Water infrastructure (network)		Stable	Stable	✓
Wastewater non-infrastructure (process)		Stable	Stable	✓
Wastewater infrastructure (network)		Stable	Stable	✓

<sup>5</sup> A trigger event would lead to lock up which would mean nil distributions outside of the Securitisation Group until resolved to the Security Trustee's satisfaction. Adjusted Interest Cover Ratio is calculated as operating cashflow adjusted for expenditure on depreciation and infrastructure renewals divided by interest paid.

<sup>6</sup> A trigger event would lead to lock up which would mean nil distributions outside of the Securitisation Group until resolved to the Security Trustee's satisfaction.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Key performance measures - highlights

Below is a summary of some of the key changes in the business that the Company has used to drive its improvement against targets.

#### Water Service and Environmental Performance

- Between 2005 and 2011, the Company has reduced leakage by 27% by replacing old Victorian pipes mainly under London. Despite the coldest start to a winter for 100 years the Company has now met Ofwat's annual leakage target for the last five years. This improved performance follows the acquisition of the Company by a consortium of investors led by the Macquarie European Infrastructure Funds in 2006.
- This year the Company's mains replacement programme moved out of London for the first time, with projects starting in Slough and Reading. This work continues to contribute to the overall range of measures and initiatives in keeping leakage under control.
- The Company's drinking water quality performance remains high at 99.97% compliance. Whilst the Company aims to achieve 100% compliance, many of the failures recorded at customers' taps are caused by the condition or maintenance of customers' pipework and fittings. To that extent, 100% compliance is not within the control of the Company. However, management continues to strive to achieve this aim and the Company is one of the best performing companies in the industry.
- The Company always encourages people to use water wisely – something which resulted in a daily saving of 5Mld last year (two Olympic-size swimming pools a day), surpassing Ofwat's 4Mld target.

#### Sewerage Service and Environmental Performance

- During this year, the number of homes at the highest risk of internal sewer flooding due to lack of sewer capacity has reduced to 1,526 (2010: 1,604). The Company's ambition is to eliminate this service failure.
- Every year the Company clears approximately 55,000 blockages in sewers at a cost of around £12m, three quarters of these are caused by 'sewer abuse' which is when anything other than human waste or toilet paper goes down into the drains.
- The Company achieved 100% compliance with the Environment Agency's standards on treated effluent across all of the 349 treatment works.
- Sludge is a by-product of the sewage treatment process. The majority of this has been recycled and used on agricultural land as fertiliser.
- The Company has maintained its 100% compliance with statutory requirements for dealing with sludge and was able to meet the new tougher quality requirements in the voluntary code of practice known as the 'Safe Sludge Matrix'.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Key performance measures – highlights (continued)

#### Security of Supply

- The Company has delivered 100% Security of Supply to all its customers.

#### Customer Service

- Digital communications are now at the forefront of modern business and the Company is very proud to have been the only UK water company named in the 'Social Brands 100' report.
- The Company's new customer centre at Kemble Court in Reading was opened in May 2010 and has already led to improvements in the way the Company plans and coordinates its work and responds to customer queries.
- The Company has also made it easier for customers to speak directly to an agent and has introduced an additional feature to enable customers to find out about anything affecting water supply on the same phone line. As a result of these changes, there has been a marked reduction in the number of calls that have been abandoned this year.
- This year the Company staged its biggest-ever public consultation on the proposed Thames Tunnel, receiving some 3,000 individual responses. The next phase of the public consultation is due to start in September 2011 before the Company submits a final planning application for the scheme in 2012.

#### Incidence Rate – accidents per 1,000 employees

Management continue to focus on health and safety, with a number of initiatives launched in the year. The headlines for 2011 show a significant improvement in the Company's processes and compliance capability:

- The number of reportable accidents fell to an Accident Incident Rate ("AIR") of 0.39, injuries per 1,000 employees, (2010: 0.50) across the business, a 22% improvement.
- The Company introduced a new Health and Safety Management System with over 400 managers now trained in risk assessment and managing health and safety. The Company aims to have all people managers trained by mid year.
- An AMP5 contractors' conference was held during the year with a presentation of the Excellence in Health and Safety Awards, recognising improvement, achievement and excellence.
- The Company introduced flu vaccinations, which have been taken up by over 300 staff at a number of locations.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Principal risks and uncertainties

#### Risk overview

The Company's Risk Management process is integrated within the business, and is designed both to identify emerging risks and to minimise the adverse impact of emerging and existing risks. Each business area is responsible for managing its risks, and maintains a risk register, which is reviewed regularly. Significant risks are escalated and reviewed by the Executive.

The Company is exposed to a number of potential risks and uncertainties that could have a material impact on its long-term performance. These include:

- **Delivery of Thames Tunnel** – As an innovative solution to the challenge of reducing sewage discharges into the Thames, the design and construction of the Thames Tunnel presents a number of major technical and logistical challenges. These include the need to identify and secure a number of construction sites in central London, to obtain the planning consents needed from London boroughs and to manage the inevitable disruption. As well as the many stakeholder issues, a key challenge is to finance the project, which has a different scale and risk profile to other Company activities. A number of possible funding and delivery models are being considered between the Company, Ofwat and the Department for Environment, Food and Rural Affairs ("Defra"), including delivery by a specialist project company appointed under the Flood and Water Management Act 2010.
- **PR14 determination** – All UK water and sewerage companies must justify the operating costs and capital investment needed to deliver service to customers in the five-year period from April 2015. Failure to demonstrate the Company's case to Ofwat's satisfaction may mean that it is unable to invest in asset improvements that the Company believes will benefit its customers in the long term.
- **Failure to meet regulatory targets** – The Company is required to meet targets set by Ofwat, the Environment Agency, the Drinking Water Inspectorate and other regulators. In order to achieve this, the Company must continue to deliver cost and efficiency savings in line with a challenging FD, while maintaining and improving operational performance. Performance against these is the subject of frequent management review.
- **Managing increased competition in the water industry** – A White Paper is expected in December 2011, leading to legislation from 2012 setting out a framework for competition beyond 2015. Separate proposals are potentially anticipated for upstream (wholesale) and downstream (retail) competition. Competition will impact the structure and financing arrangements of water companies, and may lead to significant implementation costs.
- **Transfer of private drains and sewers** – The Government has committed to transferring responsibility for operation, maintenance and replacement of private sewers and pumping stations to water and sewerage companies, with effect from 1 October 2011. Limited information is available on these assets, and companies will have to provide an acceptable level of customer service and obtain retrospective funding through Ofwat for the costs incurred in the current regulatory period.
- **Employee pension scheme funding** – The Company operates two defined benefit pension schemes. Whilst the Company has reduced its future exposure by closing the final salary schemes to new entrants, and moving a number of senior employees onto a defined contribution scheme, the Company remains liable for the historic rights earned by past and present employees. There is a risk that further falls in asset values will increase the deficit further and require further employer contributions to safeguard members' benefits.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Principal risks and uncertainties (continued)

- **Failure to maintain adequate funding arrangements** – As at 31 March 2011, the Company has adequate cash at bank and short term deposits of £776m (2010: £579m) and undrawn committed bank facilities of £1,175m (2010: £1,105m) in place to provide liquidity as required. The Company will need to renew £425m of 364 day committed facilities by July 2011. The Company has been extremely successful in raising new debt financing in difficult market conditions, with circa £1.8bn raised in the financial year to 31 March 2011. However, due to continuing uncertainties in credit markets, there is a risk that the cost of raising new debt and refinancing bank facilities will put pressure on key financial covenants (as defined by the Company's capital structure). Whilst RPI at March 2011 is at a recent high, the impact of a falling RPI rate on the RCV could create further pressure on financial covenant headroom, specifically the ratio of net debt to RCV.
- **Future changes in laws or regulations** – The Company is not funded by Ofwat for changes in obligations that would affect the whole economy. Consequently the Company may, for example, have to meet the obligations resulting from changes in environmental legislation without recourse to Ofwat. However, changes that are specific to, or are more material for, the water industry may be funded by Ofwat as a relevant change of circumstance.
- **Failure of a major asset** – A failure at one of the Company's major assets could significantly impact the safety of its workforce and the public, as well as interrupting supply to customers and breaching environmental and regulatory targets. The impact would be both financial and reputational, and as a result the Company has a specific process to manage the identified risks.
- **The effects of climate change and long-term changes in weather patterns** – As the Company continues to supply an increasing population, the effects of climate change could adversely affect its ability to maintain its Security of Supply Index (SoSI) requirements. Consequently, in addition to substantially enhanced demand management measures, the Company is currently making provision for new sources of potable water, greater network integrity and, together with other water companies and regulators, is actively contributing to work to identify the wider water resources needs across the South East of England.
- **Shortage of skilled labour** – The shortage of available skilled labour in London and the South East creates an environment in which the Company must compete with other organisations for staff with the necessary skills, particularly engineering, in order to deliver the capital programme agreed in the FD and additional major planned projects. Failure to deliver agreed targets may result in fines, intervention by Ofwat and less favourable future periodic determinations.
- **Impact of low inflation or deflation** – In return for their capital investment in assets, regulated water companies earn a return on their RCV, which is adjusted by the RPI. In times of low inflation or deflation, the return on this investment will decrease relative to the cost of funding, reducing cash flow and shareholder value.
- **Customer experience measures** – The measure for customer performance is evolving from quantitative to qualitative criteria. All water companies will need to adapt processes in order to optimise performance against these new criteria to be measured against Ofwat's Service Incentive Mechanism ("SIM").

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Transforming Thames – Making Tomorrow Better

The Transforming Thames project has continued to progress under the banner of 'Making Tomorrow Better'. The transition to the asset management based Thames Operating Model ("TOM") was completed in December 2010, which enabled the new organisational structures to come into full operation from 4 January 2011. This places the Company in a good position to fulfil the significant challenges presented in Ofwat's FD and to deliver efficiently the circa £5bn capital programme agreed with Ofwat for the AMP ending 31 March 2015.

An Integrated Delivery Plan has been compiled to ensure that all the key change initiatives being undertaken across the business, such as the Delivering Performance Excellence ("DPE"), Work Asset Management and Information ("WAMI"), Supervisory Control And Data Acquisition ("SCADA"), Customer Service Transformation and IS strategy programmes, are aligned to strategy and that interdependencies are identified, recognised and managed across all functions. In addition, future impacts of regulatory change, such as the potential private sewers programme are anticipated through this mechanism, to ensure that the Company delivers the requirements of AMP5 whilst considering its longer term strategic business plan.

To support the implementation of change across the business a Thames Way Change Methodology has been developed to provide a framework and an accompanying toolkit including tips, techniques and templates for use by managers across the business. A core team of Change Managers has been trained in its use and will be introducing the methodology and providing support and advice to managers throughout the period of transformation, including the roll-out of WAMI.

The WAMI programme has continued at a pace and remains on schedule to transform the asset management and operational planning process of the Company. The WAMI solution has been developed and signed off, and work is now in progress to ready and support the business in a phased 'Go Live' from quarter four of 2011. It will have an impact throughout the business, introducing new systems and tools so that the Company's operational teams can complete work more efficiently as well as enabling it to give customers a better service. Operating in a regulatory environment, the Company seeks to provide the best, most cost effective value-for-money service to its customers.; delivering top quality tap water to customers as required by the Drinking Water Inspectorate; treating wastewater to improve the Company's performance, as measured by SIM, and to help the Company to reduce its costs by over £100m by 2015.

The Company has demonstrated continuing improvement, whilst implementing the transformation programme, in both operational and financial performance, thus providing a strong platform for the future.



# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Looking further ahead

It is over 20 years since the water industry was privatised. Since then much has changed - costs of service are lower, performance is better and the industry has delivered significant quality improvements. However, there is still lots to do, with new challenges ahead from climate change, population growth and new quality improvements, to name a few. The industry and the Company must ensure they can meet the challenges they face.

A key to this is how the sector is regulated going forward to ensure it is fit for purpose to meet these challenges.

There is considerable work underway in this area. Ofwat is reviewing what and how it regulates; the Government is expected to publish a Water White Paper on the long term direction for the sector and the economic regulatory arrangement themselves are being reviewed by David Gray (former Managing Director of Networks at Ofgem).

Looking ahead, the Company will need to be flexible and ready for any change to the regulatory environment which occurs.

However, through this period of change there are some constants. The Company will need to ensure that:

- High performance is maintained and capitalise on opportunities for further improvements to performance.
- It delivers what customers want at the right price, in the right place and at the right time.
- It offers value for money at an affordable price.

As highlighted on page 12, a key challenge in this process will be the delivery of the proposed Thames Tunnel. Thames Water is working closely with all stakeholders to ensure this is delivered by the most appropriate means possible.

The Company is looking ahead to understand the future environment and ensuring that it takes the right actions today to protect the future.

### Strategic Direction Statement

In 2007 the Company published its Strategic Direction Statement, setting out plans for the next 25 years. As part of its Business Planning, the Company has begun the process of reviewing and updating its long term plans, building on the wants and needs of customers and challenges as diverse as future population growth and climate change.

### Water resources

In August 2009, Defra called for a public inquiry into the Company's draft Water Resources Management Plan. The Inquiry completed in August 2010 and the Inspector's report recommended additional work in a number of areas including the assessment of long-term solutions for supply security.

Defra issued instructions to Thames Water to complete the plan in line with the Inspector's report and advice from the Environment Agency.

The programme of work is expected to be completed by the end of 2011, with approval of the Final Plan by Defra in 2012.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Relationships and resources

#### Employees

This financial year has been challenging, with the largest ever five year capital investment programme commencing, continued change and transformation of the Company's business processes and the challenge of severe winter weather events. The Company's employees have continued to demonstrate high commitment and increased engagement levels throughout the year, supported by the its 'Passionate About People' strategy.

The strategy was refreshed under the Company's new HR Director and an increased focus on supporting the organisational change and transformation across the Company, alongside getting the best out of its people by giving them the right support and development. Implementation continues to engender a positive working environment, which focuses on performance, contribution and values diversity and inclusion.

Overall staff turnover in 2011 has been at a similar level to 2010.

The Company's sickness rate during the year was 2.75% (2010: 3.20%). The Company has an attendance management policy in place with the overall aim of reducing and managing sickness absence. In addition, there has been a focus on attendance management this year.

The Company is committed to effective talent management and runs regular Talking Talent reviews to assess performance and potential across the Company. These reviews support effective learning and development interventions and focus on ensuring the Company has the future talent to deliver its business strategy. This year, the Company has continued to invest in its core leadership development programmes, future talent pipeline programmes and to develop the technical and business skills of its employees.

During this year, the following key people initiatives have been delivered to support the business strategy:

- Continuous improvement of resourcing activities to enhance the quality of new employees hired, delivery of volume recruitment and enhanced offer and security vetting processes.
- Executive reward review and implementation of pensions strategy, including launch of the new Defined Contribution pension plan for new joiners.
- Review of key people policies and a major programme to review the Company's working patterns and terms and conditions for frontline operational employees.
- Implementation of enhancements to the HR system to build on the previous year's successful implementation.
- The continued focus on employee engagement across the Company resulting in a year on year increase in employee engagement, as measured through its annual employee survey.
- New intakes to the Company's Graduate, Apprentice and Bursary future talent pipeline programmes.
- Continued roll out of the Company's core 'Foundation and Advanced Leadership Development' programmes and the launch of its 'Strategic Leadership Development' programme'.
- Continued performance and development reviews for all employees linked to the annual pay review.
- Effective management of significant organisational change across the Company, including implementation of the TOM and local re-organisations.

The Company is committed to the training and development of all of its employees who undertook 12,355 (2010: 4,387) formal training days in 2011. Over 7,000 days were spent on health and safety and contractor maintenance, nearly 2,000 on leadership training with a further 2,200 days with the Company's customer services and customer management teams.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Stakeholders

Much of the Company's work with stakeholders centred on the Thames Tunnel project, following the launch in September of the first round of public consultation on the need for the project, its route and construction sites. In addition to 49 days of public exhibitions at 25 venues, the Company held briefings with Members of Parliament and local authorities, and attended community and residents' groups and public meetings.

The general election in May saw new MPs in several constituencies in the Company's region, and individual briefings and group meetings have been held with many of them, particularly where the Company's activities have a significant impact on their constituencies.

During the year the Company held events with its stakeholders to mark milestones including the opening in June of the Company's Thames Gateway Water Treatment Works in Newham, East London, and the groundbreaking ceremony in November for the Lee Tunnel.

The Company met with and attended workshops held by civil servants responsible for developing Government policy in areas including market reform, funding for large infrastructure projects, the transfer of private sewers and social tariffs. These were in addition to several discussions with civil servants on the Water White Paper.

The Company played an active role in inquiries by the Environment, Food and Rural Affairs Select Committee, submitting written evidence as part of its examination of future water legislation, and giving oral evidence as part of its scrutiny of the draft waste water National Policy Statement ("NPS"). The NPS sets out guidance for planning decisions on projects deemed of National Significance, including the construction of the Thames Tunnel, and potential upgrade and relocation of the sewage treatment works ("STW") at Deephams.

The Company met with the 'Blueprint for Water' coalition of environmental Non-Governmental Organisations to discuss their ten-point plan for the water industry, and explored opportunities for closer collaborative working. This has prompted further work on areas including metering and water efficiency, as well as water-friendly farming practices.

At a regional and local Government level, the Company continued to strengthen ties with the authorities it serves. This included giving evidence to the London Assembly Environment Committee's inquiry into flooding, and working with local authorities – both individually and through the Drain London Forum in the capital – to help them develop the Surface Water Management Plans required by the Flood and Water Management Act 2010.

The Company welcomes the introduction within the Floods and Water Management Act 2010 of a social tariff for the water industry, which the Company has strongly advocated for the last three years. This will form an essential part of the package of affordability measures the Company plans to introduce to help customers least able to pay for their bills, particularly as a result of a move to increased metering.

The Company embraced a culture of open and transparent dialogue in the public realm, and throughout the year attended several formal Scrutiny and Public Meetings with Local Authorities, giving evidence at meetings and responding to questions and feedback from councillors, officers and the public.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Public consultations and research

The focus on public consultations work has again increased this year. The Company has a number of major projects underway, which has led to its highest level of consultation activity to date. The Company recognises that these major projects have an impact on a large number of its stakeholders and customers and endeavours to make its plans reflect their views.

The Company's approach to consultation includes independently facilitated stakeholder workshops, individual discussions with MPs and other stakeholders; surveys and independently hosted online consultations.

The most significant piece of public consultation work the Company carried out during the year was on the Thames Tunnel. During Phase 1, between September 2010 and January 2011, the Company asked the public for views on its tunnel route and construction sites. The Company received over 3,000 individual responses to this initial phase of consultation. During Phase 2, which is planned to start in September 2011, the Company will consult on the final proposed route and construction sites, prior to submitting its planning application in 2012. The Company's first phase of public consultation was commended by a number of key stakeholders as being a good example of best practice.

The Company has also held deliberative workshops and focus groups with customers, at which it has provided them with background information on its work, in order to deepen their understanding of its business and help them to give more informed views. The topics covered this year have included the Company's approach to metering, the planned transfer to water companies of private sewers, research with commercial customers and customer strategy and brand reputation research. The Company also undertook reputation research with a number of its other key stakeholders.

The Company's continuing commitment to consultation and research plans will help it to understand its customers better than other water and sewage companies and ensure it has (as far as possible) developed its plans in accordance with their wishes. However, the Company's need to understand, and test, customer views is growing all the time and the Company will involve customers more in taking some of the more strategic decisions it faces and not simply seek their views on elements of its investment programme. With this in mind, the Company is setting up a panel of 2,000 customers to help it to better understand its customers' needs and preferences.

The Company is a corporate member of the Consultation Institute and follows Cabinet Office best practice guidelines for consultation, aiming to make the process as open and transparent as possible.

### Key suppliers and contractors

In 2011, the Company spent in excess of £1.4bn on construction, goods and services with a range of suppliers and contractors (2010: in excess of £1.1bn). Approximately 31 key suppliers (2010: 23) were engaged with a spend greater than £10m each. The Company's policy is to establish trading arrangements, which are made following an open non-discriminatory, competitive bidding process. Procurement processes reflect the Company's corporate responsibility commitments and, where applicable, comply with the requirements of the Utilities Contracts Regulations 2006 (as amended).

### Research and development

The Company's research and development programme consists of a portfolio of projects designed to address technical needs across the range of water cycle activities. Research and development deliver innovative technical solutions through a research programme aligned with business needs to address challenges for AMP5 and also provide specialist technical support to the business. Expenditure on research and development totalled £3.4m for the year (2010: £3.5m).

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Intellectual property

The Company protects intellectual property of material concern to the business as appropriate, including the filing of patents where necessary.

### Energy efficiency and renewable energy

The Company is committed to reducing its contribution to the causes of climate change and its voluntary target is to achieve by 2015 a challenging 20% reduction in greenhouse gas ("GHG") emissions (compared to 1990 levels)<sup>7</sup> for scope 1 and scope 2 emissions<sup>8</sup>.

The Company's total GHG emissions (Scope 1, 2 and 3) reported for 2011 were 780,436 tonnes (2010: 757,218 tonnes) of carbon emissions ("CO<sub>2</sub>e"). The Company's approach to reporting GHG emissions is consistent with both the Department of Energy and Climate Change ("Decc") and Defra guidance and Ofwat reporting requirements. During the year, the Company's reported emissions increased due to the impact of the severe cold weather during the winter and demand from new assets, although emissions were reduced by the Company's energy efficiency and renewable energy programmes. In addition, an increase in the carbon intensity of grid electricity, rather than the expected reduction, also contributed to higher reported emissions. Despite these setbacks, the Company remains determined to meet its targets by 2015.

Last year the Company consumed 1,179 Gigawatt hours ("GWh") of electricity, of which 183GWh was renewable electricity generated at the Company's operational sites - around 16% of the Company's total electricity use. The Company produced 96GWh of heat energy which displaced the need to consume natural gas. This generation of renewable electricity and heat helped reduce the Company's overall GHG emissions.

The Company continues to work hard to understand and reduce its carbon footprint. During 2011 it has:

- Completed, and had independently reviewed, an assessment of its progress against its 1990 emissions baseline. The review highlighted the fact that, despite serving over 3m more customers, the Company's GHG emissions for 2011 were around 11.4% below 1990 levels.
- Completed two years early, the innovative biogas injection scheme at Didcot cleans up and injects biogas (produced as a by-product of sewage treatment) into the gas grid to allow it to be used beneficially by gas customers. The scheme will produce enough biogas to supply 200 houses locally helping to reduce the UK's GHG emissions.
- Increased its renewable energy generation capacity by 4 megawatts ("MW"), including 1.3 MW at Chertsey STW. These assets will help to reduce the Company's GHG emissions and energy costs going forward.
- Increased its remote metering scheme that it now covers 100% of gas and more than 95% of its electricity use. This is enabling the Company to better understand its energy consumption and to identify and target opportunities for cost effective energy efficiencies.
- Installed process sub-metering on three major operational sites to provide both local, and management level monitoring and targeting of specific energy efficiency opportunities. On average, this has yielded a 6% reduction in electricity consumption at these sites. Building on this successful pilot programme, the Company will begin rolling out process sub-metering to a further 22 sites during 2012, which will give 65% coverage of its electricity consumption.

### Energy efficiency and renewable energy (continued)

<sup>7</sup> The Company has assumed for planning purposes that grid electricity intensity will decrease in line with the projections in the Government's Low Carbon Transition Plan in order to achieve this goal.

<sup>8</sup> Scope 1 emissions are those direct emissions associated with the operation of the business. Scope 2 emissions are the indirect emissions associated with the consumption of grid electricity. However, this is reliant on the Government redefining grid emissions.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

- Optimised pumping at many points on the Company's water network, to reduce leakage and energy consumption, resulting in a cut of 5.4 GWh of energy use.
- Completed surveys on 45 water pumping systems and on average have identified an average 10% energy efficiency potential on 25 of these systems, for delivery in 2011/12.
- Become the first utility to achieve re-accreditation to the Carbon Trust Standard, which recognises "real and sustained emissions reductions" over a three year period.

Looking to the future, there are a number of significant challenges facing the business in terms of reducing the Company's GHG emissions. The Company's activities are very closely linked to the weather and, as seen this winter with the extremely cold weather, the Company needed to pump more water and so use more electricity - consequently emitting more GHG. Some of the upward pressures on the Company's energy consumption and GHG emissions are beyond its control such as the weather, new obligations (including the adoption of private sewers and the construction of the Tideway Tunnels) and population growth. .

However, there are responses that the Company can influence; including energy efficiency, effective energy procurement and the generation of renewable energy. The Company therefore needs constantly to innovate in the management of its energy consumption and GHG emission to ensure they are kept as low as possible. However, changes in Government policy such as the Carbon Reduction Commitment becoming a tax rather than an incentivised cap and trade scheme, and proposed changes to the Feed-in Tariff Scheme have made effective planning and delivery much more difficult.

### Social and community

#### Corporate responsibility

The Company continues to be committed to operating in a socially responsible way and to engaging with stakeholders and communities.

The Company is pleased to report that it has retained 'Platinum' ranking in the Business in the Community Corporate Responsibility Index, having achieved this ranking for the first time in 2010.

#### Community investment

The Company's community investment programme consists of activities designed to support the social, economic and environmental aspects of the communities in which it operates. These include the Ten for Ten programme (see below), employee volunteering projects to improve community spaces, education programmes to enhance the teaching and learning about the water industry, and a charitable giving scheme.

#### Ten for Ten

The Company has continued with its £10m *Ten for Ten* programme to benefit customers and communities across the service area. In total, the Company contributed £2.5m during the year, split into two key areas.

##### 1) Thames Water Trust Fund

This year the Company donated £1.9m to the Thames Water Trust Fund, which over the year helped 3,631 disadvantaged customers to pay their water bills.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Ten for Ten (continued)

#### 2) Community projects

The key projects supported during the year are outlined below.

Education related projects have been successful over the year. An additional five students from the University of East London were awarded engineering bursaries. In addition, the first two students from the University had successful summer work placements at Beckton and in field operations and are now in the second year of their degree, supported once again by the Company.

The Company also funded the Creekside Education Centre at Deptford with £30,000 to assist with staffing ready for launch in May 2011. The Thames Water branded centre will educate around 3,000 schoolchildren a year and allow them to go wading in the Thames at Deptford Creek and learn about tidal ecology, the River Thames and the Company.

The Company is committed to improving key water related visitor attractions. Kew Bridge Steam Museum undertook a consultation with its visitors to understand how to make best use of the museum. From this research, and together with the Company's financial commitment, Kew Bridge Steam Museum is preparing a Heritage Lottery Fund bid, to transform itself into London's 'Museum of Water'

The improvements at the London Wetland Centre continued. In July 2010, an interactive pond exhibition was opened and in October 2010, the Thames Water Pond Zone and Down the Plug Hole exhibits were opened. Contributions to these projects totalled £300,000.

The Company has been working with various partners to improve key wildlife and recreation sites. £175,000 was provided to improve The Greenway, to enhance it for the Queens Golden Jubilee and Olympics in 2012. The Company confirmed support to the Fobney Island project in Reading, whereby the wetland will be enhanced and a meander added to the River Kennet to provide good angling and bird watching facilities. The National Trust woodland at The Chase, Newbury, is being transformed. The Company's donation has provided new footpaths, ponds, fencing and in the summer 2011 wild-roaming cattle and pigs will be introduced into the woodland.

#### Further community investment

The Company has sponsored a number of community events in partnership with key stakeholders including the Thames Festival and the London Youth Games. The Company also supports community organisations in projects which fit its Community Investment criteria including wildlife and environmental improvements. The Company's contribution in this area totaled some £270,000 in 2011.

#### Employee engagement

More than 300 employees took part in a number of volunteering events, working with community partners in London and the Thames Valley. The Company supports its employees' participation in community, education and fundraising events through the Time To Give volunteering scheme, an entitlement of two days volunteering leave in addition to annual leave.

The Company's volunteers participated in a range of events over the year from environmental clean ups to supporting education activity days in schools. The Company was pleased to continue to work with key partners including Thames 21, a charity focusing on cleaning up the River Thames in London Boroughs and local Education Business Partnerships which deliver skills-based activities in schools. Over 60 volunteers took part in the Thames Water-sponsored Reading RESCUE clean-up event, in partnership with Reading Borough Council, clearing rubbish from seven green spaces in and around Reading.

# Thames Water Utilities Limited

## Chief Executive Officer's Business review (continued)

### Charitable donations

The Company and its employees also took part in a variety of charity and fundraising events such as the Macmillan 'World's Biggest Coffee Morning' and numerous fun runs and cycle rides. More than 1,250 employees were involved over the year, raising over £170,000 for local and national charities, charitable good causes and community organisations.

The Company donated around £230,000 through its Charities Committee and direct donations to good causes, including the Company's principal charity, WaterAid.

A highlight in the charity calendar was Comic Relief night, which saw around 150 employees give up an evening to man phone lines and take donations from the public.

The Company's Charity Committee considered a number of requests directly from charities and charitable organisations. Following the Charity Committee's review it made donations to beneficiaries including disadvantaged people in London through the London Evening Standard's Dispossessed of London campaign and The Ahoy Centre, a sailing charity working with disadvantaged youth and people with disabilities.



**Martin Baggs**  
**Chief Executive Officer**  
**9 June 2011**



# Thames Water Utilities Limited

## Directors' report

The directors present their report and the audited financial statements for the year ended 31 March 2011. These are the Company's statutory accounts as required to be delivered to the Registrar of Companies.

### Principal activities and likely future developments

The principal activities of the Company (Registered number: 02366661) are the supply of water and the collection and treatment of sewage, serving approximately 14m customers in London and the Thames Valley.

### Business review

The information, which complies with the Operating and Financial Review ("OFR") requirements of the Companies Act 2006, can be found within the Chief Executive Officer's Business review on pages 4 to 22. The Company chose not to produce a voluntary OFR as these requirements are satisfied by the Chief Executive Officer's Business review. The Chief Executive Officer's Business review (which forms part of the Directors' report) comprises an analysis of the development and performance of the business and includes an assessment of future prospects, information about research and development activities, details of important events that have occurred since 31 March 2011 and Key Performance Indicators ("KPIs").

Details of parent and subsidiary undertakings are given in notes 10 and 28 to the Financial statements, on page 52 and 68 respectively, and the Company has no branches outside the United Kingdom.

### Results and dividends

The profit and loss account on page 33 gives the Company's financial results for the year.

The Company paid interim dividends totalling £271.4m during the year (2010: £307.9m).

The Company's dividend policy is:

- To pay a progressive dividend commensurate with the long-term returns and business performance, after considering the business' current and expected regulatory and financial performance, regulatory restrictions, management of economic risks and debt covenants.

Directors, in assessing the dividend to be paid (to a maximum of statutory distributable reserves), are required to ensure that:

- Sufficient liquidity is maintained to enable the business to meet its financial obligations for 15 months.
- Post-dividend financial ratios remain within their agreed limits at both the balance sheet date and on a forward-looking basis.

The Board does not recommend a final dividend (2010: £nil), however, the Board has proposed a further interim dividend, see note 27, page 67.

# Thames Water Utilities Limited

## Directors' report (continued)

### Directors

Details of the directors who served from 1 April 2010 to the date of this report are shown below. The constitution of the Board is covered in more detail in the Company's Corporate governance report, which can be found on pages 28 to 30.

All Board members from 1 April 2010 to 31 March 2011 inclusive were non-executive directors ("NEDs") throughout the period, with the exception of Martin Baggs (Chief Executive Officer), Stephen Shine OBE (Chief Operating Officer), and Mark Braithwaite (Chief Financial Officer).

Directors serving from 1 April 2010 to the date of this report are as follows:

Director	Appointment	Resignation
Sir Peter Mason KBE – Chairman		
L F Abaira		1 January 2011
M W Baggs		
E Beckley		
R Blomfield-Smith		
M W Braithwaite		
C R Deacon		
Dame D M Hutton CBE	22 July 2010	
G I W Parsons	10 June 2010	
M J Pavia		
E C Richards	22 July 2010	
K Roseke		1 January 2011
A F C DeP Santos	1 January 2011	
D J Shah OBE		
S F Shine OBE		
W Smit		1 September 2010
M S W Stanley		
R Verrion	1 January 2011	

The following directors have formally appointed alternate directors to represent them when they are unavailable:

director			alternate director		
Name	Appointment	Resignation	Name	Appointment	Resignation
L F Abaira		1 January 2011	D Mora		1 January 2011
E Beckley			G I W Parsons	7 June 2010	4 August 2010
			S M L Leong	4 August 2010	11 February 2011
			G I W Parsons	22 March 2011	
R Blomfield-Smith			K Boesenberg		
C R Deacon			R D Israel		
G I W Parsons	10 June 2010		S M L Leong	22 July 2010	11 February 2011
K Roseke		1 January 2011	S Kolenc		1 January 2011
A F C DeP Santos	1 January 2011		M C Guerreiro	1 January 2011	
D J Shah OBE			R Verrion		1 January 2011
			L Webb	1 January 2011	
R Verrion	1 January 2011		S Kolenc	1 January 2011	

### Material financial instruments

Financial risk management is covered on page 7 of the Chief Executive Officer's Business review.

# **Thames Water Utilities Limited**

## **Directors' report (continued)**

### **Research and development activities**

This has been covered in the Chief Executive Officer's Business review on page 18.

### **Employee involvement**

The Chief Executive Officer ("CEO") and the Executive continue to hold quarterly management briefings with managers to provide the opportunity to discuss performance and how the Company can continue to move forward. This year the Company has also introduced a 'Changing Times' publication to support the changes and transformation happening across the Company. This is in addition to the continued improvement of the Company's corporate and local communication channels that provide regular communication, information and updates to employees. Corporate channels include Company-wide Team Talk briefings, a weekly e-brief containing a message from the CEO, 'The Source' magazine, the Company's internal portal web pages and specific priority news updates and managers key information.

Consultation with other employees is undertaken in partnership with the recognised Trade Unions. Consultation with management level employees typically takes place on an individual basis, except in the case of changes that affect whole areas of the business. In these circumstances, consultation takes place on a Company-wide basis with employee representatives being elected for the relevant area.

All employees are involved in both the Company's employee engagement programme and annual Performance and Development Review ("PDR") process. Each year the Company encourages all employees to participate in its annual employee engagement survey. In July 2010, the date of the last survey, over 70% of the Company's employees participated and employee engagement improved year on year. This programme also involves circa 100 volunteer employee engagement champions from around the Company who support making the Company a great place to work. It allows all employees to give their opinion and enables managers and teams to take action on key issues identified. Corporate and Business Unit objectives are agreed by the Executive Team, communicated and cascaded through the Company and included in the annual PDR for all employees. In addition, relevant department and team objectives are cascaded and inform employees' personal objectives which in turn are agreed with each employee's manager and reviewed regularly. This process is intended to ensure that all employees are aligned to Company objectives.

### **Employment of disabled persons**

The Company is committed to fulfilling its obligations in accordance with the Disability Discrimination Act 1995. The Company has policies and procedures in place that aim to ensure that both job applicants and employees with disabilities have equality of opportunity, are treated fairly and have a safe and practical workplace, free from discrimination, bullying, harassment or victimisation.

Through disability and attendance management policies, support and training is provided for employees who become disabled during the course of their employment so that they continue to work in a position appropriate to their experience and abilities.

### **Policy and practice on payment of creditors**

The Company's policy is to pay all suppliers, contractors and service providers according to pre-agreed terms. During the year under review, the average amount due to trade creditors represented 63 days (2010: 67 days) purchases received from these creditors.

### **Market value of land and buildings**

In the opinion of the directors, the market value of the land and buildings of the Company does not in aggregate exceed the net book value at 31 March 2011.

# Thames Water Utilities Limited

## Directors' report (continued)

### Political and charitable donations and expenditure

No political donations were made by the Company (2010: £nil). The Company made charitable donations totalling £723,576 (2010: £471,500). Details of these charitable donations are:

- £106,000 (2010: £154,054) to the Charities Aid Foundation.
- £58,021 (2010: £nil) to WaterAid.
- £60,000 (2010: £60,000) to Thames 21, a range of charities which assist in cleaning rivers and streams within the Thames Valley.
- £316,807 (2010: £197,446) of donations to educational and recreational Ten for Ten projects.
- £182,748 (2010: £60,000) of other donations, including donations of £159,748 to the National Trust.

### Going concern

The directors believe, after due and careful enquiry, that the Company has sufficient resources for its present requirements and, therefore, consider it appropriate to adopt the going concern basis in preparing the 2011 financial statements. Further information is set out in note 1 'Basis of preparation' on page 38.

### Disclosure of information to the 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.

### Directors' indemnities

The Company has made qualifying third party indemnity provisions for the benefit of its directors and for the benefit of other persons who are directors of associated companies and these remain in force at the date of this report.

### Auditor

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

Approved by the Board of Directors on 9 June 2011 and signed on its behalf by



**Martin Baggs**  
**Chief Executive Officer**

Clearwater Court  
Vastern Road  
Reading  
Berkshire  
RG1 8DB

# Thames Water Utilities Limited

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

The directors are responsible for preparing the Directors' 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 they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

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 Company and of the profit or loss of the Company for that period. In preparing these 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 applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements.
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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 Company and enable them to ensure that the 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 Company and to prevent and detect fraud and other irregularities.

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.

# Thames Water Utilities Limited

## Corporate governance report

### Compliance Regime

The term 'corporate governance' is generally taken to refer to the supervision of the way in which a company is run and how the risks to its business are managed. It embraces inter alia regulation, corporate structure and the function of the Board of Directors. This statement is made in order to comply with Regulatory requirements.

The Company's shareholder and directors are committed to maintaining high standards of corporate governance. Under the terms of its Licence from Ofwat, the Company is required to pay particular regard to the UK Corporate Governance Code (the "Code"), which is something that generally applies only to companies whose shares are listed on the London Stock Exchange. The code acknowledges that departure from its provisions may be justifiable in particular circumstances. As the Company is a wholly-owned subsidiary in a privately-owned group, the Board considers that a significant number of the provisions of the Code are not directly applicable.

### Board Membership

The Board is confident that it acts as independently of the shareholder as is feasible and that it takes decisions objectively in the best interests of the Company. It also believes that it has demonstrated its commitment to ensuring that the Company's obligations to its stakeholders are understood and met, and that the necessary financial and management resources and systems of planning and internal control, are in place to fulfil these obligations. Supported by the CEO and the Executive, the Board continues to take positive action towards regenerating the Company's values and standards and establishing a clear strategic direction for the future.

Certain matters on which decisions are reserved to the Board and the authority given to the CEO and his Executive team is set out in the schedule of delegated authority ("SODA") approved by the Board. The Board is chaired by Sir Peter Mason, KBE. Sir Peter has had a long and distinguished career in the engineering and construction industries, including Private Finance Initiatives and design and project management. He has also held several public service appointments, primarily with the Department for Trade and Industry (now part of the Department for Business Innovation and Skills). Sir Peter's external appointments include, Senior Independent Director of BAE Systems plc and Subsea 7 S A (formally Acergy S.A). Owing to his directorships in other group companies, Sir Peter is considered not to be independent and neither was he upon his appointment. Sir Peter's responsibilities as Chairman include leadership of the Board, ensuring its effectiveness, setting its agenda and ensuring effective communication with the Company's shareholder. Additionally, he is responsible for ensuring that the directors receive accurate, timely and clear information and that constructive relations exist between the Board and the Executive.

The directors have specialist knowledge of the water industry and other regulated utilities. The Board and Ofwat consider that Michael Pavia (former Chief Financial Officer of the London Electricity Group), Edward Richards (Chief Executive of Ofcom) and Dame Deirdre Hutton CBE (Chair, UK Civil Aviation Authority) are independent non-executive directors.

During January and February 2011, external consultants undertook a detailed evaluation of the Board's performance and that of its committees. The results of the evaluation were considered and discussed by the Board in March 2011 and the results will be used to re-assess effectiveness during the year.

# Thames Water Utilities Limited

## Corporate governance report (continued)

### Committees of the Board

The four standing committees of the Board are as follows:

- Audit and Risk Review
- Regulatory
- Health, Safety and Environment
- Compensation and HR

Each committee has written terms of reference and the collective function of the Committees is to exercise oversight on behalf of the Board and to provide advice to the Board. Other committees are formed as and when required to deal with specific matters, for example the Thames Tideway Tunnel Project.

Membership of the committees throughout the year ended 31 March 2011 is set out below.

Audit and Risk Review Committee ("ARRC")	M Pavia (Chairman), (appointed Chairman 10 June 2010), E Beckley (resigned 10 June 2010), G I W Parsons (appointed 10 June 2010) and R Blomfield-Smith
Regulatory Committee	G I W Parsons (Chairman) (appointed 10 June 2010), M W Baggs (resigned 10 June 2010), E Beckley, E C Richards (appointed 7 September 2010), M Pavia (appointed 27 April 2010, resigned 7 September 2010) and D Shah OBE
Health, Safety and Environment Committee	M Pavia (Chairman) (resigned 7 September 2010), G I W Parsons (appointed 10 June 2010, appointed Chairman 7 September 2010), M W Baggs (resigned 4 May 2010), S Kolenc (resigned 7 September 2010), Dame D M Hutton CBE (appointed 7 September 2010) and D Shah OBE (appointed 7 September 2010)
Compensation and HR Committee	M Stanley (resigned as Chairman 23 November 2010), C Deacon, Sir Peter Mason KBE (appointed Chairman 23 November 2010), W Smit (resigned 1 September 2010) and M Pavia (appointed 7 September 2010)

The Board reviews risk management arrangements and the effectiveness of the Company's internal control systems through the work of the ARRC. The primary objectives of the ARRC are the preservation of good financial practices throughout the Company, ensuring that robust controls are in place to support the integrity of those practices, reviewing risk management processes, reviewing the Company's interim and annual financial statements and the June Return to the Water Services Regulatory Authority and the provision, by way of (amongst other things) meetings, of a line of communication between the Board and external auditor.

## Corporate governance report (continued)

### Internal control

The Board has overall responsibility for the Company's system of internal control. The system is designed to manage rather than eliminate the risk of failure to meet business objectives and can only provide reasonable, not absolute assurance, against material misstatement or loss.

The key features of the system of internal control and risk management are as follows:

- A control environment with clearly defined organisational structures operating within a framework of policies and procedures covering every aspect of the business.
- Comprehensive business planning, risk assessment and financial reporting procedures, including the annual preparation of detailed operational budgets for the year ahead and projections for subsequent years.
- Regular monitoring of risks and control systems throughout the year, supported by the use of risk registers.
- A self-certification process whereby management is required to confirm that the system of internal control is operating effectively.
- An internal audit function providing independent scrutiny of internal control systems and risk management procedures.
- A review of reports produced by internal and external audit.

The directors routinely review the effectiveness of the system of internal control and risk management, principally by means of:

- Regular presentations to the ARRC and Executive by heads of individual business units and functional heads, describing their risk management strategies and detailing the status of significant business risks.
- Reports of significant changes to the Company's overall risk profile, which are also reported to the ARRC.
- Standing reports from the Internal Audit Department to the ARRC.
- Reports to the ARRC on the results of the self-certification process and independent reports thereon by the Internal Audit Department.
- An annual review of the effectiveness of the Company's systems of risk management and internal control by the Board.

### Auditor's independence and objectivity

The ARRC monitors regularly the non-audit services provided to the Company by the external auditor. The auditor does not:

- Self review.
- Make management decisions for the Company.
- Have a mutuality of financial interest with the Company.
- Act in the role of advocate for the Company.

The ARRC regularly meets with the auditor in private. Approval of the ARRC is required for any services provided by the external auditor for which the fee is likely to be in excess of £100,000.

Details of the fees paid to the external auditor during the year ended 31 March 2011 for audit and non-audit services are set out in note 3 to the financial statements on page 46 of this Annual report and financial statements.





## **Independent Auditor's Report to the Members of Thames Water Utilities Limited**

We have audited the financial statements of Thames Water Utilities Limited for the year ended 31 March 2011 set out on pages 33 to 68. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose.

To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

### **Respective responsibilities of directors and auditor**

As explained more fully in the Directors' Responsibilities Statement set out on page 27, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

### **Scope of the audit of the financial statements**

A description of the scope of an audit of financial statements is provided on the APB's website at [www.frc.org.uk/apb/scope/private.cfm](http://www.frc.org.uk/apb/scope/private.cfm).

### **Opinion on financial statements**

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 March 2011 and of its profit for the year then ended.
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice, and
- have been prepared in accordance with the requirements of the Companies Act 2006.

## **Independent Auditor's Report to the Members of Thames Water Utilities Limited (continued)**

### **Opinion on other matter prescribed by the Companies Act 2006**

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

### **Matters on which we are required to report by exception**

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

- Adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us, or
- The financial statements 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.



**Paul Johnson (Senior Statutory Auditor)**  
**for and on behalf of KPMG Audit Plc, Statutory Auditor**  
Chartered Accountants  
15 Canada Square  
London  
E14 5GL  
9 June 2011

# Thames Water Utilities Limited

## Profit and loss account for the year ended 31 March

	Note	31 March 2011 £m	31 March 2010 £m
<b>Turnover</b>		<b>1,623.1</b>	1,623.8
Operating costs	3	<b>(1,022.9)</b>	(952.7)
<b>Operating profit</b>		<b>600.2</b>	671.1
Profit on sale of fixed assets	4	<b>10.9</b>	37.9
Interest payable and similar charges	6	<b>(426.4)</b>	(273.3)
Interest receivable	6	<b>28.1</b>	32.7
Other finance expense	25	<b>(4.3)</b>	(14.8)
<b>Profit on ordinary activities before taxation</b>		<b>208.5</b>	453.6
Taxation on profit on ordinary activities	7	<b>16.7</b>	(122.6)
<b>Profit for the financial year</b>	20	<b>225.2</b>	331.0

There are no differences between the profit on ordinary activities before taxation for the periods as stated above and their historical cost equivalents

All amounts above relate to continuing operations.

## Statement of total recognised gains and losses for the year ended 31 March

	Note	31 March 2011 £m	31 March 2010 £m
Profit for the financial year		<b>225.2</b>	331.0
Actuarial loss on pension scheme	25	<b>(1.1)</b>	(105.4)
Deferred tax (charge)/relief relating to actuarial loss		<b>(3.2)</b>	29.5
<b>Total recognised gains in the year</b>		<b>220.9</b>	255.1

# Thames Water Utilities Limited

## Balance sheet as at 31 March

	Note	31 March 2011 £m	31 March 2010 £m
<b>Fixed assets</b>			
Tangible assets	9	8,145.2	7,532.4
Investments	10	0.1	0.1
		<b>8,145.3</b>	<b>7,532.5</b>
<b>Current assets</b>			
Stocks	11	8.2	7.7
Debtors: amounts falling due within one year	12	621.9	603.0
Debtors: amounts falling due after more than one year	13	1,865.0	1,180.0
		<b>2,486.9</b>	<b>1,783.0</b>
Investments	16	775.8	573.2
Cash at bank and in hand	16	3.6	5.9
		<b>3,274.5</b>	<b>2,369.8</b>
<b>Creditors: amounts falling due within one year</b>	14	<b>(1,016.3)</b>	<b>(1,350.5)</b>
<b>Net current assets</b>		<b>2,258.2</b>	<b>1,019.3</b>
<b>Total assets less current liabilities</b>		<b>10,403.5</b>	<b>8,551.8</b>
<b>Creditors: amounts falling due after more than one year</b>	15	<b>(7,748.7)</b>	<b>(5,789.7)</b>
<b>Provisions for liabilities and charges</b>	17	<b>(1,054.3)</b>	<b>(1,098.3)</b>
<b>Net assets excluding pension liabilities</b>		<b>1,600.5</b>	<b>1,663.8</b>
Net pension liabilities	25	(94.6)	(107.4)
<b>Net assets including pension liabilities</b>		<b>1,505.9</b>	<b>1,556.4</b>
<b>Capital and reserves</b>			
Called-up share capital	18	1,029.0	1,029.0
Share premium account	19	100.0	100.0
Profit and loss account	20	376.9	427.4
<b>Total shareholder's funds</b>	21	<b>1,505.9</b>	<b>1,556.4</b>

The notes on pages 38 to 68 form part of these financial statements.

The financial statements were approved by the Board of Directors on 9 June 2011 and signed on its behalf by:



**Mark Braithwaite**  
Chief Financial Officer

# Thames Water Utilities Limited

## Cash flow statement for the year ended 31 March

	Note	31 March 2011 £m	31 March 2010 £m
Net cash inflow from operating activities	(a)	943.1	1,011.8
<b>Returns on investments and servicing of finance</b>			
Interest received		110.4	200.5
Interest paid		(269.3)	(298.1)
Interest element in finance lease payments		(6.5)	(10.5)
<b>Net cash outflow from returns on investments and servicing of finance</b>		<b>(165.4)</b>	<b>(108.1)</b>
Taxation		(26.0)	(76.0)
<b>Capital expenditure and financial investment</b>			
Gross cost of purchased fixed assets		(793.8)	(724.7)
Infrastructure renewals expenditure		(107.7)	(71.3)
Receipt of grants and contributions		41.0	43.1
Movement on long term loans to group companies		(685.0)	-
Sale proceeds of fixed assets	(d)	11.5	39.9
<b>Net cash outflow for capital expenditure and financial investment</b>		<b>(1,534.0)</b>	<b>(713.0)</b>
<b>Equity dividends paid</b>		<b>(271.4)</b>	<b>(307.9)</b>
		<b>(1,053.7)</b>	<b>(193.2)</b>
<b>Management of liquid resources</b>			
Increase in current asset investments		(202.6)	(251.6)
<b>Net cash outflow before financing</b>		<b>(1,256.3)</b>	<b>(444.8)</b>
<b>Financing</b>			
Capital element in finance lease payment		(8.6)	(5.4)
New loans		1,807.6	454.7
Repayment of loans		(545.0)	(202.8)
<b>Net cash inflow from financing</b>	(b) & (c)	<b>1,254.0</b>	<b>246.5</b>
<b>Decrease in cash</b>	(b) & (c)	<b>(2.3)</b>	<b>(198.3)</b>

Interest received of £110.4m includes £28.2m received from Thames Water Utilities Holdings Limited which is not included in the adjusted interest cover ratio calculations as defined in the Chief Executive's Report on page 9.

# Thames Water Utilities Limited

## Notes to the cash flow statement for the year ended 31 March

### (a) Reconciliation of operating profit to net cash inflow from operating activities

	Note	31 March 2011 £m	31 March 2010 £m
Operating profit		600.2	671.1
Depreciation (infrastructure renewals charge)	3	132.4	114.0
Depreciation (non infrastructure)	3	260.9	229.5
Difference between pension charge and cash contributions		(26.8)	(36.9)
Increase in stocks		(0.6)	(1.6)
Increase in debtors and prepaid expenses		(12.2)	(62.2)
Increase in creditors and accrued expenses		2.3	117.1
Increase/(decrease) in provisions		0.5	(4.7)
Release of deferred income		(13.6)	(14.6)
<b>Net cash inflow from operating activities</b>		<b>943.1</b>	<b>1,011.8</b>

### (b) Reconciliation of net cash flow to movement in net debt

	Note	31 March 2011 £m	31 March 2010 £m
Decrease in cash in the year		(2.3)	(198.3)
Cash inflow from increase in liquid resources		202.6	251.6
Cash inflow from movement in net debt and financing		(1,254.0)	(246.5)
Increase in net debt resulting from cash flows		(1,053.7)	(193.2)
Non-cash increase in net debt		(192.7)	(39.8)
Total increase in net debt		(1,246.4)	(233.0)
Opening net debt		(5,549.4)	(5,316.4)
<b>Closing net debt</b>	(c)	<b>(6,795.8)</b>	<b>(5,549.4)</b>

The non-cash increase in net debt comprises amortisation of bond fees and the carrying value accretion by RPI, of a number of RPI index-linked bonds and swaps. This adjustment for RPI index-linked bonds and swaps is in accordance with FRS 4 'Capital instruments'.



# Thames Water Utilities Limited

## Notes to the cash flow statement for the year ended 31 March (continued)

### (c) Analysis of movement in net debt

	As at 1 April 2010 £m	Cash flow £m	Other non- cash movements £m	As at 31 March 2011 £m
Cash at bank and in hand	5.9	(2.3)	-	3.6
Current asset investments	573.2	202.6	-	775.8
	579.1	200.3	-	779.4
Debt due within one year	(544.6)	537.0	-	(7.6)
Debt due after more than one year	(5,380.2)	(1,799.6)	(192.7)	(7,372.5)
Finance leases	(203.7)	8.6	-	(195.1)
	(6,128.5)	(1,254.0)	(192.7)	(7,575.2)
<b>Total</b>	<b>(5,549.4)</b>	<b>(1,053.7)</b>	<b>(192.7)</b>	<b>(6,795.8)</b>

### (d) Profit on disposal of fixed assets

The proceeds received regarding the profit on the sale of fixed assets for the year ending 31 March 2011 of £11.5m (2010: £39.9m) have been included within Capital expenditure and financial investment.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 1 Principal accounting policies

The following accounting policies have been applied consistently in dealing with items, which are considered material to the financial statements, except as noted below.

#### Basis of preparation

The financial statements are prepared in accordance with the historical cost convention and with applicable accounting standards in the UK and, except for the treatment of certain capital contributions, with the Companies Act 2006. An explanation of this departure from the requirements of the Act is given in note 1(b) below.

The Company has not prepared consolidated group financial statements, as permitted under section 400 of the Companies Act 2006. The Company and its subsidiaries are included in the consolidated financial statements of its ultimate parent company Kemble Water Holdings Limited, a company registered in the United Kingdom.

#### Going concern

The Company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Chief Executive Officer's Business review on pages 4 to 22. The financial position of the Company, its cash flows, liquidity position and borrowing facilities are described in the Chief Executive Officer's Business review on pages 7 to 9. The Chief Executive Officer's Business review also includes details of the Company's Treasury policy, capital structure and financial risk management.

The Company meets its capital programme requirements by raising new debt. Day to day working capital requirements are funded by the business. During the year £1,807.6m, net of bond issuance costs, of new debt were secured and there is no current requirement to raise additional finance to meet future project obligations. There are also cash balances of £779m and committed facilities with a group of banks of £1,175m, which are only likely to be used on rare occasions. Of the £1,175m, £425m 364 day facilities are due for renewal by July 2011 with the remainder maturing in September 2012. The current economic conditions create uncertainty particularly over (a) the level of revenue earned from regulatory activities; (b) the increased occurrence of bad debts; and (c) the availability of bank finance in the foreseeable future. The Company's forecasts and projections, taking account of reasonably possible changes in trading performance, show that the Company should be able to operate within the level of its current facilities for 15 months.

The directors believe, after due and careful enquiry, that the Company has sufficient resources for its present requirements and, therefore, consider it appropriate to adopt the going concern basis in preparing the 2011 financial statements.

#### Changes to accounting policies

The same accounting policies used for the year ended 31 March 2010 have been applied in these financial statements.

#### Changes in accounting estimates

Following the Government's announcement in July 2010 that statutory increases in deferment and retirement benefits would be based on the Consumer Price Index ("CPI") rather than the Retail Price Index ("RPI"), the Company undertook a review of its Pension Schemes' rules. Following guidance contained in the Urgent Issues Task Force ("UITF") Abstract 'Accounting implications of the replacement of the Retail Price Index with the Consumer Price Index for Retirement Benefits' the Company has recognised a £37.6m credit in the Statement of total recognised gains and losses in respect of the Thames Water Mirror Image Pension Scheme ("TWMIPS") see page 43, and note 25 page 65.



# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 1 Principal accounting policies (continued)

#### Summary of significant accounting policies

The principal accounting policies adopted in the preparation of the financial statements are set out below.

#### (a) Revenue recognition

Revenue represents the fair value of the income receivable in the ordinary course of business for goods and services provided and are recognised in accordance with FRS 5 'Reporting the Substance of Transactions'. No adjustment is made to reduce revenue by an estimated bad debt charge to reflect the fair value as this is not deemed material. Where relevant, revenue includes an estimate of the sales value of water supplied and waste water charges to customers between the date of the last meter reading and the period end, exclusive of value added tax. The estimated usage is based upon historical data, judgement and assumptions; actual results could differ from these estimates, which would result in operating revenues being adjusted in the period for which the revision to the estimates is determined. For customers who do not have a meter, the receivable billed is dependent upon the rateable value of the property, as assessed by an independent rating officer.

Additional charges added to a customer's account as a result of debt recovery activity, such as court costs or solicitors fees, are recognised as favourable operating costs when payment is received in both the statutory and regulatory accounts. The Company currently does not have any charges on income; any outstanding revenue is recovered in the normal course of business. All water and sewerage charges billed to customers are recognised as income at the time they are billed and apportioned over the period to which they relate. For consumption by measured customers which has not yet been billed, an accrual is estimated.

Where there is a change of customer in an unmeasured property but the Company cannot confirm the name, a bill is raised in the name of "The Occupier". The Company does not raise billing in the name of the Occupier for metered accounts. However, an unmeasured bill in the name of the Occupier will be cancelled and rebilled once the Company has confirmation of the customer's name. If confirmation is not received the bill is cancelled and the property is classified as empty.

Where a property is classified as empty, an empty property process is followed to verify when the property becomes occupied and/or obtain the name of the customer. The status is established with the customer at point of contact, if the property is not chargeable after 10 weeks the unfurnished / unoccupied state is confirmed visually. The empty property process comprises a number of steps. If these steps confirm that a property appears to be empty then the supply may be turned off. The property will only cease to be classified as empty when a named customer is identified and billed. The Company does not recognise income in respect of empty properties. If the Company has turned off the supply of water at the mains to a property at a customer's request then water supply charges are not payable. A customer may request the supply to be turned off in instances such as the property is to be demolished or where a house previously converted into flats (and additional supplies made) to be converted back into a house.

With regard to new properties, an estimate is made of the sales value of water supplied and waste water charges to customers between the date of connection and the period end.

The Company recognises all revenue at the time of delivery. Should the Company consider that the criteria for revenue recognition are not met for a transaction, revenue recognition would be delayed until such time as the transaction becomes fully earned. Payments received in advance of delivery are recorded as deferred revenue.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 1 Principal accounting policies (continued)

#### (b) Tangible fixed assets

Tangible fixed assets comprise infrastructure assets (mains, sewers and pumped raw water storage reservoirs and sludge pipelines), and other assets (including land, buildings, properties, over ground plant and equipment).

Directly attributable costs are capitalised within fixed assets. These costs include employee costs and other internal costs that are incremental to the business due to the scale and nature of the capital implementation programme of the Company. Interest costs are not capitalised.

The estimated useful economic lives of fixed assets are based on management's judgement and experience. When management identifies that actual useful lives differ materially from the estimates used to calculate depreciation, that charge is adjusted prospectively.

The carrying values of fixed assets are also reviewed for impairment where there has been a trigger event by assessing the present value of estimated future cash flows and net realisable value compared with net book value. The calculation of estimated future cash flows and residual values is based on the directors' best estimates of future prices, output and costs and is therefore subjective.

- **Infrastructure assets**

Infrastructure assets comprise a network of systems. In the UK Water and Waste regulated business, all expenditure on infrastructure assets is capitalised at cost, whilst the planned element incurred in maintaining the operating capability of the network in accordance with defined service standards is expensed as Infrastructure Renewals Charge ("IRC") within depreciation.

Following the completion of the Company's assessment of the infrastructure renewals expenditure requirement to the end of AMP 7 for the Final Business Plan, the Company now considers that it would be appropriate to reflect in its regulatory and statutory accounts an infrastructure renewals charge consistent with its expenditure plans for the AMP 5 to AMP 7 (2010-2025) periods.

- **Capital contributions**

Capital contributions received in respect of infrastructure assets have been deducted from the cost of fixed assets. This is not in accordance with Schedule 1 to the Companies Act 2006, which requires fixed assets to be stated at their purchase price without deduction of contributions, which are accordingly accounted for as deferred income. This departure from the requirement of the Act is, in the opinion of the directors, necessary for the financial statements to give a true and fair view because infrastructure assets do not have a determinable finite life. The financial effect of this departure is disclosed in note 9.

Where material, contributions received towards the cost of other assets are accounted for as deferred income and released to the profit and loss account over the estimated economic lives of the assets.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 1 Principal accounting policies (continued)

#### (b) Tangible fixed assets (continued)

- Other assets

All other assets, comprising plant and equipment and land and buildings, are stated at cost less accumulated depreciation.

Cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably.

Freehold land is not depreciated and assets in the course of construction are not depreciated until they are commissioned. Other assets are depreciated by writing off their cost less their estimated residual value evenly over their estimated useful lives, down to zero, based on management's judgement and experience, which are principally as follows:

Buildings	15 - 60 years
Operational structures	30 - 100 years
Other operational assets	5 - 40 years
Fixtures, fittings, vehicles and computers	3 - 7 years
Fixed and mobile plant	3 - 40 years

Depreciation methods, residual values and useful lives are re-assessed annually and, if necessary, changes are accounted for prospectively.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the profit and loss account.

#### (c) Impairment of tangible fixed assets

Fixed assets are assessed for impairment whenever there is an indication of impairment to determine whether any assets may have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. Where the asset does not generate cash flows that are independent from other assets, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs.

The recoverable amount is the higher of fair value less costs to sell, and value in use. Value in use represents the net present value of expected future cash flows discounted on a pre-tax basis using a rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. Impairment of non-current assets is recognised in the profit and loss account within operating costs.

Where an impairment loss subsequently reverses, it is recognised in the profit and loss account and the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but not so as to exceed the carrying amount that would have been determined had no impairment loss been recognised in prior years.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 1 Principal accounting policies (continued)

#### (d) Stocks

Stocks are stated at the lower of cost and net realisable value. Costs comprise direct materials and, where applicable, direct labour costs and those overheads that have been incurred in bringing the inventories to their present location and condition. Cost is calculated using the weighted average method. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

#### (e) Taxation

The tax expense represents the sum of current tax and deferred tax.

- **Current taxation**

Current taxation, including UK corporation tax and foreign tax, is based on the taxable profit for the period and is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantially enacted at the balance sheet date.

Taxable profit differs from the profit on ordinary activities before tax as reported in the profit and loss account because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible.

- **Deferred taxation**

Deferred taxation is recognised without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes, which have arisen but not reversed by the balance sheet, except as otherwise required by FRS 19 'Deferred tax'.

A net deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits against which to recover carried forward tax losses and from which the future reversal of underlying timing differences can be deducted.

Deferred taxation is measured at the tax rates that are expected to apply in the periods in which the timing differences are expected to reverse based on tax rates and laws that have been enacted or substantially enacted by the balance sheet date.

Deferred tax is charged or credited in the profit and loss account except when it relates to items charged or credited to equity, in which case the deferred tax is also dealt with via the Statement of total recognised gains and losses.

#### (f) Leased assets

Leases are classified according to the substance of the transaction. A lease that transfers substantially all the risks and rewards of ownership to the lessee is classified as a finance lease. All other leases are classified as operating leases.

- **Finance leases**

Finance leases are capitalised in the balance sheet at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease.

The corresponding liability is shown as a finance lease obligation to the lessor. Leasing repayments comprise both a capital and a finance element. The finance element is written off to the profit and loss account so as to produce an approximately constant periodic rate of charge on the outstanding obligation. Such assets are depreciated over the shorter of their estimated useful lives and the period of the lease to the first break clause.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 1 Principal accounting policies (continued)

#### (f) Leased assets (continued)

- Operating leases

Operating lease rentals are charged to the profit and loss account on a straight-line basis over the period of the lease.

#### (g) Pension and other post retirement benefits

The Company operates two large defined benefit pension schemes. The Company accounts for these schemes in accordance with FRS 17 'Retirement Benefits'. These schemes are independently, administered funds, for the substantial majority of the Company's employees. Actuarial valuations are carried out as determined by the pension scheme trustees using the projected unit credit method for both pension schemes at intervals of not more than three years, the rates of contribution payable and the pension cost being determined on the advice of the actuaries, having regard to the results of these valuations. The Company believes that the assumptions utilised in recording obligations under the two schemes are reasonable based on prior experience, market conditions and the advice of scheme actuaries. However, actual results may differ from such assumptions. For any intervening reporting period, the actuaries review the continuing appropriateness of the contribution rates (a complete actuarial valuation is performed every three years). Defined benefit assets are measured at fair value while liabilities are measured at present value (which approximates to fair value).

The difference between the assets and liabilities of the schemes are recognised as a surplus (to the extent that the surplus is recoverable) or obligation in the balance sheet.

The cost of providing pension benefits to employees is included in the profit and loss account within the cost of employee benefits. The difference between the expected return on scheme assets and interest on scheme liabilities are included within other finance income/expense in the profit and loss account.

Actuarial gains and losses are recognised outside the profit and loss account in retained earnings and are presented in the Statement of total recognised gains and losses.

In addition, the Company operates two closed defined contribution pension schemes. The Company has no further payment obligations for these schemes. However, defined funds for individuals are held within these schemes.

During 2010-11 the Company has introduced a new Defined Contribution Stakeholder Pension Scheme ("DCSPS"), managed through Standard Life Assurance Limited ("Standard Life"). In 2010-11 the only members joining this scheme were six newly-recruited executives joining the Company who were not offered a defined benefit pension arrangement. From 1 April 2011 the DCSPS will become the only scheme to which new entrants to the Company will be eligible. The remainder of the Company's Extended Leadership Team of executives have joined this scheme from 1 April 2011 and are no longer active members of a defined benefit arrangement.

For further details in respect of changes in accounting estimates see page 38, and for information regarding post balance sheet events see note 27, page 67

#### (h) Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange current at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into sterling using the rate of exchange current at the balance sheet date. Gains and losses arising on retranslation are included in the profit and loss account for the year.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 1 Principal accounting policies (continued)

#### (i) Cash

Cash includes cash at bank and in hand, deposits, and short-term highly liquid investments which are readily convertible on initial investment into known amounts of cash at any time without penalty or if a maturity or period of notice of not more than 24 hours or one working day has been agreed.

#### (j) Debtors

Debtors are stated at nominal value (which approximates to fair value) less allowances for estimated irrecoverable amounts.

#### (k) Creditors

Creditors are stated at their nominal value (which approximates to fair value).

#### (l) Financial liabilities and equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities.

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

#### • Borrowings

Interest bearing bank loans and overdrafts are recorded as the proceeds received, net of direct issue costs. Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an amortised cost basis in the profit and loss using the effective interest method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

#### • Financial instruments and derivatives

Interest rate swap agreements and financial futures are used to manage interest rate exposure. While the Company enters into currency swaps to manage its exposure to fluctuations in exchange rates, the Company does not use derivative financial instruments for speculative purposes.

The Company currently does not apply FRS 26 'Financial Instruments: Recognition and Measurement', and accordingly the disclosure requirements of FRS 29 'Financial Instruments: Disclosures' are not applicable. Therefore, the presentation requirements of FRS 25 'Financial Instruments: Presentation' have been applied. However, certain voluntary disclosures have been prepared to aid understanding and comparability with prior year.

Foreign currency and interest rate swaps are accounted for on an amortised cost basis in accordance with FRS 4 'Capital Instruments'. Swaps are included in the appropriate caption in note 16.

#### (m) Accruals and deferred income

Grants and contributions receivable in respect of depreciating fixed assets are treated as deferred income, which is credited to the profit and loss account over the estimated economic lives of the related assets.

#### (n) Research and development

Expenditure on research and development is written off to the profit and loss account in the year in which it is incurred.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 1 Principal accounting policies (continued)

#### (o) Accounting for provisions and contingencies

The Company is subject to a number of claims that are incidental to the normal conduct of its business. These relate to and include commercial and contractual claims, which are handled and defended in the ordinary course of business. The Company routinely assesses the likelihood of any adverse judgements or outcomes to these matters as well as ranges of probable and reasonably estimated losses. Reasonable estimates involve judgements made by management after considering information including notifications, settlements, estimates performed by independent parties and legal counsel, available facts, identification of other potentially responsible parties and their ability to contribute, and prior experience.

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Insurance provisions are recognised or released by assessing their adequacy using current estimates of future cash flows under insurance contracts. Provisions are recorded in the balance sheet at their full value and are not therefore discounted.

#### (p) Related party disclosures

The Company has taken advantage of the exemption under paragraph 3(c) from the provisions of FRS 8 'Related party disclosures', which requires the disclosure of the details of material transactions between the reporting entity and any related parties within the Kemble Water Holdings Limited Group, on the grounds that it is a wholly owned subsidiary of Kemble Water Holdings Limited, a company registered in the United Kingdom.

#### (q) Dividends

Dividends unpaid at the balance sheet date are only recognised as a liability at that date to the extent that they are appropriately authorised and are no longer at the discretion of the Company. Unpaid dividends that do not meet these criteria are disclosed in the notes to the financial statements.

#### (r) Provision for doubtful debts

At each reporting date, the Company evaluates the collectability of trade receivables and records provisions for doubtful receivables based on experience. These provisions are based on, amongst other things, comparisons of the relative age of accounts and consideration of actual write-off history. The actual level of receivables collected may differ from the estimated levels of recovery, which could impact operating results positively or negatively.

### 2 Segmental analysis

The directors consider that the Company has one class of business and this is conducted wholly within the United Kingdom.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 3 Operating costs

Analysis of operating costs by type of expense:

	Note	31 March 2011 £m	31 March 2010 £m
Staff costs	5	207.5	200.8
Materials and consumables		136.6	135.2
Other operating charges		433.7	437.9
Depreciation:			
Owned assets (infrastructure renewals charge)	9	132.4	114.0
Owned assets (non-infrastructure)	9	251.3	219.9
Assets held under finance leases (non-infrastructure)	9	9.6	9.6
Rental under operating leases:			
Hire of plant and machinery		9.3	3.1
Other		5.4	7.2
Research and development		3.4	3.5
Other operating income		(7.3)	(8.1)
Foreign currency loss		0.9	0.8
		1,182.8	1,123.9
Own work capitalised		(159.9)	(171.2)
		1,022.9	952.7

Included in the above is auditor's remuneration in respect of the following:

	31 March 2011 £'000	31 March 2010 £'000
<b>Fees payable to the auditor:</b>		
Fees payable to the Company's auditor for the audit of the Company's accounts	213	187
Fees payable to the Company's auditor and its associates for other services:		
Other services pursuant to legislation	78	77
Other services relating to taxation	18	4
All other services	241	78
Total aggregate remuneration	550	346

No other fees were payable to KPMG Audit Plc in respect of this year or the prior year.

### 4 Profit on sale of fixed assets

	31 March 2011 £m	31 March 2010 £m
Profit on disposal of fixed assets	10.9	37.9
Taxation attributable, included in the charge for the period	2.0	4.7



# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 5 Information regarding directors and employees

Aggregate directors' emoluments:

	<b>31 March 2011 £'000</b>	<b>31 March 2010 £'000</b>
Salary	<b>1,092</b>	916
Pension	<b>89</b>	346
Bonus	<b>1,981</b>	1,641
Other benefits	<b>65</b>	985
<b>Total aggregate emoluments</b>	<b>3,227</b>	3,888

Included in the table above, is £2,911,903 (2010: £3,200,064) for the executive directors for their services to the Company. In addition, the executive directors received total remuneration of £883,112 (2010: £1,608,657) for their services to other companies within the Group.

At 31 March 2011 £45,031 is accruing to 2 directors (2010: £39,898 for 2 directors) under the Group's defined benefit scheme in respect of services to the Company.

At 31 March 2011 £79,495 is accruing to 1 director (2010: £nil for nil directors) under a defined contribution scheme.

#### Highest paid director

Total emoluments, including payments and accruals under long term incentive schemes of the highest paid director in respect of work done for the Company during the year was £1,168,425 (2010: £1,247,711) and accrued pension under a defined contribution scheme was £79,495 (2010: £25,824, defined benefit scheme). In addition, emoluments of £500,753 (2010: £244,693) was paid to the highest paid director for services to other companies within the Group.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 5 Information regarding directors and employees (continued)

#### Employee information

The average number of persons employed by the Company, including executive directors, during the year, analysed by category, was as follows:

	31 March 2011 Number	31 March 2010 Number
Support	331	292
Operations	4,555	4,803
<b>Total employee numbers</b>	<b>4,886</b>	<b>5,095</b>

Employment costs including executive directors' remuneration were:

	Note	31 March 2011 £m	31 March 2010 £m
Salaries and wages		167.3	169.1
Social security costs		13.7	15.1
Pension costs	25	25.2	17.6
Severance costs		3.1	0.9
<b>Total</b>		<b>209.3</b>	<b>202.7</b>
Employment costs included within research and development		(1.8)	(1.9)
<b>Net employment costs</b>		<b>207.5</b>	<b>200.8</b>

### 6 Net interest payable and similar charges

	31 March 2011 £m	31 March 2010 £m
Bank loans, overdrafts and other loans:		
Group loans	(358.0)	(223.4)
Bank loans	(28.7)	(34.5)
Other loans	(21.8)	(5.6)
Swaps	(12.3)	-
Finance charges in respect of finance leases	(5.6)	(9.8)
<b>Interest payable and similar charges</b>	<b>(426.4)</b>	<b>(273.3)</b>
Interest receivable:		
Group loans	24.4	28.3
Other loans	3.7	4.2
Swaps	-	0.2
<b>Interest receivable</b>	<b>28.1</b>	<b>32.7</b>
<b>Net interest payable and similar charges</b>	<b>(398.3)</b>	<b>(240.6)</b>

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 6 Net interest payable and similar charges (continued)

Amounts (payable)/receivable on swaps relate to interest rates taken out to hedge rates on borrowings. See note 16, page 56.

The net interest (payable)/receivable on swaps is the aggregate effect of all swaps held in the Company.

### 7 Taxation

#### (a) Analysis of charge in the year

	Note	31 March 2011 £m	31 March 2010 £m
Current tax:			
Amounts payable in respect of corporation tax for the year		4.8	59.7
Adjustment in respect of prior years		(4.3)	(12.2)
Total current tax	7(b)	0.5	47.5
Deferred tax:			
Origination and reversal of timing differences		50.1	57.4
Adjustments in respect of prior years		2.1	11.8
Impact on deferred tax of tax rate change to 26%		(74.8)	-
Deferred tax (credit)/provision	17	(22.6)	69.2
Timing difference on pension cost charge	25	5.4	5.9
Total deferred tax (credit)/charge		(17.2)	75.1
Taxation (credit)/charge on profit on ordinary activities		(16.7)	122.6

#### (b) Factors affecting tax charge for the year

The corporation tax (credit)/charge is based upon UK corporation tax at 28% (2010: 28%).

The tax (credit)/charge for the year is lower (2010: lower) than the standard rate of corporation tax in the UK (28%), (2010: 28%). The differences are explained below:

	31 March 2011 £m	31 March 2010 £m
Profit on ordinary activities before tax	208.5	453.6
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 28% (2010: 28%)	58.4	127.0
Effects of:		
Disallowable expenditure less non taxable income	1.9	(4.0)
Capital allowances for the year in excess of depreciation and other timing differences	(50.1)	(57.4)
Pension cost charge lower than pension cost relief	(5.4)	(5.9)
Adjustments to tax charge in respect of prior years	(4.3)	(12.2)
Current tax charge for the year	0.5	47.5

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 7 Taxation (continued)

#### (c) Factors affecting tax charge for the year

On 23 March 2011 the Chancellor announced the reduction in the main rate of UK corporation tax to 26% with effect from 1 April 2011. This change became substantively enacted on 29 March 2011 and therefore the effect of the rate reduction creates a reduction in the deferred tax liability, which has been included in the figures above.

The Chancellor also proposed changes to further reduce the main rate of corporation tax by 1% per annum to 23% by 1 April 2014, but these changes have not yet been substantively enacted and therefore are not included in the figures above. The overall effect of the further reductions from 26% to 23%, if these are applied to the deferred tax balance at 31 March 2011, would be to further reduce the deferred tax liability by approximately £112.3m.

### 8 Dividends

The aggregate amount of dividends comprises:	Note	31 March 2011 £m	31 March 2010 £m
<i>Dividends paid in respect of prior year but not recognised as liabilities in that year:</i>			
Second interim paid 2.7p (2010: nil) per ordinary share		<b>28.2</b>	-
Third interim paid: 7.3p (2010: 11.4p) per ordinary share		<b>75.1</b>	116.9
Fourth interim paid: nil (2010: 5.8p) per ordinary share		-	60.0
<i>Interim dividends paid in respect of the current year:</i>			
First interim paid: 5.6p (2010: 12.7p) per ordinary share		<b>57.3</b>	131.0
Second interim paid 7.3p (2010: nil) per ordinary share		<b>75.0</b>	-
Third interim paid 3.5p (2010: nil) per ordinary share		<b>35.8</b>	-
	20 & 21	<b>271.4</b>	307.9

For information in respect of post balance sheet events, see note 27 on page 67.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 9 Tangible fixed assets

	Land and buildings	Plant and equipment	Infrastructure assets	Assets in course of construction	Total
	£m	£m	£m	£m	£m
<b>Cost</b>					
At 1 April 2010	2,274.5	4,102.0	4,174.0	1,176.3	11,726.8
Reclassification *	-	-	13.7	-	13.7
At 1 April 2010 restated	2,274.5	4,102.0	4,187.7	1,176.3	11,740.5
Additions	-	-	-	1,035.0	1,035.0
Transfers between items **	242.9	317.9	461.9	(1,022.7)	-
Disposals	(0.8)	(3.8)	-	-	(4.6)
<b>At 31 March 2011</b>	<b>2,516.6</b>	<b>4,416.1</b>	<b>4,649.6</b>	<b>1,188.6</b>	<b>12,770.9</b>
<b>Capital contributions</b>					
At 1 April 2010	-	-	589.1	-	589.1
Reclassification *	-	-	13.7	-	13.7
At 1 April 2010 restated	-	-	602.8	-	602.8
Additions	-	-	28.4	-	28.4
<b>At 31 March 2011</b>	<b>-</b>	<b>-</b>	<b>631.2</b>	<b>-</b>	<b>631.2</b>
<b>Depreciation</b>					
At 1 April 2010	598.2	2,066.4	940.7	-	3,605.3
Provided during the year	40.4	220.5	132.4	-	393.3
Disposals	(0.3)	(3.8)	-	-	(4.1)
<b>At 31 March 2011</b>	<b>638.3</b>	<b>2,283.1</b>	<b>1,073.1</b>	<b>-</b>	<b>3,994.5</b>
<b>Net book value</b>					
<b>At 31 March 2011</b>	<b>1,878.3</b>	<b>2,133.0</b>	<b>2,945.3</b>	<b>1,188.6</b>	<b>8,145.2</b>
At 31 March 2010	1,676.3	2,035.6	2,644.2	1,176.3	7,532.4

The net book value of land and buildings is analysed as follows:

	31 March 2011 £m	31 March 2010 £m
Freehold land and buildings	1,867.7	1,670.8
Leasehold – over 50 years	7.8	2.7
Leasehold – under 50 years	2.8	2.8
	<b>1,878.3</b>	<b>1,676.3</b>

\* The directors have reclassified income received in respect of new infrastructure assets to capital contributions, which were netted within additions in a prior period, as considered to more accurately reflect the nature of the transaction. The net book values have been unaffected as a result of this reclassification.

\*\* The transfers between items within land and buildings include a land purchase of £80.8m for the Thames Tunnel.

Depreciation has not been charged on freehold land stated in the financial statements at cost of £117.1m (2010: £34.9m).

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 9 Tangible fixed assets (continued)

Details of the Company's tangible fixed assets, which are held under finance leases, are:

	<b>Total £m</b>
<b>Cost</b>	
At 1 April 2010	272.5
Disposals	(9.3)
<b>At 31 March 2011</b>	<b>263.2</b>
<b>Depreciation</b>	
At 1 April 2010	136.5
Provided during the year	9.6
Disposals	(9.3)
<b>At 31 March 2011</b>	<b>136.8</b>
<b>Net book value</b>	
<b>At 31 March 2011</b>	<b>126.4</b>
At 31 March 2010	136.0

### 10 Fixed asset investments

	<b>31 March 2011 £m</b>	31 March 2010 £m
Cost of shares in subsidiaries	<b>0.1</b>	0.1

At 31 March 2011 the Company held the allotted share capital of the following undertakings:

<b>Name of undertaking</b>	<b>Nominal value and class of shares held</b>	<b>Proportion of nominal value of issued shares held</b>	<b>Activity</b>
Thames Water Utilities Finance Limited	£1 Ordinary	100%	Finance Company
Thames Water Utilities Cayman Finance Holdings Limited	\$1 Ordinary	100%	Finance Company

Thames Water Utilities Finance Limited was incorporated and registered in Great Britain. Thames Water Utilities Cayman Finance Holdings Limited was incorporated and registered in the Cayman Islands.

At 31 March 2011 Thames Water Utilities Finance Limited had net liabilities of £43.2m (2010: liabilities £32.1m) and incurred a loss for the year ended 31 March 2011 of £11.1m (2010: loss £32.2m).

At 31 March 2011 Thames Water Utilities Cayman Finance Holdings Limited had net assets of £1 (2010: £1). No profit or loss had been made in the year (2010: £nil).

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 11 Stocks

	31 March 2011 £m	31 March 2010 £m
Raw materials and consumables	8.2	7.7

### 12 Debtors: amounts falling due within one year

	31 March 2011 £m	31 March 2010 £m
Trade debtors	267.6	242.5
Amounts owed by group undertakings		
- Interest	24.4	28.2
- Non interest	0.4	4.0
Amounts receivable in respect of corporation tax	12.3	13.0
Amounts receivable in respect of group relief	28.0	1.8
Other debtors	65.2	52.1
Insurance claims receivable	53.7	75.7
Prepayments and accrued income	170.3	185.7
	621.9	603.0

Amounts owed by group undertakings are comprised of:

- Interest receivable of £24.4m (2010: £28.2m) owed by Thames Water Utilities Holdings Limited, the immediate parent undertaking, on a loan of £1,865.0m (2010: £1,180.0m), of which £24.4m (2010: £28.2m) is included within debtors: amounts falling due within one year and £nil (2010: £nil) within debtors: amounts falling due after more than one year.

Repayment of the interest (£24.4m) was received on 11 April 2011.

- All other amounts are unsecured, interest free and payable on demand.

### 13 Debtors: amounts falling due after more than one year

	31 March 2011 £m	31 March 2010 £m
Amounts owed by group undertakings	1,865.0	1,180.0

Amounts owed by group undertakings are comprised of:

- An unsecured loan of £1,865.0m (2010: £1,180.0m) owed by Thames Water Utilities Holdings Limited, the immediate parent undertaking. The directors do not anticipate any repayment of principal within the next twelve months.

Interest is charged at Libor + 0.35%.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 14 Creditors: amounts falling due within one year

	31 March 2011 £m	31 March 2010 £m
Secured bank loans	-	144.6
Obligations under finance leases	7.9	8.4
Trade creditors:		
- Operating	254.4	247.1
- Capital	332.3	201.6
Amounts owed to group undertakings:		
- Secured loan amounts (see below)	7.6	400.0
- Interest	129.2	90.8
- Non interest	-	0.5
Other taxation and social security payable	3.7	8.0
Accruals and deferred income	281.2	249.5
	<b>1,016.3</b>	<b>1,350.5</b>

### 15 Creditors: amounts falling due after more than one year

	31 March 2011 £m	31 March 2010 £m
Secured bank loans	573.4	619.7
Obligations under finance leases	187.2	195.3
Amounts owed to group undertakings – secured loan amounts (see below)	6,799.1	4,760.5
Accruals and deferred income	189.0	214.2
	<b>7,748.7</b>	<b>5,789.7</b>

Amounts owed to group undertakings for secured loans for the year ended 31 March 2011 are shown net of external cross currency and index linked swaps.

	31 March 2011 £m	31 March 2010 £m
<b>Amounts owed to group undertakings are:</b>		
Inter-company secured loans		
- Within one year	15.0	400.0
- After more than one year	6,672.6	4,760.5
	<b>6,687.6</b>	<b>5,160.5</b>
Non-loan amounts due within one year		
- Interest	129.2	90.8
- Non interest	-	0.5
	<b>6,816.8</b>	<b>5,251.8</b>

Inter-company secured loans for the year ended 31 March 2011 as shown in the above table represent the gross liability of the Company owed to group undertakings as detailed on page 55 and do not include the effect of derivatives.



# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 15 Creditors: amounts falling due after more than one year (continued)

#### Secured bank loans

Each Obligor (the companies within the Securitisation Group) has entered into the Security Trust and Inter-creditor Deed ("STID") with the Security Trustee pursuant to which Thames Water Utilities Holdings Limited will guarantee the obligations of each other Obligor under the finance documents and the Company and its wholly-owned subsidiaries will guarantee the obligations of each other under the finance documents, in each case to the Security Trustee.

Amounts due to group undertakings in respect of non-interest amounts are unsecured, interest free and payable on demand.

Loan amounts owed to group undertakings include:

- £2,699.7m (2010: £2,883.1m) owed to Thames Water Utilities Finance Limited, a subsidiary undertaking, of which £15.0m (2010: £250.0m) is included within creditors due within one year and £2,684.7m (2010: £2,633.1m) within creditors due after more than one year.
- £4,001.5m (2010: £2,139.9m) owed to Thames Water Utilities Cayman Finance Limited, a subsidiary undertaking, of which £nil (2010: £nil) is included within creditors due within one year and £4,001.5m (2010: £2,139.9m) within creditors due after more than one year.
- £nil (2010: £150.0m) of Subordinated debt owed to Thames Water Limited, a parent undertaking of which £nil (2010: £150.0m) is included within creditors due within one year and £nil (2010: £nil) within creditors due after more than one year.

Details of maturity of loans falling due after more than one year are detailed in note 16.

### 16 Financial instruments

FRS 25 requires the disclosure of the funding and treasury policy together with further details on financial assets and liabilities.

#### Funding and treasury policy

The Company's treasury operations are managed centrally by a small specialist team within the Thames Water Group reporting directly to the Chief Financial Officer. The treasury team manages the financing (including debt, interest costs and foreign exchange) for the Group. Treasury policy is focussed on efficient and effective management of cash and financial resources within the Group.

The Company's funding policy is to maintain a broad portfolio of debt. The debt arranged via Thames Water Utilities Finance Limited and Thames Water Utilities Cayman Finance Limited is diversified by source and maturity in order to protect profits against risks arising from adverse movements in interest rates and currency exposures.

Derivative financial instruments, including cross currency swaps, interest rate swaps and index-linked swaps, are employed to manage the currency interest rate and inflation risks arising from the primary financial instruments used to finance the Company's activities.

Short-term debtors and creditors have been excluded from the financial instruments disclosures.

#### Interest rate risk profile of financial liabilities and assets

After taking into account the Company's interest rate and currency swaps, the interest rate risk profile of the Company's financial liabilities and assets is as follows:

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 16 Financial instruments (continued)

#### Financial liabilities

	Total at floating rates		Total at fixed rates *		Total book value		Weighted average interest rate		Weighted average period until maturity for which rate is fixed	
	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m	2011 %	2010 %	2011 Years	2010 Years
Bank loans and overdraft										
- £ Sterling	122.1	397.2	451.3	367.1	573.4	764.3	2.2	2.4	14.1	17.1
Other loans and finance leases **										
- £ Sterling	323.8	350.3	6,678.0	5,013.9	7,001.8	5,364.2	3.7	5.1	24.1	23.8
	445.9	747.5	7,129.3	5,381.0	7,575.2	6,128.5	3.6	4.9	23.5	23.4

\* Included in fixed rate liabilities are index linked loans/swaps at a fixed coupon rate and RPI indexation.

\*\* Includes inter-company debt.

The Company's interest rate and cross currency swaps convert £27.9m (2010: £34.1m) of floating rate borrowing to fixed rate and £235.0m (2010: £235.0m) of fixed rate borrowing to floating rate. Cross currency swaps hedge currency risk on £632.8m (2010: £632.8m) of foreign currency borrowing through conversion to Sterling. Index linked swaps of £894.1m (2010: £894.1m) swapped inter-company fixed rate debt to index linked debt. All swaps are included at their notional amount, Total accretion on the index linked swaps is £92.0m (2010: £44.0m).

Short-term floating rate loans bear interest at rates linked to LIBOR. Base rate is the benchmark rate for all cash at bank.

	Total at floating rates		Total at book value	
	31 March 2011 £m	31 March 2010 £m	31 March 2011 £m	31 March 2010 £m
Short term deposits	775.8	573.2	775.8	573.2
Cash in bank and in hand	3.6	5.9	3.6	5.9
	779.4	579.1	779.4	579.1

#### Currency risk

The Company is not exposed to any significant currency risk after taking the effects of its cross currency swaps into consideration.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 16 Financial instruments (continued)

#### Fair values

Fair value is the amount at which a financial instrument could be exchanged in an arm's length transaction between informed and willing parties, other than in a forced or liquidation sale. The table below sets out a comparison of the book and fair values of the Company's financial instruments.

	<b>Book value</b>		<b>Fair value</b>	
	<b>31 March 2011 £m</b>	<b>31 March 2010 £m</b>	<b>31 March 2011 £m</b>	<b>31 March 2010 £m</b>
<b>Primary financial instruments</b>				
Financial assets:				
- Short term deposits	<b>775.8</b>	573.2	<b>775.8</b>	573.2
- Cash at bank and in hand	<b>3.6</b>	5.9	<b>3.6</b>	5.9
Financial liabilities:				
- Bank loans	<b>(573.4)</b>	(694.0)	<b>(580.8)</b>	(628.0)
- Other loans and finance leases *	<b>(6,881.0)</b>	(5,364.2)	<b>(6,944.4)</b>	(5,425.9)
<b>Derivative financial instruments</b>				
- Interest rate swaps	-	-	<b>(25.3)</b>	(6.4)
- Cross currency swaps	<b>(28.8)</b>	(25.0)	<b>(32.1)</b>	(35.7)
- Index linked swaps	<b>(92.0)</b>	(45.3)	<b>(206.3)</b>	(283.8)
<b>Total</b>	<b>(6,795.8)</b>	(5,549.4)	<b>(7,009.5)</b>	(5,800.7)

\* Includes inter-company debt.

Thames Water Utilities Limited does not itself hold bonds.

Other loans include bonds issued by group undertakings and external providers, which are publicly traded and loaned to Thames Water Utilities Limited. Fair values for these have been calculated using the 31 March 2011 quoted prices.

Mark-to-market techniques (discounting expected cash flows at prevailing interest and exchange rates) are employed in computing fair values for the remaining fixed rate borrowings and all derivative financial instruments.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 16 Financial instruments (continued)

Maturities	31 March 2011 £m	31 March 2010 £m
Bank loans and overdrafts		
- Within one year	-	144.6
- Between one and two years	-	(6.4)
- Between two and five years	-	20.4
- After more than five years	573.4	605.7
	<b>573.4</b>	<b>764.3</b>
Other loans inc. inter-company		
- Within one year	7.6	400.0
- Between one and two years	469.9	10.3
- Between two and five years	299.9	549.6
- After more than five years	6,029.3	4,200.6
	<b>6,806.7</b>	<b>5,160.5</b>
Finance leases		
- Within one year	7.9	8.4
- Between one and two years	56.5	9.4
- Between two and five years	93.3	138.5
- After more than five years	37.4	47.4
	<b>195.1</b>	<b>203.7</b>
<b>Total borrowing</b>	<b>7,575.2</b>	<b>6,128.5</b>

Loans are repayable between 2011 and 2062.

Loans wholly repayable after more than five years, excluding finance leases are:

	31 March 2011 £m	31 March 2010 £m
Bank loans	573.4	605.7
Other loans including inter-company	6,029.2	4,214.7
	<b>6,602.6</b>	<b>4,820.4</b>

Other secured loans repayable to Group undertakings in order of maturity include:

2bn Yen 3.00% Fixed rate bond due 2011.	20bn Yen 3.28% Fixed rate bond due 2038.
€500m 6.13% Fixed rate bond due 2013.	£50m 3.85% Index linked bond due 2040.
£200m 4.90% Fixed rate bond due 2015.	£500m 5.5% Fixed rate bond due 2041.
€500m 3.25% Fixed rate bond due 2016.	£50m 1.98% Index linked bond due 2042.
£400m 7.21% Fixed rate bond due 2018.	£55m 2.09% Index linked bond due 2042.
£200m 5.05% Fixed rate bond due 2020.	£40m 1.97% Index linked bond due 2045.
£225m 6.59% Fixed rate bond due 2021.	£100m 1.85% Index linked bond due 2047.
£175m 3.38% Index linked bond due 2021.	£200m 1.82% Index linked bond due 2049.
£550m 5.38% Fixed rate bond due 2025 (note 1).	£300m 1.68% Index linked bond due 2053.
£330m 6.75% Fixed rate bond due 2028.	£300m 1.68% Index linked bond due 2055.
£300m 5.75% Fixed rate bond due 2030 (note 2).	£200m 1.77% Index linked bond due 2057.
£200m 6.50% Fixed rate bond due 2032.	\$156m 3 month US\$ libor + 0.95% floating rate bond due 2015.
£600m 5.13% Fixed rate bond due 2037.	£350m 1.76% Index linked bond due 2062.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 16 Financial instruments (continued)

#### Maturities (continued)

Note 1: £550m Class B bond issued on a fixed coupon basis until 21 July 2017, when the bond resets to floating rate interest at LIBOR plus margin.

Note 2: £300m Class B bond issued on a fixed coupon basis until 13 September 2022, when the bond resets to floating rate interest at LIBOR plus margin.

See note 15, page 55 for details of secured bank loans.

Loans repayable by instalments after more than five years hence are:

	<b>31 March 2011 £m</b>	31 March 2010 £m
Finance leases	<b>37.4</b>	47.4

The ranges of interest rates on outstanding loans are 0.78% to 8.35% (2010: 1.23% to 8.35%).

These interest rates are those contracted on the underlying borrowing before taking account of interest rate protection. There are no interest free loans.

#### Borrowing facilities

At 31 March 2011 the Company had access to committed facilities of £1,175.0m (2010: £1,105.0m) of which £nil (2010: £nil) had been drawn at the balance sheet date, through its subsidiary company Thames Water Utilities Cayman Finance Limited.

### 17 Provisions for liabilities and charges

	<b>Deferred tax £m</b>	<b>Insurance liabilities £m</b>	<b>Restructuring £m</b>	<b>Other £m</b>	<b>Total £m</b>
At beginning of the year	995.5	75.7	2.3	24.8	1,098.3
Utilised during the year	-	-	(3.6)	(4.2)	(7.8)
(Credit)/charge to profit and loss for the year	(22.6)	(22.0)	3.1	5.3	(36.2)
<b>At end of the year</b>	<b>972.9</b>	<b>53.7</b>	<b>1.8</b>	<b>25.9</b>	<b>1,054.3</b>

On 23 March 2011 the Chancellor announced the reduction in the main rate of UK corporation tax to 26% with effect from 1 April 2011. This change became substantively enacted on 29 March 2011 and therefore the effect of the rate reduction creates a reduction in the deferred tax liability which has been included in the figures above.

The Chancellor also proposed changes to further reduce the main rate of corporation tax by 1% per annum to 23% by 1 April 2014, but these changes have not yet been substantively enacted and therefore are not included in the figures above. The overall effect of the further reductions from 26% to 23%, if these are applied to the deferred tax balance at 31 March 2011, would be to further reduce the deferred tax liability by approximately £112.3m.

The insurance provision is in respect of insurance claims notified. A debtor in respect of these obligations is included in note 12 (see page 53) representing the reimbursement value from captive and third party insurance companies.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 17 Provisions for liabilities and charges (continued)

The restructuring provision principally relates to severance costs as a result of the Company's restructuring and reorganisation. This provision is expected to be utilised over the next year.

Other provisions principally relate to a number of legal claims against the Company and represents Management's best estimate of the value of settlement and costs. It is estimated that some claims will be settled in more than one year.

The elements of deferred tax are as follows:

	Note	31 March 2011 £m	31 March 2010 £m
Accelerated capital allowances		979.6	1,000.1
Other timing differences		(6.7)	(4.6)
		<b>972.9</b>	<b>995.5</b>
<b>Total deferred tax provision:</b>			
Included above		972.9	995.5
Deferred tax asset recognised on pension deficit	25	(33.2)	(41.8)
		<b>939.7</b>	<b>953.7</b>

At 31 March 2011 there are no amounts of deferred tax unprovided for (2010: £nil).

The pension liability per note 25 is shown net of deferred tax.

### 18 Called up share capital

	31 March 2011 £m	31 March 2010 £m
<b>Allotted, called up and fully paid</b>		
1,029,050,000 ordinary shares of £1 each	<b>1,029.0</b>	<b>1,029.0</b>

### 19 Share premium account

	31 March 2011 £m	31 March 2010 £m
At 1 April and 31 March	<b>100.0</b>	<b>100.0</b>

Premium of 25p on issue of 400 million £1 ordinary shares.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 20 Profit and loss account

	Note	31 March 2011 £m	31 March 2010 £m
At the beginning of the year		427.4	480.2
Profit for the year		225.2	331.0
Dividends paid	8	(271.4)	(307.9)
Retained (loss)/profit		(46.2)	23.1
Actuarial loss on pension scheme	25	(1.1)	(105.4)
Movement on deferred tax relating to pension scheme		(3.2)	29.5
<b>At the end of the year</b>		<b>376.9</b>	<b>427.4</b>

### 21 Reconciliation of movements in shareholder's funds

	Note	31 March 2011 £m	31 March 2010 £m
At the beginning of the year		1,556.4	1,609.2
Profit for the year		225.2	331.0
Dividends paid	8	(271.4)	(307.9)
Retained (loss)/profit		(46.2)	23.1
Actuarial loss on pension scheme	25	(1.1)	(105.4)
Movement on deferred tax relating to pension scheme		(3.2)	29.5
		(50.5)	(52.8)
<b>At the end of the year</b>		<b>1,505.9</b>	<b>1,556.4</b>

### 22 Capital commitments

	31 March 2011 £m	31 March 2010 £m
Contracted for but not provided	1,517.2	1,045.3

As part of its ongoing review of contractual arrangements, the Company has negotiated a number of large capital contracts for the circa £5.0bn capital programme in AMP 5.

In addition to these commitments, the Company has long-term capital investment plans to provide for future growth.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 23 Contingencies

There are claims arising in the normal course of business, which are in the process of negotiation.

The Company has set aside amounts considered appropriate for all legal and similar claims as per note 17.

### 24 Operating leases

At 31 March 2011 the Company was committed to making the following annual payments in respect of non-cancellable operating leases:

	31 March 2011		31 March 2010	
	Land and buildings	Other	Land and buildings	Other
	£m	£m	£m	£m
<b>Leases which expire:</b>				
- Within one year	-	-	0.2	0.2
- In the second to fifth year inclusive	0.2	5.1	0.2	4.6
- Over five years	6.2	-	4.7	-
	<b>6.4</b>	<b>5.1</b>	<b>5.1</b>	<b>4.8</b>

See note 16 'Financial instruments' on page 58 for further information regarding obligations under finance leases.

### 25 Pension schemes

Pension arrangements for the majority of the Company's employees are of the defined benefit type, funded through two Group pension schemes; Thames Water Pension Scheme ("TWPS") and Thames Water Mirror Image Pension Scheme ("TWMIPS") (see table below for details of each schemes' respective deficit or surplus), covering employees within the Thames Water Group, whose assets are held separately from those of the Group in independently administered funds. The defined benefit arrangements were closed to new employees from 1 April 2011. From this date, new employees have been offered membership of a defined contribution scheme managed through Standard Life, see note 1, page 43 and note 27, page 67. Contributions to the scheme are charged to the profit and loss account in the period to which they relate.

Contributions to the defined contribution pension scheme in the year were £0.2m (2010: £nil).

The Company's defined benefit pension arrangements are of the group multi-employer scheme nature, such that the Company's pension schemes' assets and liabilities are included with those of other companies in the Group. The Company contributes the vast majority of the contributions into the schemes and any consequence of there being a surplus or a deficit in the schemes is felt by the Company. Accordingly, the directors have decided it is appropriate to recognise the net deficit of the two Group pension schemes within these financial statements.

The service cost of the Company, as included in the profit and loss account, represents the net of the total service cost of the Group schemes and the pension contributions made by the other group companies into the schemes in the financial period.

In addition to the cost of the UK Pension arrangements, the Company operates arrangements under which it augments benefits on retirement. These augmentations are funded by way of additional employer contributions to the schemes. In the year ended 31 March 2011 payments amounted to £2.1m (2010: £3.3m).

The latest full actuarial valuation was undertaken as at December 2007. This valuation has been updated at 31 March 2011 by Mercer Limited ("Mercer"), independent and professionally qualified consulting actuaries, using revised assumptions that are consistent with the requirements of FRS 17 and shown in this note to the accounts.



# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 25 Pension schemes (continued)

The next full actuarial valuation as at 31 December 2010 has commenced on behalf of the pension Trustee's by Hewitt Associates Limited ("Hewitt") (the independent and professionally qualified consulting actuaries to the schemes) and will be completed during 2011.

#### Changes in accounting estimates

As stated in note 1 'Principal accounting policies' on page 38 the Company has recognised a £37.6m credit in the Statement of total recognised gains and losses in respect of the Government's announcement in July 2010 that increases in retirement benefits would be based on CPI rather than RPI for TWMIPS only.

Thames Water Group has taken advice from Mercer in respect of the funding position of the Group pension schemes

#### Net liability by pension schemes before deferred tax

	31 March 2011 £m	31 March 2010 £m
<i>Thames Water Pension Scheme:</i>		
Deficit in scheme	(165.8)	(166.6)
<i>Thames Water Mirror Image Scheme:</i>		
Surplus in scheme	59.6	17.4
Impact of irrecoverable surplus	(21.6)	-
	38.0	17.4
<b>Liability before deferred tax asset</b>	<b>(127.8)</b>	<b>(149.2)</b>

The Company has recognised a surplus in the TWMIPS to the extent that it may possibly be able to recover it by paying a reduced rate of contributions in the future. The recognisable surplus has been calculated in accordance with FRS17 as the present value of the current service cost projected over the future working lifetime of all active members of the scheme, using the assumptions adopted at 31 March 2011

The assumptions used in the valuation of assets and liabilities of the schemes are the same for both schemes, therefore the following tables are for the combined values for both schemes.

#### Reconciliation of funded status to balance sheet:

	31 March 2011 £m	31 March 2010 £m
Fair value of scheme assets	1,403.8	1,317.4
Present value of scheme liabilities	(1,510.0)	(1,466.6)
Deficit in scheme	(106.2)	(149.2)
Impact of irrecoverable surplus	(21.6)	-
Liability recognised on the balance sheet	(127.8)	(149.2)
Deferred tax asset	33.2	41.8
<b>Net pension liability</b>	<b>(94.6)</b>	<b>(107.4)</b>

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 25 Pension schemes (continued)

#### Movement in the present value of scheme liabilities:

	31 March 2011 £m	31 March 2010 £m
Opening present value of scheme liabilities	1,466.6	1,105.4
Current service cost: Thames Water Utilities Limited	25.2	17.6
Current service cost: Other Thames Water Group participating companies	0.2	1.4
Interest cost	81.2	72.7
Contribution by scheme participants	0.3	0.2
Actuarial losses on scheme liabilities	32.1	326.0
Actuarial gain from changes in inflation assumptions	(37.6)	-
Net benefit paid out	(60.1)	(60.0)
Termination pension cost	2.1	3.3
<b>Closing present value of scheme liabilities</b>	<b>1,510.0</b>	<b>1,466.6</b>

#### Movement in fair value of scheme assets:

	31 March 2011 £m	31 March 2010 £m
Opening fair value of scheme assets	1,317.4	1,040.3
Expected return on scheme assets	76.9	57.9
Actuarial gains on scheme assets	14.1	220.6
Contributions by the employer	52.0	53.7
Contributions by Other Thames Water Group participating companies	0.2	1.4
Contribution of section 75 debt payment	0.9	-
Contributions by scheme participants	0.3	0.2
Termination pension costs	2.1	3.3
Net benefits paid out	(60.1)	(60.0)
<b>Closing fair value of scheme assets</b>	<b>1,403.8</b>	<b>1,317.4</b>

#### Expense recognised in the profit and loss account:

	31 March 2011 £m	31 March 2010 £m
Current service cost	25.2	17.6
Interest cost	81.2	72.7
Expected return on scheme assets	(76.9)	(57.9)
<b>Total expense recognised in the profit and loss account</b>	<b>29.5</b>	<b>32.4</b>

#### The expense is recognised in the following line items in the profit and loss account:

	31 March 2011 £m	31 March 2010 £m
Operating costs: staff costs	25.2	17.6
Other finance expense	4.3	14.8
<b>Total expense charged in the profit and loss account</b>	<b>29.5</b>	<b>32.4</b>

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 25 Pension schemes (continued)

#### Analysis of amount recognised in the Statement of total recognised gains and losses:

	31 March 2011 £m	31 March 2010 £m
Actual return less expected return on pension scheme assets	14.1	220.6
Changes in assumptions underlying the present value of scheme liabilities	(32.1)	(326.0)
Changes in inflation assumption – CPI from RPI	37.6	-
Contribution of section 75 debt payment	0.9	-
Adjustment relating to irrecoverable surplus	(21.6)	-
<b>Actuarial loss recognised in the Statement of total recognised gains and losses</b>	<b>(1.1)</b>	<b>(105.4)</b>
Cumulative amount of losses recognised in the Statement of total recognised gains and losses	<b>(310.4)</b>	<b>(309.3)</b>

#### Fair value of scheme assets and return on these assets:

The fair value of the assets held by the pension schemes, the long-term expected rate of return on each class of assets and the average expected long-term rate of return obtained by weighting the individual rates in accordance with the anticipated balance in the schemes' investment portfolio are shown in the following table:

	31 March 2011 Long-term expected rate of return	Value £m	31 March 2010 Long-term expected rate of return	Value £m
Equities	8.4%	473.2	8.5%	435.9
Bonds	5.5%	101.3	5.5%	231.0
Gilts	4.15-4.40%	638.8	4.25-4.5%	530.9
Property	7.4%	90.6	7.5%	81.1
Other assets	4.4%	99.9	4.5%	38.5
Weighted average expected long-term rate of return/total fair value of assets	5.90%	1,403.8	6.1%	1,317.4

The Company employs a building block approach in determining the long-term rate of return on pension plan assets. Historical markets are studied and assets with higher volatility are assumed to generate higher returns consistent with widely accepted capital market principles. The assumed long-term rate of return on each asset class is set out within this note. The overall expected rate of return on assets is then derived by aggregating the expected return for each asset class over the actual asset allocation for the schemes.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 25 Pension schemes (continued)

The main financial assumptions used for FRS 17 purposes are as follows:

	31 March 2011	31 March 2010
Price inflation – RPI	3.5%	3.5%
Price inflation – CPI	3.0%	-
Salary increases - TWPS	4.5%	4.5%
Salary increases - TWMIPS	4.0%	4.5%
Pension increases – RPI	3.5%	3.5%
Pension increases – CPI	3.0%	-
Discount rate for scheme liabilities	5.5%	5.6%

In valuing the liabilities of the pension schemes at 31 March 2011, mortality assumptions have been made as indicated below. These mortality assumptions are based on the recent actual mortality experience of members within the schemes and the assumptions also allow for future improvements to mortality rates

The assumptions are that TWMIPS members and TWPS members who joined the Scheme before 1 January 1995 who retire in 2028 at age 60 will live on average for a further 26 years (2010: 26 years) after retirement if they are male and for a further 28 years (2010: 28 years) after retirement if they are female. TWPS members who joined the Scheme after 1 January 1995 who retire in 2028 at age 60 are assumed to live on average for a further 28 years (2010: 28 years) after retirement if they are male and for a further 29 years (2010: 29 years) after retirement if they are female.

In addition, it is assumed that TWMIPS pensioners and TWPS pensioners who joined the Scheme before 1 January 1995 and are currently aged 60 will live on average for a further 24 years (2010: 24 years) if they are male and a further 26 years (2010: 26 years) if they are female. TWPS pensioners who joined the Scheme after 1 January 1995 and are currently aged 60 are assumed to live on average for a further 26 years (2010: 26 years) if they are male and for a further 28 years (2010: 28 years) if they are female.

#### History of fair value of assets, present value of liabilities, (deficit)/surplus in scheme and experience gains and losses:

	31 March 2011 £m	31 March 2010 £m	31 March 2009 £m	31 March 2008 £m	31 March 2007 £m
Fair value of scheme assets	1,403.8	1,317.4	1,040.3	1,214.8	1,246.4
Present value of scheme liabilities	(1,510.0)	(1,466.6)	(1,105.4)	(1,098.9)	(1,205.9)
<b>(Deficit)/surplus in scheme</b>	<b>(106.2)</b>	<b>(149.2)</b>	<b>(65.1)</b>	<b>115.9</b>	<b>40.5</b>

#### Experience adjustments:

	31 March 2011 £m	31 March 2010 £m	31 March 2009 £m	31 March 2008 £m	31 March 2007 £m
<b>Experience gains/(losses) on scheme assets:</b>					
Amounts	14.1	220.6	(250.4)	(102.7)	7.1
Percentage of scheme assets	1.0%	16.7%	24.1%	8.5%	0.6%
<b>Experience (losses)/gains on scheme liabilities:</b>					
Amounts	-	-	(44.3)	(5.4)	11.9
Percentage of scheme liabilities	-	-	4.0%	0.5%	1.0%
<b>Total amount recognised in the Statement of total gains and losses:</b>					
Amounts	(2.0)	(105.4)	(133.0)	3.9	81.2
Percentage of present value of scheme liabilities	0.1%	7.2%	12.0%	0.4%	6.7%

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 25 Pension schemes (continued)

The Kemble Water Holdings Limited Group expects to contribute approximately £55.5m to the defined benefit schemes in the next financial year.

### 26 Off-balance sheet arrangements

The Company is party to a number of contractual arrangements for the purposes of its principal activities that are not required to be included on its balance sheet. The principal off-balance sheet arrangements are listed below:

- Operating leases (see note 24)
- Outsourcing contracts

In respect of outsourcing contracts, the Company has entered into various arrangements to outsource the provision of certain back-office and operational functions with third party providers. These outsourced arrangements include IT support, Legal Services, metering and capital delivery. These arrangements are on commercial terms and no associated penalty or termination clauses will have a material impact on the financial position of the Group.

### 27 Post-balance sheet events

#### Dividends

On 3 March 2011, the directors approved a fourth interim dividend of £24.4m (2.4p per ordinary share) in respect of the year ended 31 March 2011. This interim dividend was paid to Thames Water Utilities Holdings Limited ("TWUHL") on 11 April 2011, and will be used by TWUHL to settle inter-company interest owing to Thames Water Utilities Limited.

#### Pensions

Following extensive consultation with employees and with the agreement of the pension fund trustees the Company has changed certain provisions in respect of the TWPS for both existing and new employees.

The defined benefit scheme is now closed to new entrants. From 1 April 2011 new employees of the Company will be offered participation in the DCSPS managed through Standard Life.

For existing members of the TWPS, certain provisions have changed that will affect future benefits to its members. Principally, the defined benefit provision from 1 May 2011 will be on a Career Average Revalued Earnings ("CARE") basis and no longer on a Final Salary basis.

# Thames Water Utilities Limited

## Notes to the Financial statements for the year ended 31 March

### 28 Intermediate and ultimate parent company and controlling party

Thames Water Utilities Holdings Limited, a company incorporated in the United Kingdom, is the immediate parent company.

Kemble Water Finance Limited, a company incorporated in the United Kingdom, is an intermediate parent company and the smallest group to consolidate these financial statements.

The directors consider that Kemble Water Holdings Limited, a company incorporated in the United Kingdom, is the ultimate and controlling party and the largest group to consolidate these financial statements.

Copies of the accounts of all of the above companies may be obtained from The Company Secretary's Office, Thames Water Group, Clearwater Court, Vastern Road, Reading, Berkshire, RG1 8DB.

Kemble Water Holdings Limited is owned by a consortium of investors led by Macquarie European Infrastructure Funds LP and Macquarie European Infrastructure Fund II LP ("MEIF 1 & 2"). The directors do not consider there to be an ultimate parent or controlling party. Kemble Water Holdings Limited is the largest group to consolidate these financial statements.

MEIF 1 and 2 are wholesale investment funds in which the investors are largely pension funds and institutional investors. On behalf of these investors, MEIF 1 and 2 make long-term investments in infrastructure and related businesses located across Europe, aiming to deliver sustainable cash yields and moderate capital growth from diversified portfolios of quality infrastructure investments.

MEIF 1 & 2 are managed by Macquarie Infrastructure and Real Assets (Europe) Limited ("MIRAEL"). MIRAEL is a wholly owned member of the Macquarie Group, and is authorised and regulated by the Financial Services Authority. MIRAEL is resourced by executives of the Macquarie Infrastructure and Real Assets division of Macquarie Group.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Explanatory note

The regulatory accounts and required regulatory information on pages 69 to 94 are provided to comply with Condition F of the Instrument of Appointment of Thames Water Utilities Limited as a water and sewerage undertaker under the Water Industry Act 1991.

The regulatory accounts are prepared in accordance with the Regulatory Accounting Guidelines ("RAG") issued by Ofwat.

There are differences between UK Generally Accepted Accounting Practice and the RAG. Where different treatments are specified under each, the RAG take precedence.

A glossary of regulatory terms is shown on pages 103 to 105.

The regulatory financial statements should be read in conjunction with the statutory Annual report and financial statements ("AR&A"). The AR&A include the Chief Executive Officer's business review (pages 4 to 22). In addition the Directors' report (pages 23 to 26) includes a statement as to the disclosure of information to the auditor (page 26), the dividend policy of the Company which also applies to the appointed business (page 23) and information in respect of the Company's charitable donations (page 26).

### Statement of directors' responsibilities for regulatory information

Further to the requirements of Company law, the directors are required to prepare accounting statements which comply with the requirements of Condition F of the Instrument of Appointment of the Company as a water and sewerage undertaker under the Water Industry Act 1991 and Regulatory Accounting Guidelines issued by Ofwat.

This requires the directors to:

- Confirm that, in their opinion, the Company has sufficient financial resources and facilities, management resources and methods of planning and internal control for the next 12 months.
- Confirm that, in their opinion, the Company has sufficient rights and assets to enable a special administrator to manage the affairs, business and property of the Company.
- Confirm that, in their opinion, the Company has contracts with any associate Company with the necessary provisions and requirements concerning the standard of service to be supplied to ensure compliance with the Company's obligations as a water and sewerage undertaker.
- Report to Ofwat changes in the Company's activities, which may be material in relation to the Company's ability to finance its regulated activities.
- Undertake transactions entered into by the appointed business, with or for the benefit of associated companies or other businesses or activities of the appointed business, at arm's length.
- Keep proper accounting records, which comply with Condition F.

These responsibilities are additional to those already set out in the statutory financial statements.

### Ring fencing

In the opinion of the directors, the Company was in compliance with paragraph 3.1 of Condition K of the Instrument of Appointment at the end of the financial year. This relates to the availability of rights and assets in the event of a special administration order.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Regulatory historical cost profit and loss account for the year ended 31 March

	2011			2010		
	Appointed business £m	Non-Appointed business £m	Total £m	Appointed business £m	Non-Appointed business £m	Total £m
<b>Turnover (Note 2, page 87)</b>	<b>1,600.0</b>	<b>23.1</b>	<b>1,623.1</b>	1,593.1	30.7	1,623.8
Operating costs	(752.9)	(9.1)	(762.0)	(712.3)	(10.9)	(723.2)
Historical cost depreciation *	(259.9)	(1.0)	(260.9)	(229.2)	(0.3)	(229.5)
Operating income	10.9	-	10.9	37.9	-	37.9
<b>Operating profit</b>	<b>598.1</b>	<b>13.0</b>	<b>611.1</b>	689.5	19.5	709.0
Other expense	(4.3)	-	(4.3)	(14.8)	-	(14.8)
Net interest payable	(398.1)	(0.2)	(398.3)	(240.4)	(0.2)	(240.6)
<b>Profit on ordinary activities before taxation</b>	<b>195.7</b>	<b>12.8</b>	<b>208.5</b>	434.3	19.3	453.6
Taxation:						
- Current tax	3.2	(3.7)	(0.5)	(42.1)	(5.4)	(47.5)
- Deferred tax	17.2	-	17.2	(75.1)	-	(75.1)
	20.4	(3.7)	16.7	(117.2)	(5.4)	(122.6)
<b>Profit for the year</b>	<b>216.1</b>	<b>9.1</b>	<b>225.2</b>	317.1	13.9	331.0
Dividend	(262.3)	(9.1)	(271.4)	(281.2)	(26.7)	(307.9)
<b>Retained (loss)/profit for the year</b>	<b>(46.2)</b>	<b>-</b>	<b>(46.2)</b>	35.9	(12.8)	23.1

\* The historical cost depreciation has been analysed separately in order to comply with the presentational requirements of RAG 3.06

### Statement of total recognised gains and losses (historical cost accounting) for the appointed business for the year ended 31 March

	31 March 2011	31 March 2010
	£m	£m
Profit for the year	216.1	317.1
Actuarial loss on pension schemes	(1.1)	(105.4)
Deferred tax (charge)/relief relating to actuarial loss	(3.2)	29.5
<b>Total recognised gains in the year</b>	<b>211.8</b>	<b>241.2</b>



# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Regulatory historical cost balance sheet at 31 March

	Appointed business £m	2011 Non- Appointed business £m	Total £m	Appointed business £m	2010 Non- Appointed business £m	Total £m
<b>Fixed assets</b>						
Tangible assets	8,154.1	8.1	8,162.2	7,532.5	8.9	7,541.4
Investments - other	0.1	-	0.1	0.1	-	0.1
<b>Total fixed assets</b>	<b>8,154.2</b>	<b>8.1</b>	<b>8,162.3</b>	<b>7,532.6</b>	<b>8.9</b>	<b>7,541.5</b>
<b>Current assets</b>						
Stocks	8.2	-	8.2	7.7	-	7.7
Debtors: amounts falling due within one year	621.9	-	621.9	599.1	3.9	603.0
Debtors: amounts falling due after more than one year	1,865.0	-	1,865.0	1,180.0	-	1,180.0
	2,486.9	-	2,486.9	1,779.1	3.9	1,783.0
Cash at bank and in hand	3.6	-	3.6	5.9	-	5.9
Short term deposits	775.8	-	775.8	573.2	-	573.2
<b>Total current assets</b>	<b>3,274.5</b>	<b>-</b>	<b>3,274.5</b>	<b>2,365.9</b>	<b>3.9</b>	<b>2,369.8</b>
<b>Creditors: amounts falling due within one year:</b>						
Creditors	(986.0)	(8.1)	(994.1)	(776.9)	(12.8)	(789.7)
Borrowings	(15.5)	-	(15.5)	(553.0)	-	(553.0)
Infrastructure renewals accrual	(17.0)	-	(17.0)	(9.0)	-	(9.0)
<b>Total creditors</b>	<b>(1,018.5)</b>	<b>(8.1)</b>	<b>(1,026.6)</b>	<b>(1,338.9)</b>	<b>(12.8)</b>	<b>(1,351.7)</b>
<b>Net current assets/(liabilities)</b>	<b>2,256.0</b>	<b>(8.1)</b>	<b>2,247.9</b>	<b>1,027.0</b>	<b>(8.9)</b>	<b>1,018.1</b>
<b>Total assets less current liabilities</b>	<b>10,410.2</b>	<b>-</b>	<b>10,410.2</b>	<b>8,559.6</b>	<b>-</b>	<b>8,559.6</b>
<b>Creditors: amounts falling due after more than one year:</b>						
Borrowings	(7,559.7)	-	(7,559.7)	(5,575.5)	-	(5,575.5)
Other creditors	(52.7)	-	(52.7)	(77.3)	-	(77.3)
<b>Total creditors</b>	<b>(7,612.4)</b>	<b>-</b>	<b>(7,612.4)</b>	<b>(5,652.8)</b>	<b>-</b>	<b>(5,652.8)</b>
<b>Provisions for liabilities and charges:</b>						
Deferred tax provision	(972.9)	-	(972.9)	(995.5)	-	(995.5)
Deferred income – grants and contributions	(143.0)	-	(143.0)	(144.7)	-	(144.7)
Other provisions	(81.4)	-	(81.4)	(102.8)	-	(102.8)
Post employment liabilities	(94.6)	-	(94.6)	(107.4)	-	(107.4)
<b>Net assets employed</b>	<b>1,505.9</b>	<b>-</b>	<b>1,505.9</b>	<b>1,556.4</b>	<b>-</b>	<b>1,556.4</b>
<b>Capital and reserves</b>						
Called-up share capital	1,029.0	-	1,029.0	1,029.0	-	1,029.0
Share premium	100.0	-	100.0	100.0	-	100.0
Profit and loss account	376.9	-	376.9	427.4	-	427.4
<b>Capital and reserves</b>	<b>1,505.9</b>	<b>-</b>	<b>1,505.9</b>	<b>1,556.4</b>	<b>-</b>	<b>1,556.4</b>

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Historical cost reconciliation between statutory and regulatory accounts at 31 March

	2011 Statutory UK GAAP £m	Regulatory RAG 3 £m	Explanation
<b>Profit and loss account</b>			
Operating profit	600.2	611.1	The difference of £10.9m is due to the statutory accounts profit on sale of assets is shown below operating result. Ofwat accounting guidelines state that this should be classified within operating costs as 'operating income' for regulatory accounts.
Profit before taxation	208.5	208.5	Profit before taxation is unaffected by this re-classification.
<b>Balance sheet</b>			
<u>Fixed assets</u>			
Tangible fixed assets (net book value)	8,145.2	8,162.2	The difference of £17.0m is due to the infrastructure renewals (accrual) (2010: £9m accrual) as this is excluded from the fixed assets net book value in the regulatory accounts. This is in line with RAG 3.06 as FRS 15 is not applied for infrastructure renewals accounting for regulatory accounting purposes. For more detail see page 80.
<u>Creditors: amounts falling due within one year</u>			
Infrastructure renewals accrual	-	(17.0)	The difference of £17.0m reflects the reclassification of infrastructure renewals accrual described above.
<u>Short-term and long-term creditors</u>			
Deferred income – grants and contributions:	(143.0)	-	Deferred grants and contributions of £143.0m (2010: £144.7m) within the statutory accounts are analysed between creditors: amounts falling due within one year (£6.7m) and creditors: amounts falling due after more than one year (£136.3m). This is in contrast to the regulatory accounts, which shows total deferred grants and contributions within provisions for liabilities and charges.
Provision for liabilities and charges	-	(143.0)	As above.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Additional information required by the licence

#### Basis of preparation

In accordance with Condition F of the Instrument of Appointment, these regulatory financial statements have been prepared to show separately in respect of the appointed business, non-appointed business and total business, a profit and loss account and balance sheet prepared on a historical cost basis.

In accordance with the requirements of FRS 18, the directors review the Company's accounting policies to ensure that they remain the most appropriate to its particular circumstances for the purpose of giving a true and fair view.

The financial statements have been prepared in accordance with the historical cost convention and, except for the classification of profit on the sale of fixed assets as explained in note (a) below, the treatment of infrastructure renewals expenditure as explained in note (b) below and the treatment of certain capital contributions as explained in note (c) below, have been prepared in accordance with the Companies Act 2006. The departures from applicable UK Accounting Standards are necessary to comply with regulatory reporting requirements laid down by the Water Services Regulation Authority ("Ofwat").

#### Changes to accounting policies

The same accounting policies as those used for the year ended 31 March 2010 have been applied in these financial statements.

#### (a) Profit on sale of fixed assets

Profit and loss on sale of fixed assets has been included within operating profit, as operating income, in accordance with RAG 3. This represents a departure from FRS 3 as adopted in the Company's 31 March 2011 statutory financial statements in which profit and loss on sale of fixed assets is shown after operating profit.

#### (b) Infrastructure renewals expenditure

Infrastructure renewals expenditure ("IRE") has been accounted for in accordance with RAG 3 in these financial statements and is consistent with the reporting of IRE in the Company's regulatory historical cost financial statements for the year ended 31 March 2010. Accordingly, IRE net of depreciation has been included within creditors.

This treatment of reporting IRE net of depreciation within creditors in the regulatory historical cost financial statements for the year ended 31 March 2011 represents a departure from the accounting policy adopted in the Company's 31 March 2011 statutory financial statements for infrastructure renewals expenditure and renewals accounting per FRS 15, which requires this amount to be included within fixed assets.

Reconciliation to the tangible fixed assets shown in the statutory financial statements with the regulatory historical cost financial statements is shown on page 80.

#### (c) Capital contributions

Capital contributions received in respect of infrastructure assets have been deducted from the cost of fixed assets. This is not in accordance with Schedule 4 to the Companies Act 2006, which requires fixed assets to be stated at their purchase price without deduction of contributions, with the latter accounted for as deferred income. This departure from the requirement of the Act is, in the opinion of the directors, necessary for the financial statements to give a true and fair view because infrastructure assets do not have a determinable finite life. Accordingly, related capital contributions would not be recognised in the profit and loss account.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Basis of preparation (continued)

#### **(d) Allocation of costs**

All direct costs are allocated immediately to the activity to which they relate. Indirect costs and overheads are apportioned on an appropriate basis to reflect the incidence of such costs. Indirect costs include administrative expenses and the provision of common services.

Direct costs attributable to the provision of services other than the Appointed Business are separately allocated and identified as 'Non-Appointed'. Indirect costs, relating to non-appointed activities, are recovered as a fixed percentage of direct costs based upon the analysis of operating costs.

#### **(e) Revenue**

There are no differences between the accounting policy for revenue under the statutory accounts and the policy for the regulatory accounts.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Link between directors' remuneration and standards of regulatory performance

#### Compensation & HR committee

The Company has a Compensation & HR Committee ("Committee") which functions as both a remuneration and a nomination committee. The Committee comprises of four non-executive directors, one of whom is independent, and is chaired by Sir Peter Mason KBE. The other members are Michael Pavia (independent non-executive director), Martin Stanley and Christopher Deacon.

The Committee's responsibilities include, but are not limited to, making recommendations to the Board on the Company's executive remuneration policy and directors' terms of appointment. During the year, the Committee advised the Board of directors and received advice and input from various directors and specialist staff within the Company, including the CEO and the Director of Human Resources (both of whom are invited to attend from time to time). No individuals are involved in the determination of their own remuneration.

To ensure that the Company's remuneration practices are competitive, the Committee has access to detailed external research on market data and trends from experienced specialist remuneration consultants. In August 2009, the Committee appointed PricewaterhouseCoopers to undertake a complete review of the remuneration package, for the executive team.

The Committee considers carefully the blend of remuneration linked to regulatory performance and remuneration linked to other performance measures in order to produce well balanced short-term and long-term incentive plans leading to value creation and a high quality service to customers.

#### Remuneration policy

The Committee bases its decision-making with respect to remuneration policy on a number of underlying principles, which can be summarised as follows:

- Arrangements should attract, retain, motivate and reward high calibre directors and executives.
- Packages should be aligned with the interests of the Company's stakeholders, in particular its shareholders and its customers.
- Packages should be commensurate with those provided by other companies of similar size and complexity, taking into account individual contribution and experience.
- Policy should establish firm links between an executive's performance and remuneration and between the Company's performance and the executive's total remuneration.
- Packages should include a mix of basic salary and performance related incentives. Further detail is included within the bonus section on page 77 which indicates how directors' pay is linked to standards of performance.

The Committee will continue to review arrangements regularly to ensure that they remain effective and appropriate to the Company's circumstances and prospects, and to monitor the level of potential awards.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Link between directors' remuneration and standards of regulatory performance (continued)

#### Remuneration of executive directors

The remuneration arrangements for executive directors comprise the following elements:

- Base salary and benefits.
- Bonuses.
- Long Term Incentive Schemes ("LTIS").
- Post retirement benefits.

Details of each of the above elements are set out on the following pages.

#### Base salaries and benefits

Base salaries for the executive directors have, in recent years, been reviewed annually with any changes taking effect from the commencement of the financial year. For 2011 onwards the effective date will change to 1 July. Base salaries are a fixed sum payable monthly.

As part of the review of the executive remuneration package, the Chief Operating Officer ("COO") and Chief Financial Officer ("CFO") were awarded a pay increase effective from 1 April 2010.

In addition to base salary, bonus and LTIS, in 2011, the COO and CFO received a car allowance, private medical insurance, membership of a defined benefit pension scheme, life assurance and 25 days holiday. The CEO also received a car allowance, private medical insurance, 25 days paid holiday and life assurance but received membership of a defined contribution pension scheme.

All of these benefits were reviewed in 2010 as part of the executive reward review.

None of the base salaries or benefits are linked to business or individual performance.

#### Bonuses

Executive directors are eligible to participate in an annual bonus scheme, which is designed to motivate them to achieve the Company's key operational and strategic objectives.

The amount of any annual incentive award is determined by and at the discretion of the Committee. The Committee, when determining the level of award, take into account the overall performance of the Company and exercise their judgement accordingly. The Kemble Water Holdings Group ("Group") Board believes that this is the most appropriate means of aligning directors' remuneration to performance.

#### Executive directors' annual bonus plan measures 2011

The 2011 annual bonus plan aimed to reward significant improvement in the Group's financial performance. The financial measures used in the annual bonus plan for the executive directors are regulated net capital expenditure, regulated net operating expenditure, Group cash flow and Group Earnings Before Interest Tax Depreciation and Amortisation ("EBITDA") targets. These targets were selected as being the most critical for the organisation during 2011.

In addition, there is a personal performance element of the bonus which is based on the performance of the executives against their key business objectives. There is a financial underpin on the personal element of the 2011 bonus whereby no payment is made against the personal element of the annual bonus unless the Group cash flow before funding business plan target is achieved.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Link between directors' remuneration and standards of regulatory performance (continued)

Any payment, under this scheme, will be made in July 2011 following Board approval of the audited accounts.

The bonus is paid on the basis of performance against financial measures and personal objectives. As the main focus of the Group is now on the regulatory business a percentage of the bonus relating to financial measures is in relation to regulatory performance.

The total bonus awarded to the executive directors was £874,688 for services to the Company. In addition, the executive directors were awarded £278,438 for services to other companies within the Group.

The level of bonus potential, which was dependent on regulatory measures, was as follows:

	Bonus related to regulatory measures
Martin Baggs	£179,297
Mark Braithwaite	£126,563
Stephen Shine	£126,563

### Executive directors' annual bonus plan measures 2012

The 2012 annual bonus plan will mirror the 2011 plan. The gateway on the personal element of the bonus will continue to be a Group cash flow before funding target.

### Long Term Incentive Schemes ("LTIS")

As an element of the retention strategy, and to incentivise long term, sustained performance, the Company's executive directors and senior management team, are from time to time invited to participate in an LTIS.

#### LTIS 2008

An LTIS commenced in 2008, in which the COO and CFO participate. The plan period runs from 1 April 2008 to 31 March 2011 and payment will be made in July 2011 following Board approval of the audited accounts. The plan is based on four cumulative financial measures, being Group EBITDA, Group cash flow, distributions and Group capital expenditure. These measures were selected as being critical for the Group's value creation.

The measures have been reviewed annually to make any amendments required to take into account business acquisitions, capital restructuring, long-term debt draw-downs and any refinancing of the Company (including fees paid for any refinancing).

Payment will be made in full if all four measures have been achieved over each of the three financial years which form the performance period. No payment will be made under the plan if one or more measures have not been achieved.

The amount accrued in the year for participating directors for services to the Company was £133,334. In addition a further £33,334 was awarded to participating directors for services to the Group. None of the targets is linked specifically to regulatory performance.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Link between directors' remuneration and standards of regulatory performance (continued)

#### LTIS 2009

An LTIS covering the period 1 April 2009 to 31 March 2012 was introduced in 2010, in which the COO and CFO participate. Any payment under the scheme will be made in July 2012 following Board approval of the audited accounts. The plan is based on the Company's performance against the following measures between 1 April 2010 and 31 March 2012:-

Measurement Area		Overall Weighting
Financial Performance	Delivering on core financials over the period 1 April 2009 to 31 March 2012	40%
Sustainability	Delivering on measures that ensure a sustainable future and success beyond AMP5	40%
Regulatory and Customer	Improving the Company's scores under Ofwat's core measures	20%

The performance measures will be reviewed annually taking in to account relevant economic factors.

The table below details the LTIS accrued to each participating director during the year for services to the Company. In addition a further £43,200 has been accrued for participating directors for services to the Group.

The LTIS accrued all relates to regulatory performance.

	Amount accrued
Mark Braithwaite	£86,400
Stephen Shine	£86,400

#### LTIS 2010

A new five year LTIS was introduced in 2010 for the executive directors and senior managers in key strategic positions across the Company. The plan period runs from 1 April 2010 to 31 March 2015. The plan focuses on the key objectives, which are critical to the Company's business plan as follows:

Measurement Area		Overall Weighting
Financial Performance	Delivering on core financials over AMP5	40%
Sustainability	Delivering on measures that ensure a sustainable future and success beyond AMP5	40%
Regulatory and Customer	Improving the Company's scores under Ofwat's core measures	20%

The performance measures will be reviewed annually taking in to account relevant economic factors.

The table below details the LTIS accrued to each participating director during the year for services to the Company. In addition a further £204,450 has been accrued for participating directors for services to the Group.

The LTIS accrued all relates to regulatory performance.

	Amount accrued
Martin Baggs	£479,400
Stephen Shine	£338,400

Payments under the plan will start in 2013 and will continue until 2017.



# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Link between directors' remuneration and standards of regulatory performance (continued)

#### Service contracts

Reflecting current market practice, the executive directors do not hold service contracts that provide for a notice period longer than one year. It is not the Committee's intention to recommend the appointment of any new executive directors with contracts that provide for a longer notice period.

The Committee endorses the principle of mitigation of loss on early termination of a service contract and generally seeks to achieve that objective where possible and appropriate. In the event that the Company wished to terminate an executive director's contract other than in circumstances where either the Company is entitled to summarily dismiss an executive director, it would need to give up to 12 months' notice or make a payment in lieu of salary and benefits.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Reconciliation of tangible fixed assets shown in the statutory financial statements and their regulatory financial equivalents:

	Other assets £m	Infra- structure assets £m	Total £m
<b>Cost</b>			
At 31 March 2011 as per statutory accounts (FRS 15)	8,121.3	4,649.6	12,770.9
Infrastructure renewals expenditure capitalised in previous years	-	(932.6)	(932.6)
Infrastructure renewals expenditure capitalised in the year	-	(124.4)	(124.4)
Disposals in prior years	-	0.9	0.9
<b>Cost at 31 March 2011 per regulatory accounts (RAG 3)</b>	<b>8,121.3</b>	<b>3,593.5</b>	<b>11,714.8</b>
<b>Capital contributions</b>			
Contributions at 31 March 2011 as per statutory accounts (FRS 15)	-	631.2	631.2
Contributions at 31 March 2011 as per regulatory accounts (RAG 3)	-	<b>631.2</b>	<b>631.2</b>
<b>Depreciation</b>			
At 31 March 2011 as per statutory accounts (FRS 15)	2,921.4	1,073.1	3,994.5
Infrastructure renewals charge in previous years	-	(941.6)	(941.6)
Infrastructure renewals charge in the year	-	(132.4)	(132.4)
Disposals in prior years	-	0.9	0.9
<b>Depreciation at 31 March 2011 per regulatory accounts (RAG 3)</b>	<b>2,921.4</b>	<b>-</b>	<b>2,921.4</b>
<b>Net book value</b>			
At 31 March 2011 as per statutory accounts (FRS 15)	5,199.9	2,945.3	8,145.2
Adjustment for infrastructure renewals accounting (see below)	-	17.0	17.0
<b>At 31 March 2011 per regulatory accounts (RAG 3)</b>	<b>5,199.9</b>	<b>2,962.3</b>	<b>8,162.2</b>
<b>Adjustment for infrastructure renewals accounting:</b>		<b>Infrastructure assets £m</b>	
<b>RAG 3 net infrastructure renewals reclassification:</b>			
Infrastructure renewals accrual at 31 March 2010			(9.0)
Infrastructure renewals expenditure capitalised in the year			124.4
Infrastructure renewals charge in the year			(132.4)
<b>Infrastructure renewals accrual at 31 March 2011</b>			<b>(17.0)</b>

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Regulatory current cost profit and loss account for the appointed business for the year ended 31 March

	Note	31 March 2011 £m	31 March 2010 £m
<b>Turnover</b>	2	<b>1,600.0</b>	1,593.1
Current cost operating costs	3	<b>(1,100.8)</b>	(1,044.3)
Operating income	2	<b>(1.5)</b>	37.6
Working capital adjustment	2	<b>13.0</b>	1.2
<b>Current cost operating profit</b>		<b>510.7</b>	587.6
Net interest		<b>(402.4)</b>	(255.2)
Financing adjustment		<b>119.2</b>	11.0
<b>Current cost profit on ordinary activities before taxation</b>		<b>227.5</b>	343.4
Taxation:			
- Current tax		<b>3.2</b>	(42.1)
- Deferred tax		<b>17.2</b>	(75.1)
<b>Current cost profit attributable to shareholder's</b>		<b>247.9</b>	226.2
Dividends		<b>(262.3)</b>	(281.2)
<b>Current cost loss retained</b>		<b>(14.4)</b>	(55.0)

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Regulatory current cost balance sheet for the appointed business at 31 March

	Note	31 March 2011 £m	31 March 2010 £m
<b>Fixed assets</b>			
Tangible assets	4c	71,775.3	51,240.5
Third party contributions since 31 March 1990		(1,008.5)	(934.9)
		<b>70,766.8</b>	<b>50,305.6</b>
Working capital	5	(418.9)	(262.5)
Cash		3.6	5.9
Short term deposits		775.8	573.2
Infrastructure renewals accrual		(17.0)	(9.0)
<b>Net operating assets</b>		<b>71,110.3</b>	<b>50,613.2</b>
<b>Non operating assets and liabilities</b>			
Borrowings		(15.5)	(553.0)
Non-trade debtors		171.8	157.9
Non-trade creditors due within one year		(121.1)	(78.5)
Investment – loan to group company		1,865.0	1,180.0
Investments – other		0.1	0.1
Corporation tax receivable		12.3	13.0
<b>Total non operating assets and liabilities</b>		<b>1,912.6</b>	<b>719.5</b>
<b>Creditors: amounts falling due after more than one year</b>			
Borrowings		(7,559.7)	(5,575.5)
Other creditors		(52.7)	(77.3)
<b>Total creditors falling due after more than one year</b>		<b>(7,612.4)</b>	<b>(5,652.8)</b>
<b>Provisions for liabilities and charges</b>			
Deferred tax provision		(972.9)	(995.5)
Post employment liability		(94.6)	(107.4)
Other provisions		(81.4)	(102.8)
<b>Total provisions</b>		<b>(1,148.9)</b>	<b>(1,205.7)</b>
<b>Net assets</b>		<b>64,261.6</b>	<b>44,474.2</b>
<b>Capital and reserves</b>			
Called up share capital		1,029.0	1,029.0
Share premium		100.0	100.0
Profit and loss account		(783.9)	(765.3)
Current cost reserve	6	63,916.5	44,110.5
<b>Total capital and reserves</b>		<b>64,261.6</b>	<b>44,474.2</b>

The notes on pages 84 to 94 form part of these regulatory current cost financial statements.

The regulatory current cost financial statements were approved by the Board of Directors on 9 June 2011.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Regulatory current cost statement of cash flows for the year ended 31 March

	Notes	Appointed business £m	2011 Non- Appointed business £m	Total £m	Appointed business £m	2010 Non- Appointed business £m	Total £m
<b>Net cash inflow from operating activities</b>	(a)	<b>929.9</b>	<b>13.2</b>	<b>943.1</b>	974.2	37.6	1,011.8
<b>Returns on investments and servicing of finance</b>							
Interest received		110.4	-	110.4	200.5	-	200.5
Interest paid		(269.1)	(0.2)	(269.3)	(297.9)	(0.2)	(298.1)
Interest element of finance lease payments		(6.5)	-	(6.5)	(10.5)	-	(10.5)
<b>Net cash outflow from returns on investments and servicing of finance</b>		<b>(165.2)</b>	<b>(0.2)</b>	<b>(165.4)</b>	(107.9)	(0.2)	(108.1)
<b>Taxation paid</b>		<b>(22.3)</b>	<b>(3.7)</b>	<b>(26.0)</b>	(70.6)	(5.4)	(76.0)
<b>Capital expenditure and financial investment</b>							
Gross cost of purchased fixed assets		(793.6)	(0.2)	(793.8)	(719.4)	(5.3)	(724.7)
Infrastructure renewals expenditure		(107.7)	-	(107.7)	(71.3)	-	(71.3)
Receipt of grants and contributions		41.0	-	41.0	43.1	-	43.1
Movement on long term loans to group companies		(685.0)	-	(685.0)	-	-	-
Disposal of fixed assets		11.5	-	11.5	39.9	-	39.9
<b>Net cash outflow from investing activities</b>		<b>(1,533.8)</b>	<b>(0.2)</b>	<b>(1,534.0)</b>	(707.7)	(5.3)	(713.0)
<b>Equity dividends paid</b>		<b>(262.3)</b>	<b>(9.1)</b>	<b>(271.4)</b>	(281.2)	(26.7)	(307.9)
<b>Management of liquid resources</b>							
Net cash inflow from management of liquid resources		(202.6)	-	(202.6)	(251.6)	-	(251.6)
<b>Net cash outflow before financing</b>		<b>(1,256.3)</b>	<b>-</b>	<b>(1,256.3)</b>	(444.8)	-	(444.8)
<b>Financing</b>							
Capital element in finance lease payment		(8.6)	-	(8.6)	(5.4)	-	(5.4)
New loans		1,807.6	-	1,807.6	454.7	-	454.7
Repayment of loans		(545.0)	-	(545.0)	(202.8)	-	(202.8)
<b>Net cash inflow from financing</b>	(b)	<b>1,254.0</b>	<b>-</b>	<b>1,254.0</b>	246.5	-	246.5
<b>Decrease in cash</b>	(b)	<b>(2.3)</b>	<b>-</b>	<b>(2.3)</b>	(198.3)	-	(198.3)

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Notes to regulatory current cost statement of cash flows for the year ended 31 March

#### (a) Reconciliation of current cost operating profit to net cash flow from operating activities for the appointed business

	31 March 2011 £m	31 March 2010 £m
Current cost operating profit	510.7	587.6
Working capital adjustment	(13.0)	(1.2)
Movement in working capital (excluding short term capital creditors)	25.7	11.4
Current cost depreciation (net of deferred income)	341.3	331.8
Current cost (loss)/profit on sale of fixed assets	1.5	(37.6)
Infrastructure renewals charge	132.4	114.0
Difference between pension charge and cash contributions	(26.8)	(36.9)
Other non-cash profit and loss items (including provisions)	(41.9)	5.1
<b>Net cash flow from operating activities</b>	<b>929.9</b>	<b>974.2</b>

#### (b) Reconciliation of net cash flow to movement in net debt for the Appointed business

	Note	31 March 2011 £m	31 March 2010 £m
Decrease in cash in the period		(2.3)	(198.3)
Cash inflow from increase in liquid resources		202.6	251.6
Cash inflow from movement in net debt and financing		(1,254.0)	(246.5)
Increase in net debt resulting from cashflows		(1,053.7)	(193.2)
Non-cash increase in net debt		(192.7)	(39.8)
Total increase in net debt		(1,246.4)	(233.0)
Opening net debt		(5,549.4)	(5,316.4)
<b>Closing net debt</b>	<b>7</b>	<b>(6,795.8)</b>	<b>(5,549.4)</b>

Non-cash increase in net debt comprises amortisation of bond fees and the carrying value accretion by RPI, of a number of RPI index-linked bonds and swaps. This adjustment for RPI index-linked bonds and swaps is in accordance with FRS 4 'Capital instruments'.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Notes to the regulatory current cost financial statements for the year ended 31 March

#### 1 Current cost accounting policies

These financial statements have been prepared in accordance with guidance issued by the Water Services Regulation Authority for modified real term financial statements suitable for regulation in the water industry. They measure profitability on the basis of real financial capital maintenance, in the context of which assets are valued at their current cost value to the business.

These financial statements have been prepared in accordance with applicable RAG. In respect of cost allocations, the Company has continued to allocate costs by cost centre as in previous years rather than on an activity based method, which is the preferred system under RAG 3.

The principal current cost accounting policies used are the same as those adopted in the regulatory historical cost financial statements, except as set out below.

#### Changes to accounting policies

The accounting policies used for the year ended 31 March 2010 have been applied in these financial statements, except as noted below.

The Company undertook a review of its current cost assets in line with Ofwat's Accounting Separation guidance. Accordingly, the Company has reclassified certain assets and their related depreciation between asset types and between water and sewerage services.

The net book values have not been affected by this review.

#### (a) Valuation bases for determining the current cost of fixed assets

##### (i) Review of asset valuations

In accordance with Ofwat's guidelines RD12/07, the Company undertook a review of the modern equivalent asset ("MEA"), values (see page 104) as at 31 March 2009 as one aspect of the 2009 Periodic Review. This involved a comprehensive review of the asset stock at the time, as well as the unit costs underpinning the valuations. In accordance with RD12/07 companies were given the option to report the results of the revaluation in the regulatory accounts either in 2010 or 2011. The Company has therefore applied the results of the revaluation in the regulatory accounts in 2011. Accordingly, MEA net book values have increased by £16,448.5m; see notes 4a, b and c, on pages 90 – 92 and note 6, on page 93.

##### (ii) Tangible fixed assets

The assets have been valued in accordance with RAG 1.04, on an MEA basis. Depreciation is charged over the estimated remaining economic life of the asset. Infrastructure assets are not depreciated.

Additions during the year are taken at their historical cost values. Disposals are stated at the value of the replacement assets.

#### • Land and buildings

Non-specialised operational properties are valued on the basis of estimated open market value for existing use at 31 March 1991, indexed since that date by the movement in the RPI, except for certain properties which have been valued at 31 March 1995 by professionally qualified employees of the Company.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Notes to the regulatory current cost financial statements for the year ended 31 March

#### (a) Valuation bases for determining the current cost of fixed assets (continued)

##### (ii) Tangible fixed assets (continued)

- **Land and buildings (continued)**

Specialised operational properties acquired since 31 March 1990 are valued at the lower of depreciated replacement cost and recoverable amount, restated annually, between periodic reviews of replacement costs, by adjusting for inflation as measured by changes in the RPI.

- **Infrastructure assets**

Mains, sewers, impounding and pumped raw water storage reservoirs, and sludge pipelines are stated at their MEA value, in the manner described above. Due to the nature of these assets, the MEA value is calculated based on the length of sewer or pipe, or the capacity of the asset.

Following the repeal of Section 24 of the Public Health Act 1936 by the Water Act 1989, the Company assumed responsibility for the maintenance and operation of a significant length of additional sewers. The Company has estimated the length of these pipes in order to include their asset values in these accounts. The value is £6,183m (2010: £5,891m) based upon a pipe length of 19,000km (2010: 19,000km). Adjustments may be required to those estimates in future years as more accurate information becomes available.

- **Specialised/non-specialised assets**

Specialised operational assets include those assets, used routinely in operating the business, which are directly attributable to water supply or sewerage services.

Non-specialised assets are those assets used routinely within the business, which cannot be directly attributed to either part of the business.

- **Surplus land**

Surplus land is valued at recoverable amounts less, where appropriate, that part of any proceeds to be passed on to customers under Condition B of the Licence.

##### (iii) Capital contributions

All third party capital contributions received since 31 March 1990 are carried forward as deferred income to the extent that any balance has not been credited to revenue, or deducted from net operating assets in the case of infrastructure assets. The balance carried forward is restated in accordance with the change in the RPI for the year.

#### (b) Real finance capital maintenance adjustments

The following adjustments are made to historical cost profit in order to arrive at profit after the maintenance of financial capital in real terms.

(i) **Depreciation adjustment** - this is the difference between depreciation based on the current cost value of assets in these financial statements and depreciation charged in arriving at historical cost profit.

(ii) **Working capital adjustment** - this is calculated by applying the change in the RPI over the year to the working capital of the Company at the beginning of the year.



# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Notes to the regulatory current cost financial statements for the year ended 31 March

#### (b) Real finance capital maintenance adjustments (continued)

(iii) **Disposal of fixed assets adjustment** - this is the difference between the book values of realised assets in the current cost financial statements and in the historical cost financial statements.

(iv) **Financing adjustment** - this is calculated by applying the change in the RPI over the year to the opening balance of net finance, which comprises all monetary assets and liabilities in the balance sheet apart from those included in working capital, but excluding index rate linked debt and the deferred tax provision.

#### (c) Operating costs

In note 3, direct costs incurred with associated companies are less than 20% of the total operating costs of the business before interest and tax. Therefore the costs have been allocated across the appropriate headings in accordance with RAG 3.

## 2 Analysis of turnover, operating income and working capital adjustment for the appointed business

	Water supply £m	2011 Sewerage services £m	Appointed business £m	Water supply £m	2010 Sewerage services £m	Appointed business £m
<b>Turnover</b>						
Unmeasured	468.0	426.2	894.2	453.0	440.9	893.9
Measured	325.2	295.0	620.2	315.2	296.6	611.8
Trade effluent	-	4.5	4.5	-	6.1	6.1
Large user and special agreement	33.5	23.1	56.6	30.8	25.7	56.5
Rechargeable works	2.1	6.6	8.7	2.9	6.0	8.9
Bulk supplies/inter-company payments	2.9	-	2.9	2.9	0.0	2.9
Third party services (excl. non-potable water)	5.0	6.6	11.6	5.8	6.0	11.8
Other sources	5.4	7.5	12.9	5.6	7.4	13.0
<b>Total turnover</b>	<b>837.1</b>	<b>762.9</b>	<b>1,600.0</b>	<b>810.4</b>	<b>782.7</b>	<b>1,593.1</b>
<b>Operating income</b>						
Current cost profit on disposal fixed assets	(0.8)	(0.7)	(1.5)	33.8	3.8	37.6
<b>Working capital adjustment</b>						
Working capital adjustment	6.8	6.2	13.0	0.6	0.6	1.2

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Notes to the regulatory current cost financial statements for the year ended 31 March (continued)

#### 3(a) Operating costs and associated fixed asset book values (year ended 31 March 2011)

	Water supply			Sewerage services			
	Resource & treatment £m	Distribution £m	Water supply total £m	Sewerage £m	Sewage treatment £m	Sludge treatment & disposal £m	Sewerage service total £m
<b>Direct costs</b>							
Employment costs	10.0	24.6	34.6	10.3	15.6	6.4	32.3
Power	12.8	25.0	37.8	7.4	22.6	3.1	33.1
Hired and contracted services	8.5	58.3	66.8	30.3	24.5	35.9	90.7
Materials and consumables	11.1	0.1	11.2	0.9	8.4	7.7	17.0
Service charges	15.7	-	15.7	2.1	3.4	-	5.5
Bulk supply imports	0.2	-	0.2	-	-	-	-
Other direct costs	(1.2)	6.0	4.8	1.6	1.6	0.6	3.8
Total direct costs	57.1	114.0	171.1	52.6	76.1	53.7	182.4
General & support expenditure	12.4	53.7	66.1	12.6	8.8	6.5	27.9
Total functional expenditure	69.5	167.7	237.2	65.2	84.9	60.2	210.3
<b>Business activities</b>							
Customer services			32.1				33.5
Scientific services			4.2				1.3
Other business activities			1.1				1.1
Business activities sub-total			37.4				35.9
Local authority rates			29.3				34.0
Doubtful debts			20.7				17.6
Exceptional items			-				-
Total opex less third party services			324.6				297.8
Third party services - opex			1.3				3.4
Total operating expenditure			325.9				301.2
<b>Capital maintenance</b>							
Infrastructure renewals charges	2.6	84.3	86.9	45.5	-	-	45.5
Current cost depreciation							
- service activities	110.6	44.7	155.3	38.5	107.2	46.9	192.6
- business activities			0.9				1.1
Amortisation of grants			(1.8)				(6.8)
Total capital maintenance			241.3				232.4
<b>Total operating costs</b>			<b>567.2</b>				<b>533.6</b>
<b>CCA (MEA) values</b>							
Services activities	2,779.9	11,467.7	14,247.6	54,818.8	1,921.0	762.0	57,501.8
Business activities			8.6				17.3
<b>Service totals</b>			<b>14,256.2</b>				<b>57,519.1</b>

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Notes to the regulatory current cost financial statements for the year ended 31 March (continued)

#### 3(b) Operating costs and associated fixed asset book values (year ended 31 March 2010)

	Water supply			Sewerage services			
	Resource & treatment	Distribution	Water supply total	Sewerage	Sewage treatment	Sludge treatment & disposal	Sewerage service total
	£m	£m	£m	£m	£m	£m	£m
<b>Direct costs</b>							
Employment costs	11.0	19.9	30.9	7.6	17.0	6.5	31.1
Power	13.9	28.4	42.3	7.9	23.9	3.1	34.9
Hired and contracted services	5.8	59.6	65.4	29.1	22.4	32.7	84.2
Materials and consumables	7.0	0.2	7.2	0.9	6.1	7.7	14.7
Service charges	14.2	-	14.2	1.0	3.8	-	4.8
Bulk supply imports	0.5	-	0.5	-	-	-	-
Other direct costs	0.8	2.9	3.7	1.0	0.3	0.2	1.5
Total direct costs	53.2	111.0	164.2	47.5	73.5	50.2	171.2
General & support expenditure	12.6	51.3	63.9	11.4	8.2	6.0	25.6
Total functional expenditure	65.8	162.3	228.1	58.9	81.7	56.2	196.8
<b>Business activities</b>							
Customer services			35.9				37.4
Scientific services			4.5				1.3
Other business activities			4.0				4.0
Business activities sub-total			44.4				42.7
Local authority rates			24.7				29.6
Doubtful debts			18.3				16.2
Exceptional items			-				-
Total opex less third party services			315.5				285.3
Third party services - opex			1.4				2.6
Total operating expenditure			316.9				287.9
<b>Capital maintenance</b>							
Infrastructure renewals charges	2.2	69.8	72.0	42.0	-	-	42.0
Current cost depreciation							
- service activities	82.0	61.0	143.0	28.4	113.9	44.8	187.1
- business activities			0.8				0.9
Amortisation of grants			(1.6)				(4.7)
Total capital maintenance			214.2				225.3
<b>Total operating costs</b>			531.1				513.2
<b>CCA (MEA) values</b>							
Services activities	2,729.5	9,291.5	12,021.0	35,572.9	2,596.2	684.0	38,853.1
Business activities			8.4				11.6
<b>Service totals</b>			12,029.4				38,864.7

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Notes to the regulatory current cost financial statements for the year ended 31 March (continued)

#### 4 (a) Current Cost Analysis of Fixed Assets by Asset Type as at 31 March 2011

##### Water Services

	Specialised operational assets £m	Non- specialised operational properties £m	Infrastructure assets £m	Other tangible assets £m	Total £m
<b>Gross replacement cost</b>					
At 1 April 2010	4,294.3	56.4	9,729.9	199.0	14,279.6
Reclassification *	20.3	0.5	-	(21.3)	(0.5)
At 1 April 2010 - Restated	4,314.6	56.9	9,729.9	177.7	14,279.1
AMP adjustment**	230.6	2.9	1,580.5	(172.3)	1,641.7
Reclassification adjustment	2.3	-	(40.4)	-	(38.1)
RPI adjustment	243.1	3.2	602.6	0.3	849.2
Disposals	(97.1)	(1.2)	*** (80.2)	(8.6)	(187.1)
Additions	140.0	2.0	78.5	23.8	244.3
At 31 March 2011	<b>4,833.5</b>	<b>63.8</b>	<b>11,870.9</b>	<b>20.9</b>	<b>16,789.1</b>
<b>Depreciation</b>					
At 1 April 2010	1,978.1	26.0	-	163.9	2,168.0
Reclassification *	10.2	0.3	-	(10.6)	(0.1)
At 1 April 2010 - Restated	1,988.3	26.3	-	153.3	2,167.9
AMP adjustment**	328.3	4.2	-	(150.1)	182.4
Reclassification adjustment	0.5	-	-	-	0.5
RPI adjustment	123.9	1.6	-	0.2	125.7
Disposals	(97.1)	(1.2)	-	(1.5)	(99.8)
Charge for year	153.3	2.0	-	0.9	156.2
At 31 March 2011	<b>2,497.2</b>	<b>32.9</b>	<b>-</b>	<b>2.8</b>	<b>2,532.9</b>
<b>Net book value</b>					
At 31 March 2011	<b>2,336.3</b>	<b>30.9</b>	<b>11,870.9</b>	<b>18.1</b>	<b>14,256.2</b>
At 31 March 2010	2,316.2	30.4	9,729.9	35.1	12,111.6
Reclassification *	10.1	0.2	-	(10.7)	(0.4)
At 31 March 2010 - Restated	2,326.3	30.6	9,729.9	24.4	12,111.2

\* Please see "changes to accounting policies" on page 85 for details of these reclassifications.

\*\* Please see "Review of asset valuations" on page 85 for details of the AMP adjustment.

\*\*\* Note: The disposal of £80.2m (2010: £128.4m) of infrastructure assets, shown above, relates to the MEA value of the length of main abandoned in 2010 as a result of the Victorian mains replacement programme. The corresponding entry, shown in note 6 is against the current cost reserve.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Notes to the regulatory current cost financial statements for the year ended 31 March (continued)

#### 4 (b) Current Cost Analysis of Fixed Assets by Asset Type as at 31 March 2011

##### Sewerage Services

	Specialised operational assets £m	Non- specialised operational properties £m	Infrastructure assets £m	Other tangible assets £m	Total £m
<b>Gross replacement cost</b>					
At 1 April 2010	7,140.0	45.3	35,033.0	270.9	42,489.2
Reclassification *	4.1	(0.8)	-	(2.8)	0.5
At 1 April 2010 - Restated	7,144.1	44.5	35,033.0	268.1	42,489.7
AMP adjustment**	297.9	2.2	16,007.7	(254.9)	16,052.9
Reclassification adjustment	(2.3)	-	40.4	-	38.1
RPI adjustment	397.8	2.5	2,731.1	0.7	3,132.1
Disposals	(168.3)	(1.1)	-	(6.0)	(175.4)
Additions	496.2	3.8	156.8	9.2	666.0
At 31 March 2011	<b>8,165.4</b>	<b>51.9</b>	<b>53,969.0</b>	<b>17.1</b>	<b>62,203.4</b>
<b>Depreciation</b>					
At 1 April 2010	3,093.3	29.1	-	237.9	3,360.3
Reclassification *	(3.1)	0.2	-	3.0	0.1
At 1 April 2010 - Restated	3,090.2	29.3	-	240.9	3,360.4
AMP adjustment**	1,288.4	13.3	-	(238.0)	1,063.7
Reclassification adjustment	(0.5)	-	-	-	(0.5)
RPI adjustment	234.1	2.3	-	0.1	236.5
Disposals	(167.7)	(1.6)	-	(0.2)	(169.5)
Charge for year	190.8	1.8	-	1.1	193.7
At 31 March 2011	<b>4,635.3</b>	<b>45.1</b>	<b>-</b>	<b>3.9</b>	<b>4,684.3</b>
<b>Net book value</b>					
At 31 March 2011	<b>3,530.1</b>	<b>6.8</b>	<b>53,969.0</b>	<b>13.2</b>	<b>57,519.1</b>
At 31 March 2010	4,046.7	16.2	35,033.0	33.0	39,128.9
Reclassification *	7.2	(1.0)	-	(5.8)	0.4
At 31 March 2010 - Restated	4,053.9	15.2	35,033.0	27.2	39,129.3

\* Please see "changes to accounting policies" on page 85 for details of these reclassifications.

\*\* Please see "Review of asset valuations" on page 85 for details of the AMP adjustment.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Notes to the regulatory current cost financial statements for the year ended 31 March (continued)

#### 4 (c) Current Cost Analysis of Fixed Assets by Asset Type at 31 March 2011

##### Total

	Specialised operational assets £m	Non- specialised operational properties £m	Infrastructure assets £m	Other tangible assets £m	Total £m
<b>Gross replacement cost</b>					
At 1 April 2010	11,434.3	101.7	44,762.9	469.9	56,768.8
Reclassification *	24.4	(0.3)	-	(24.1)	-
At 1 April 2010 - Restated	11,458.7	101.4	44,762.9	445.8	56,768.8
AMP adjustment **	528.5	5.1	17,588.2	(427.2)	17,694.6
RPI adjustment	640.9	5.7	3,333.7	1.0	3,981.3
Disposals	(265.4)	(2.3)	*** (80.2)	(14.6)	(362.5)
Additions	636.2	5.8	235.3	33.0	910.3
At 31 March 2011	<b>12,998.9</b>	<b>115.7</b>	<b>65,839.9</b>	<b>38.0</b>	<b>78,992.5</b>
<b>Depreciation</b>					
At 1 April 2010	5,071.4	55.1	-	401.8	5,528.3
Reclassification *	7.1	0.5	-	(7.6)	-
At 1 April 2010 - Restated	5,078.5	55.6	-	394.2	5,528.3
AMP adjustment **	1,616.7	17.5	-	(388.1)	1,246.1
RPI adjustment	358.0	3.9	-	0.3	362.2
Disposals	(264.8)	(2.8)	-	(1.7)	(269.3)
Charge for year	344.1	3.8	-	2.0	349.9
At 31 March 2011	<b>7,132.5</b>	<b>78.0</b>	<b>-</b>	<b>6.7</b>	<b>7,217.2</b>
<b>Net book value</b>					
At 31 March 2011	<b>5,866.4</b>	<b>37.7</b>	<b>65,839.9</b>	<b>31.3</b>	<b>71,775.3</b>
At 1 April 2010	6,362.9	46.6	44,762.9	68.1	51,240.5
Reclassification *	17.3	(0.8)	-	(16.5)	-
At 1 April 2010 - Restated	6,380.2	45.8	44,762.9	51.6	51,240.5

\* Please see "changes to accounting policies" on page 85 for details of these reclassifications.

\*\* Please see "Review of asset valuations" on page 85 for details of the AMP adjustment..

\*\*\* Please see the note to table 4a in respect of the infrastructure assets disposal value.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Notes to the regulatory current cost financial statements for the year ended 31 March (continued)

#### 5 Current cost working capital

	31 March 2011 £m	31 March 2010 £m
Stocks	8.2	7.7
Trade debtors:		
- Measured household	78.7	68.3
- Unmeasured household	121.1	115.5
- Measured non-household	46.0	44.1
- Unmeasured non-household	1.9	1.7
- Other	19.9	12.9
Measured income accrual	136.1	141.4
Prepayments and other debtors	34.1	44.3
Trade creditors	(254.4)	(247.1)
Deferred income – customer advance receipts	(86.4)	(88.7)
Capital creditors	(332.3)	(201.6)
Accruals and other creditors	(191.8)	(161.0)
<b>Total working capital</b>	<b>(418.9)</b>	<b>(262.5)</b>

#### 6 Movement on current cost reserve

	2011 £m	2010 £m
Balance at 1 April	44,110.5	42,095.5
RPI adjustments:		
- Fixed assets	3,619.1	2,188.0
- Working capital	(13.0)	(1.2)
- Financing	(119.2)	(11.0)
- Grant and third party contributions	(49.2)	(32.4)
- Mains replacement adjustment (see note 4a)	(80.2)	(128.4)
- AMP adjustment *	16,448.5	-
<b>Balance at 31 March</b>	<b>63,916.5</b>	<b>44,110.5</b>

\* Please see “Review of asset valuations” on page 85 for details of the AMP adjustment.

# Thames Water Utilities Limited

## Regulatory accounts and required regulatory information

### Notes to the regulatory current cost financial statements for the year ended 31 March (continued)

#### 7 Net debt analysis

March 2011:

	Interest rate risk profile			
	Fixed rate £m	Floating rate £m	Index linked £m	Total £m
<b>Maturity profile</b>				
Less than one year	(7.7)	(7.8)	-	(15.5)
Between one and two years	(295.4)	(231.1)	-	(526.5)
Between two and five years	(258.6)	(134.6)	-	(393.2)
Between five and twenty years	(1,051.1)	(172.4)	(318.2)	(1,541.7)
In more than twenty years	(2,817.3)	100.0	(2,381.0)	(5,098.3)
<b>Total borrowings</b>	(4,430.1)	(445.9)	(2,699.2)	(7,575.2)
Cash	3.6	-	-	3.6
Short term deposits	775.8	-	-	775.8
<b>Net debt</b>	<b>(3,650.7)</b>	<b>(445.9)</b>	<b>(2,699.2)</b>	<b>(6,795.8)</b>

March 2010:

	Interest rate risk profile			
	Fixed rate £m	Floating rate £m	Index linked £m	Total £m
Maturity profile				
Less than one year	(345.6)	(207.4)	-	(553.0)
Between one and two years	(4.8)	(8.5)	-	(13.3)
Between two and five years	(359.1)	(349.3)	-	(708.4)
Between five and twenty years	(1,366.8)	(182.4)	(516.0)	(2,065.2)
In more than twenty years	(933.5)	-	(1,855.1)	(2,788.6)
Total borrowings	(3,009.8)	(747.6)	(2,371.1)	(6,128.5)
Cash	5.9	-	-	5.9
Short term deposits	573.2	-	-	573.2
Net debt	(2,430.7)	(747.6)	(2,371.1)	(5,549.4)

All values in the above tables are post cross currency rate swaps, interest rate swaps and index-linked swaps.



# Thames Water Utilities Limited

## Supplementary regulatory information for the year ended 31 March

### Rolling five-year summary

Regulatory current cost profit and loss account for the Appointed business for the year ended 31 March 2011 with corresponding amounts for prior periods (at 2011 prices)

	2011 £m	2010 £m	2009 £m	2008 * £m	2007 * £m
<b>Turnover</b>	<b>1,600.0</b>	1,671.9	1,620.5	1,579.0	1,566.9
Current cost operating costs	(1,100.8)	(1,096.0)	(1,096.1)	(1,109.5)	(1,210.9)
Operating income	(1.5)	39.5	8.2	27.0	8.5
Working capital adjustment	13.0	1.3	8.9	8.5	7.2
<b>Current cost operating profit</b>	<b>510.7</b>	616.7	541.5	505.0	371.7
Net interest	(402.4)	(267.8)	(188.6)	(186.2)	(191.6)
Financing adjustment	119.2	11.5	56.4	104.1	139.5
<b>Current cost profit on ordinary activities before taxation</b>	<b>227.5</b>	360.4	409.3	422.9	319.6
Taxation:					
- Current tax	3.2	(44.2)	(25.1)	(117.5)	(59.2)
- Deferred tax	17.2	(78.8)	(98.9)	77.1	(26.3)
<b>Current cost profit on ordinary activities after taxation</b>	<b>247.9</b>	237.4	285.3	382.5	234.1
Dividends	(262.3)	(295.1)	(226.8)	(105.7)	(594.3)
<b>Current cost (loss)/profit retained</b>	<b>(14.4)</b>	(57.7)	58.5	276.8	(360.2)

Corresponding amounts have been stated at current year prices using movements in the average RPI.

\* Current cost operating costs in 2008 and 2007 (restated) include the reclassification of active leakage costs from capital to operating costs and the treatment of income from energy generation and the national grid reserve, which is now included in current cost operating cost for the appointed business.

# Thames Water Utilities Limited

## Supplementary regulatory information for the year ended 31 March

### Rolling five-year summary

Regulatory current cost balance sheet for the appointed business at 31 March 2011 with corresponding amounts for prior periods (at 2011 prices)

	2011 £m	2010 £m	2009 £m	2008 * £m	2007 * £m
<b>Fixed assets</b>					
Tangible assets **	71,775.3	53,980.2	53,705.9	53,323.9	53,060.9
Third party contributions since 31 March 1990	(1,008.5)	(984.9)	(959.8)	(940.4)	(899.5)
	<b>70,766.8</b>	52,995.3	52,746.1	52,383.5	52,161.4
Working capital	(418.9)	(276.5)	(283.2)	(309.5)	(232.9)
Cash	3.6	6.2	224.7	72.1	101.7
Short term deposits	775.8	603.8	353.9	17.1	127.9
Infrastructure renewals (accruals) / prepayment	(17.0)	(9.5)	37.1	40.2	(37.1)
<b>Net operating assets</b>	<b>71,110.3</b>	53,319.3	53,078.6	52,203.4	52,121.0
<b>Non operating assets and liabilities</b>					
Borrowings	(15.5)	(582.6)	(395.0)	(401.5)	(24.1)
Non-trade debtors	171.8	166.3	234.2	100.6	83.7
Non-trade creditors due within one year	(121.1)	(82.6)	(127.5)	(114.7)	(99.0)
Investment – loan to group company	1,865.0	1,243.1	1,298.3	1,341.5	-
Investments – other	0.1	0.1	0.1	0.1	0.1
Corporation tax receivable/(payable)	12.3	13.7	13.1	(8.4)	-
<b>Total non operating assets and liabilities</b>	<b>1,912.6</b>	758.0	1,023.2	917.6	(39.3)
<b>Creditors: amounts falling due after more than one year</b>					
Borrowings	(7,559.7)	(5,873.6)	(6,033.3)	(4,890.7)	(3,886.4)
Other creditors	(52.7)	(81.4)	(40.2)	(27.2)	-
Total creditors falling due after more than one year	<b>(7,612.4)</b>	(5,955.0)	(6,073.5)	(4,917.9)	(3,886.4)
<b>Provisions for liabilities and charges</b>					
Deferred tax provision	(972.9)	(1,048.8)	(1,019.2)	(922.3)	(1,042.6)
Post employment (liability)/asset	(94.6)	(113.1)	(51.6)	28.6	12.6
Other provisions	(81.4)	(108.3)	(94.2)	(86.3)	(80.3)
Total provisions	<b>(1,148.9)</b>	(1,270.2)	(1,165.0)	(980.0)	(1,110.3)
<b>Net assets</b>	<b>64,261.6</b>	46,852.1	46,863.3	47,223.2	47,085.0
<b>Capital and reserves</b>					
Called up share capital	1,029.0	1,084.0	1,132.2	1,128.0	1,170.5
Share premium	100.0	105.4	110.0	109.6	113.8
Profit and loss account	(783.9)	(806.2)	(697.9)	(651.1)	(968.9)
Current cost reserve	63,916.5	46,468.9	46,319.0	46,636.7	46,769.6
<b>Total capital and reserves</b>	<b>64,261.6</b>	46,852.1	46,863.3	47,223.2	47,085.0

Corresponding amounts have been stated at current year prices using movements in the year-end RPI.

\* Current cost operating costs in 2008 and 2007 include the reclassification of insurance liabilities from non-trade creditors to other provisions.

\*\* The tangible fixed asset values for 2011 include an AMP adjustment of £16,448.5m; see "Review of asset valuations" on page 85 for details of the AMP adjustment.

# Thames Water Utilities Limited

## Supplementary regulatory information for the year ended 31 March

### Regulatory Capital Value (RCV)

	2011 £m
Opening RCV (March 2010 prices)	7,721
Price review opening adjustments (March 2010 prices)	182
Indexation to year end (March 2011 prices)	423
Opening RCV at year end prices	8,326
Capital expenditure (excluding infrastructure renewals expenditure)	960
Infrastructure renewals expenditure	142
Grants and contributions	(19)
Depreciation	(372)
Infrastructure renewals charge	(141)
Out performance of past regulatory assumptions	(47)
<b>Closing RCV (March 2011)</b>	<b>8,849</b>
<b>Average RCV (2010/2011 year average prices)</b>	<b>8,366</b>

The figures quoted reflect those used by Ofwat at the 2009 Periodic Review to set prices for 2010/2011, as confirmed by Ofwat in their RCV update on 26 April 2011. The opening balance includes adjustments from the 2009 Price Review as published by Ofwat in RD04/10. All costs have been indexed to March 2011 prices (RPI index) except for the average RCV, which is shown at year average prices (RPI index) in accordance with Ofwat's convention.

Differences between the figures shown above and actual costs/income will not affect price limits in the current period. Capital efficiencies will be taken into account in the calculation at the next price review through operation of the Capital Incentive Scheme.

### RAG 5 Intra-group trade

During the year there were no contracts in excess of 0.5% (£8.0m) of the Company's turnover with any subsidiary of the Thames Water group of companies.

To the best of the directors' knowledge, all appropriate transactions with associated companies have been disclosed.

# Thames Water Utilities Limited

## Supplementary regulatory information for the year ended 31 March

### RAG 5 Directors' interests information

Listed below are details of directorships held by Thames Water Utilities Limited directors at 31 March 2011 in associated companies that have traded with the regulated business during the year.

#### Directorships held in Associated Companies

The following directors held directorships in Thames Water Limited and Thames Water Utilities Holdings Limited:

Director	Appointment	Resignation
Sir Peter Mason KBE – Chairman		
L F Abaira		1 January 2011
E Beckley		
R Blomfield-Smith		
C R Deacon		
G I W Parsons	10 June 2010	
K Roseke		1 January 2011
A F C DeP Santos	1 January 2011	
D J Shah OBE		
M S W Stanley		
R Verrion	1 January 2011	

The following directors have formally appointed alternate directors to represent them when they are unavailable. These alternate directors also held alternate directorships in Thames Water Limited and Thames Water Utilities Holdings Limited:

director			alternate director		
Name	Appointment	Resignation	Name	Appointment	Resignation
L F Abaira		1 January 2011	D Mora		1 January 2011
E Beckley			G I W Parsons	7 June 2010	4 August 2010
			S M L Leong	4 August 2010	11 February 2011
			G I W Parsons	22 March 2011	
R Blomfield-Smith			K Boesenberg		
C R Deacon			R D Israel		
G I W Parsons	10 June 2010		S M L Leong	22 July 2010	11 February 2011
K Roseke		1 January 2011	S Kolenc		1 January 2011
A F C DeP Santos	1 January 2011		M C Guerreiro	1 January 2011	
D J Shah OBE			R Verrion		1 January 2011
			L Webb	1 January 2011	
R Verrion	1 January 2011		S Kolenc	1 January 2011	

Thames Water Utilities Limited conducts its appointed business so as to ensure arm's length trading and avoidance of cross-subsidy in the spirit of Condition F of the Instrument of Appointment.

No directorships are held by Thames Water Utilities Limited directors in circumstances, which, might, in practice, result in conflicts of interest in intra-group trading relationships.

# Thames Water Utilities Limited

## Supplementary regulatory information for the year ended 31 March

### Directors' Certificate under Condition F6A of the Company's Appointment

This is to certify that at their meeting on 9 June 2011 the directors of Thames Water Utilities Limited ("the Appointee") resolved as follows:

- That, in the opinion of the directors', the Appointee will have available to it sufficient financial resources and facilities to enable it to carry out, for at least the next 12 months, the Regulated Activities (including the investment programme necessary to fulfil the Appointee's obligations under the Appointment(s)).
- That, in the opinion of the directors, the Appointee will, for at least the next 12 months, have available to it:
  - (a) Management resources.
  - (b) Systems of planning and internal control.

Which are sufficient to enable it to carry out those functions as required by sub-paragraph 6A.1(1).

- That, in the opinion of the directors, all contracts entered into with any associated company include all necessary provisions and requirements concerning the standard of service to be supplied to the Appointee, to ensure that it is able to meet all its obligations as a water and a sewerage undertaker.

The main factors the directors have taken into account in issuing the Directors' Certificate under condition F6A of the Company's appointment are:

- That the processes and systems of internal control operated as expected.
- That the Appointee operated as if it were substantially the Appointee's sole business and that the Appointee were a separate public limited company.
- That financial resources and facilities are adequate to enable the Appointee to meet its regulatory obligations.
- The net worth of the Company and the strength of the Company's key performance indicators as shown on page 6 of the Chief Executive Officer's Business review.
- The strong investment grade ratings as shown on page 8 of the Chief Executive Officer's Business review.
- Borrowing facilities, which include significant undrawn bank facilities.
- The outcome of the 2009 regulatory price review for the five year period to 31 March 2015 and its impact on the appointee's business plans.



**M Braithwaite**  
Chief Financial Officer  
9 June 2011





## **Independent Auditors' report to the Water Services Regulation Authority and the Directors of Thames Water Utilities Limited**

We have audited the Regulatory Accounts of Thames Water Utilities Limited ("the Company") for the year ended 31 March 2011 on pages 69 to 98 which comprise:

- The regulatory historical cost accounting statements, comprising the regulatory historical cost profit and loss account, the regulatory historical cost balance sheet, the regulatory historical cost statement of total recognised gains and losses and the historical cost reconciliation between statutory and regulatory accounts; and
- The regulatory current cost accounting statements for the appointed business, comprising the current cost profit and loss account, the current cost balance sheet, the current cost cash flow statement and the related notes to the current cost financial statements, including the statement of accounting policies.

These Regulatory Accounts have been prepared in accordance with the basis of preparation and accounting policies set out in the Statement of Accounting Policies.

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 Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water and sewerage undertaker under the Water Industry Act 1991. 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 WSRA, 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 27, the directors are responsible for the preparation of the Regulatory Accounts 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 Accounts in accordance with International Standards on Auditing (UK and Ireland), except as stated in the 'Scope of the audit of the Regulatory Accounts' 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.

### **Scope of the audit of the Regulatory Accounts**

An audit involves obtaining evidence about the amounts and disclosures in the Regulatory Accounts sufficient to give reasonable assurance that the Regulatory Accounts 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 Regulatory Accounts. In addition, we read all the financial and non-financial information in the regulatory accounts to identify material inconsistencies with the audited Regulatory Accounts. If we become aware of any apparent misstatements or inconsistencies, we consider the implications for our report.

# **Independent Auditors' report to the Water Services Regulation Authority and the Directors of Thames Water Utilities Limited (continued)**

## **Opinion on Regulatory Accounts**

In our opinion, the Regulatory Accounts:

- Fairly present in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA and the accounting policies set out on pages 73 to 74 and 85 to 87, the state of the Company's affairs at 31 March 2011 on an historical cost and current cost basis, and its historical cost and current cost profit and its current cost cash flow for the year then ended.
- Have been properly prepared in accordance with Condition F, the Regulatory Accounting Guidelines and the accounting policies.

## **Emphasis of matter regarding basis of preparation**

Without modifying our opinion, we draw attention to the fact that the Regulatory Accounts have been prepared in accordance with Condition F of the Appointment and the Regulatory Accounting Guidelines, the accounting policies set out in the statement of accounting policies and, in the case of the regulatory historical cost accounting statements, under the historical cost convention.

The Regulatory Accounts are separate from the statutory financial statements of the Company and have not been prepared under the basis of United Kingdom Generally Accepted Accounting Practice ('UK GAAP'). 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. Furthermore, the regulatory historical cost accounting statements on pages 70 and 71 have been drawn up in accordance with Regulatory Accounting Guideline 3.06, in that infrastructure renewals accounting as applied in previous years should continue to be applied and accordingly, that the relevant sections of Financial Reporting Standards 12 and 15 be disapplied. The effect of this departure from Generally Accepted Accounting Practice and a reconciliation of the balance sheet drawn up on this basis to the balance sheet drawn up under the Companies Act 2006 is given on page 72.

## **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 as required by paragraph 3 of Condition F.
- The Regulatory Accounts are in agreement with the accounting records and returns retained for the purpose of preparing the Regulatory Accounts.

## **Other matters**

The nature, form and content of Regulatory Accounts are 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 Regulatory Accounts is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2011 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.



## **Independent Auditors' report to the Water Services Regulation Authority and the Directors of Thames Water Utilities Limited (continued)**

### **Other matters**

The nature, form and content of Regulatory Accounts are 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 Regulatory Accounts is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2011 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.



KPMG Audit Plc  
Chartered Accountants  
London  
9 June 2011

### **Notes:**

1. The maintenance and integrity of the Company's web site is the responsibility of the directors and the maintenance and integrity of the Regulator's web site 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 Regulatory Accounts since they were initially presented on the web sites.

2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements and Regulatory Accounts may differ from legislation in other jurisdictions



# Thames Water Utilities Limited

## Glossary of regulatory terms

**AMP adjustment** – The revision in the real value of fixed assets arising periodically from improved information in the five-year Asset Management Plan process.

**Appointed Business** – The appointed business comprises the regulated activities of the Company which are activities necessary in order for a company to fulfil the function and duties of a water and sewerage undertaker under the Water Industry Act 1991.

**Arm's-length trading** – Trading in which the Company treats the other party, usually an associate company on the same basis as an external party.

**Asset Management Plan (AMP)** – A plan agreed with Ofwat on a five-yearly basis for the management of water and wastewater assets. The plan runs for a five-year period. AMP4 covers the investment period April 2005 to March 2010 AMP5 covers the investment period April 2010 to March 2015.

**Associate company** – Condition A of the Licence defines an associate company to be any group or related company. Condition F of the Licence requires all transactions between the Company and its associated companies to be disclosed subject to specified materiality considerations.

**Capital Incentive Scheme ("CIS")** – This will be the new capital expenditure incentive mechanism introduced by Ofwat to take effect in AMP 5. Under this mechanism Ofwat sets a baseline capital expenditure plan, which they believe companies should be able to deliver. Companies are rewarded or penalised during the AMP 5 for submitting a business plan, which is lower or higher than the baseline respectively. Companies will then be further rewarded or penalised at the start of AMP 6 for underspending or overspending against that business plan.

CIS will apply to capital expenditure only, not to operational expenditure and will not apply to large projects such as the Lee Tunnel.

**Final determination** – The conclusion of discussions on the scale and content of the asset management plan for the forthcoming five-year AMP period. It is accompanied by a determination of the allowable K factor for the forthcoming AMP.

**Financing adjustment** – The impact of RPI on the real value of net finance for the business.

**K factor** – The annual increase, set by Ofwat, in charges that companies in the water industry can make. The amount by which a company can increase (or must decrease) its charges is controlled by the price limit formula  $RPI + \text{or} - 'K' + 'U'$ . RPI is expressed as the percentage increase in the Retail Price Index in the year to November before the charging year. 'K' is a number determined by Ofwat for each company, usually at a price review, for each year to reflect what it needs above or below inflation in order to finance the provision of services to customers and 'U' is the amount of 'K' not taken up by a company in previous years.

**Licence** – The Instrument of Appointment dated August 1989 under Section 11 and 14 of the Water Act 1989 (as in effect on 1 August 1989) under which the Secretary of State for the Environment appointed Thames Water Utilities Limited as a water and sewerage undertaker under the Act for the areas described in the Instrument of Appointment, as modified or amended from time to time.

# Thames Water Utilities Limited

## Glossary of regulatory terms (continued)

**Modern Equivalent Asset (MEA)** – The cost of an asset of equivalent productive capability to satisfy the remaining service potential of the asset being valued if the asset would be worth replacing, or the recoverable amount if it would not. The gross MEA value is what it would cost to replace an old asset with a technically up to date new asset with the same service capability allowing for any difference both in the quality of output and in operating costs. The net MEA value is the depreciated value taking into account the remaining service potential of an old asset compared with a new asset, and is stated gross of third-party contributions.

**Monitoring plan** – The document required by Ofwat after the outcome of a price review that sets out annual targets for delivery against the Final Determination. The June Return is the annual submission to Ofwat that allows the Regulator to track progress against the Monitoring Plan.

**Non-appointed business** – The non-appointed business activities of the Company are activities for which the Company as a water and sewerage undertaker is not a monopoly supplier (for example, the sale of laboratory services to an external organisation) or involves the optional use of an asset owned by the Company (for example, the use of underground assets for cable television).

**Ofwat** – The name used to refer to the Water Services Regulation Authority (WSRA). The WSRA acts as the economic Regulator of the water industry.

**Overall Performance Assessment (“OPA”)** – This is the measure used by Ofwat to assess the performance of water only and water and sewerage companies within the industry. Ofwat uses a scoring system, up to a maximum of 437.5 whereby it compares companies performance across the industry.

**Periodic Review (PR)** – The price determination process undertaken by Ofwat every five years. Each water and sewerage undertaker submits an Asset Management Plan covering the five-year period for which Ofwat will determine prices (the K factor – see above).

**Price limit** – The name given to the combination of the RPI and K.

**Regulatory Accounting Guidelines (RAG)** – The accounting guidelines for regulatory accounts issued, and amended from time to time, by Ofwat.

**Retail Price Index (RPI)** – The RPI is compiled and published monthly by the Office for National Statistics. RPI is an average measure of change in the prices of goods and services bought for the purpose of consumption by the vast majority of households in the United Kingdom.

**Regulatory Capital Value (RCV)** – The capital base used in setting price limits. The value of the appointed business that earns a return on investment. It represents the initial market value (200-day average), including debt at privatisation, plus subsequent net new capital expenditure including new obligations imposed since 1989. The capital value is calculated using the Ofwat methodology (i.e. after current cost depreciation and infrastructure renewals accrual).

# Thames Water Utilities Limited

## Glossary of regulatory terms (continued)

**Third-party contributions since 1989/90** – Grants and third-party contributions received in respect of infrastructure assets and any deferred income relating to grants and third-party contributions for non-infrastructure assets.

**Working capital** – The aggregate of stocks, trade debtors and trade creditors, if material.

**Working capital adjustment** – The impact of RPI on the real value of working capital to the business.

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