2366619

Sustainable growth

Annual Report and Accounts 2011

Contents

Introduction

Severn Trent is a FTSE 100 company. Our core business is water. We provide and treat water and waste water in the UK and internationally through our two complementary businesses – Severn Trent Water and Severn Trent Services.

Find out more at our corporate website
www.severntrent.com

Severn Trent Water website
www.stwater.co.uk

Severn Trent Services website
www.severntrentservices.com

Severn Trent Plc
Severn Trent Plc is a public limited company listed on the London Stock Exchange and registered in England and Wales with company number 2366619 This is the Annual Report and Accounts for the year ended 31 March 2011

More information on Severn Trent Plc can be found on our website at www severntrent com

2011 Severn Trent group highlights

- **Good start to AMP5 regulatory period – realising benefits of efficiency improvement programmes and planned outputs delivered**
- **Severn Trent Water opex below level allowed in Final Determination**
- **Self-generated renewables now supplying 22% of Severn Trent Water's power requirements**
- **Real price reduction in first year of new AMP has rebased underlying profitability**
- **Full year dividend 65.09 pence per share. Dividend for 2011/12 to grow by 7.7%* to 70.10p**
- **On track to deliver further efficiencies – ambition remains to outperform over AMP5**

* November 2010 RPI of 4 7%, + 3%

Group turnover £m

£1,711.3m

2011

2010 £1 703 9m

Group profit* £m

£288.6m

2011

2010 £338 4m

*before tax gains/losses on financial instruments and exceptional items

Group profit before tax £m

£253.0m

2011

2010 £334 4m

Dividend pence per share

65.09p

2011

2010 72 32p

Earnings per share* pence

105.6p

2011

2010 122 8p

before exceptional items gains/losses on financial instruments and deferred tax

■ Severn Trent Plc

■ FTSE 100 Index

This graph illustrates the value at 31 March 2011 of £100 invested in Severn Trent on 31 March 2006 compared with the value of £100 invested in the FTSE 100 Index. The intermediate points show the value at intervening financial year ends Source Datastream

Group at a glance
Severn Trent Water

Find out more on page 10

Severn Trent Water provides high quality water and sewerage services to over 3.2 million households and businesses in the Midlands and mid-Wales.

Key strengths

- We are committed to the long term sustainable stewardship of the business, the environment, customers and the communities in which we live and work
- Our efficiencies and high standards help us keep our costs low and generate progressive, sustainable returns for our shareholders
- We continually work to improve our performance and deliver cost and operational efficiencies against 18 Key Performance Indicators (KPIs), each of which is aligned to our long term strategy
- Our bills for water and sewerage combined are the lowest on average in England and Wales
- We have one of the lowest reported per capita consumption rates in the UK
- We have a strong management team, a clear business plan and we launched our long term plans in our 25 year Strategic Direction Statement in 2007

Our industry
The water industry in England and Wales invests more than £3 billion a year and employs over 27,000 people There are currently 10 water and sewerage companies in England and Wales

Our sector is facing significant long term challenges The privatisation of the industry just over 20 years ago led to improvements in services to customers, better quality drinking water and higher environmental standards It also attracted new investment Those successes, however, have also had consequences, such as high levels of debt, rising prices for customers and increased carbon emissions Our proposals for changes in our industry are helping us to play a role in shaping the debate We talk more about our position and how other bodies with a stake in our industry are responding on pages 20 and 21

Our business
Severn Trent Water is a regulated business We work within five year price cycles, with the prices we charge our customers set at the beginning of each cycle by our economic regulator, Ofwat These five year cycles are known as Asset Management Plan (AMP) periods We have just reached the end of the first year of AMP5

Our performance
Every June, all water companies submit a detailed annual breakdown of their performance, known as the June Return, to Ofwat Ofwat uses this information to monitor and compare companies' performance

As well as being regulated by Ofwat, our performance is monitored by

- the Drinking Water Inspectorate (DWI), which is responsible for making sure we comply with drinking water quality regulations
- the Environment Agency, which controls water abstraction, river pollution and flooding

We also work with the government (including the Department for Environment, Food and Rural Affairs (DEFRA) and the Welsh Assembly government) and other agencies such as the Consumer Council for Water (CCWater) and Natural England to make sure we meet the highest customer service and environmental standards, while offering our customers the lowest prices

Our vision for the future
Our 25 year Strategic Direction Statement sets out the long term direction and development of our group for the years 2010–35 (see 'Our strategy', page 8) You can also find the full report on our website www stwater co uk/sds

Where we operate in the UK

Our region stretches across the heart of the UK, from the Bristol Channel to the Humber, and from mid-Wales to the East Midlands

Our physical assets include
- **46,000 km** of water mains
- **126** water treatment works
- **54,000 km** of sewers
- **1,026** sewage treatment works

Drinking water supplied per day

1.8bn litres

Waste water collected per day

1.4bn litres

Employees

5,128

As at 31 March 2011

Turnover £m
2010/11 (up 0 3%)

2011	1,389 8
2010	1,385 3

Split of business

Severn Trent Water
Profit* 2010/11

£503.7m

(down 6 9%)

*before exceptional items interest and tax

Group at a glance
Severn Trent Services

Find out more on page 16

Severn Trent Services is one of the world's leading suppliers of water and waste water treatment solutions.
We are known for continual innovation, reliability, quality services and leadership in our chosen markets.

Key strengths

- Our business has a clear strategy for growth, which focuses on the growing global demand for clean water and safe, efficient waste water treatment
- We are known for our quality, reliability and stability
- We provide operating services to an increasing number of utilities, municipalities and commercial customers in targeted countries
- We are a leader in high growth technology markets such as disinfection, filtration, adsorption and marine/offshore waste water treatments
- We have a track record of growth and efficient operations

Our industry
The market for water and waste water products and services is large with substantial prospects for growth in the areas we serve That is because the drivers of the water and waste water business – water scarcity, population growth, climate change and more stringent regulatory requirements – remain strong

Our business
Severn Trent Services provides water and waste water treatment and operating services to utilities, municipalities and commercial customers around the world

We focus on the high growth markets and geographies where our broad line of products and services meet the significant needs of our customers

We have three principal business streams

- **Operating Services** provides contract operating services to manage and maintain water and waste water plants and networks in selected countries worldwide We are a leading provider in the United States and United Kingdom, one of the few integrated water operators in Italy and are building a strong presence in Ireland
- **Water Purification (Products)** is one of the leading global providers of advanced technologies and integrated solutions for water and waste water disinfection, filtration, adsorption and marine/offshore waste water treatment
- **Analytical Services** is a leader in UK environmental water testing services

Our performance
We measure our performance against our Key Strategic Initiatives We discuss how these shape our businesses on page 9

Where we operate
Our activities are focused in four regions – the Americas, Europe, Middle East and North Africa (MENA) and Asia Pacific Operating Services operates in the US, UK, Ireland and Italy Water Purification operates in all four regions and Analytical Services operates in the UK

Number of countries with operating entity

11

Employees

3,056

As at 31 March 2011

Turnover £m
2010/11 (down 0 1%)

2011	336 1
2010	336 5

Severn Trent Services
Profit* 2010/11

£25.7m

(down 10 5%)

*before exceptional items interest and tax

Chairman's statement

At the end of my first financial year as Chairman, I'm pleased to report that we have made a good start to delivering our targets for the new AMP5 regulatory period and are realising the benefits of our efficiency improvement programmes. As expected the price reductions at the start of the five year determination have reduced profitability below prior years' levels but from this base Severn Trent Water has continued to outperform.

For the year, total group turnover was up 0.4% to £1.7 billion. The real price reduction in the first year of the new AMP has rebased underlying profitability with group profit before tax, gains/losses on financial instruments and exceptional items, down 14.7% to £288.6 million, giving adjusted earnings per share, excluding deferred tax, of 105.6p, a 14% decrease on the prior year.

This is a good solid business on track to perform well and deliver total overall benefits for shareholders, customers and the environment.

There remains significant opportunity for growth in both our Services business and in delivering further outperformance in Severn Trent Water.

Andrew Duff, Chairman

I am delighted to find, at Severn Trent, a strong board of executives, very capably led by Tony Wray, that is committed to operational excellence and continuous improvement Momentum within the company is strong and we have the ambition to be recognised as a top performer in our sector I am also grateful to the management team for the wholehearted support that they have given to me in my first year as Chairman

We have a solid track record of financial performance and the board is proposing a final dividend of 39 05p, to be paid on 29 July 2011 This will give a total dividend of 65 09 pence per ordinary share From this new base, we will look to grow the dividend by 3% above RPI each year up to 2014/15

The single largest profit driver was the performance of Severn Trent Water, which continued to outperform with planned operational expenditure below the level of the Final Determination

This improvement in efficiency is a consequence of the group's ongoing change programme, which is resulting in significant business improvement One of the most momentous changes during the year was the move to our new operating centre in Coventry, resulting in not only a change of environment for our people, but a change to new, more efficient and innovative, working practices I've yet to meet a visitor who isn't impressed by this truly modern working environment and the building has created a level of energy and enthusiasm that is infectious

The change programme extends beyond the office to the group's operations and processes and includes significant systems investment Naturally, as with many programmes of this size and scale, it comes with its challenges But we're confident we have embarked upon a course that will allow us to continue to deliver further efficiencies throughout the AMP period

'We have the talent, the innovation, the systems and the resources to continue to achieve profitable and sustainable growth for our group whilst also meeting the needs of our customers and the environment.'

Andrew Duff,
Chairman

Operational performance during the year was impacted by the severe winter weather, placing pressure on our leakage performance During the year the number of unplanned interruptions to customers' water supply increased We have decided to increase the level of investment in our water distribution system in order to build even greater resilience in our infrastructure to cope with severe weather in future years

Severe weather notwithstanding however, we continue to provide some of the highest standards of customer service in the industry, with excellent drinking water quality and a year on year reduction in the number of properties suffering from sewer flooding

I am particularly pleased to see the focus on health and safety within the business The personal safety of employees has always been one of my priorities so I was pleased to find a strong culture and focus on safety in the company Our recent Employee Engagement survey shows that 95% of our people say that health and safety is taken seriously at Severn Trent Water and this is reflected in the Severn Trent Water Lost Time Incident (LTI) performance which remains the best in the sector Safety is one issue but the commitment of our employees is vital to our group's success and so we are continuing to invest in the development and training of our employees and future leaders

During the year, we made good progress in protecting our environment and dealing with waste water whilst continuing to lead the industry in the production of renewable energy Self-generated renewables now supply 22% of Severn Trent Water's power requirements, helping to mitigate our carbon impact

Severn Trent Services had a mixed year with performance falling below expectations Although the business made good progress in reducing its costs and maintains a strong order book, results were affected by project delays in our Middle East and North Africa region and the slowdown in the global economic environment, impacting public funded initiatives Growth and profitability in our Services business remains a priority and we are well placed to make progress on this aim

As I write this statement it seems likely that there will be some regulatory change following the publication of the government's White Paper later this year We intend to continue to play an active role in regulatory reform and play an influential role in the debate about how our industry addresses the challenges ahead of us in order to promote sustainable growth We also want to make sure that any change strikes the right balance between delivering value and security to our customers and reliable returns to our shareholders We must get this right because the investment challenge over future years means that we must be able to compete for capital internationally as the need for infrastructure funding globally becomes more pressing You can read more about our position on page 20 of this report

All of this will undoubtedly bring more challenges but I firmly believe that we have the talent, the innovation, the systems and the resources to continue to achieve profitable and sustainable growth for our group whilst also meeting the needs of our customers and the environment

Chief Executive's review

Our strategy of sustainable growth through a focus on water and waste water operations in the UK and internationally, continues to deliver significant overall value.

In the UK, Severn Trent Water made a good start to the new five year regulatory period, performing broadly in line with expectations.

In a challenging year, I would like to pay tribute to our people, who professionally handled both difficult operational circumstances and significant internal change.

Our Severn Trent Services business started the year strongly, but was affected by the economic slowdown and political and regulatory uncertainty in the second half.

Fundamentally, we remain well placed to deliver our business plan and to continue to play an active role in shaping the future of the UK water industry.

A.P Wray

Tony Wray, Chief Executive

Business Performance Review
Group profit before interest, tax and exceptional items is down 7% due to expected price reductions in the first year of the AMP period for Severn Trent Water and a disappointing second half performance in Severn Trent Services, in challenging market conditions

From the new dividend base of 65 09p we will grow the dividend by 3% above RPI up to 2014/15

Underlying financial performance remains strong and we continued to outperform our regulatory targets

Severn Trent Water
With our focus on operational excellence and continuous improvement, our goal is to keep prices low and deliver the highest customer service and environmental standards

Overall, we achieved these goals in the past year We delivered industry-leading drinking water quality and reduced the number of incidents of sewer flooding, one of the biggest causes of distress to our customers Our customers also benefited from the lowest combined average water and sewerage bills in England and Wales

In these straitened times, we've carried on helping customers who have difficulties paying their bills and as a result we have also been able to reduce bad debt

Environmental performance continues to be strong and we are reinforcing our leading position in renewable energy generation, with 22% of Severn Trent Water's electricity requirements being met by self-generated renewables Some of that was generated by the UK's first commercial scale crops to energy plant, which was opened this year

Leakage was above target as a result of the severe winter weather However, despite significant operational challenges we maintained our leakage at the same level as last year Unplanned interruptions to supply also increased during the year

Steps are in place to improve the resilience of our water distribution network, but I would like to pay tribute to our people who, faced with unprecedented operational challenges, kept customer supplies running over this difficult period

That we are able to work in such a flexible and responsive way is thanks in part to the changes we have made to our internal operations This year we moved to our new operating centre, Severn Trent Centre in Coventry, bringing together under one roof many teams previously dispersed over seven older buildings We have transformed our technology infrastructure and implemented the second phase of SAP which will help us to run our business more effectively

Once again, I would like to use this opportunity to thank our people for the way they have responded to such a significant change in technology and ways of working

Severn Trent Services
The economic environment remained especially challenging for our Severn Trent Services business, which started the year well only to experience a market downturn in the second half

While the underlying market is growing and demand remains strong, projects are being delayed as project financing has been less available and slower to obtain In addition, political uncertainty in the Middle East, a key market for our water purification products, and the moratorium on deep well drilling in the US, led to lower sales of our highly successful electrochlorination product line In the US, in particular, municipal budget shortfalls have limited infrastructure spending on products while driving more project opportunities for outsourcing in our Operating Services units

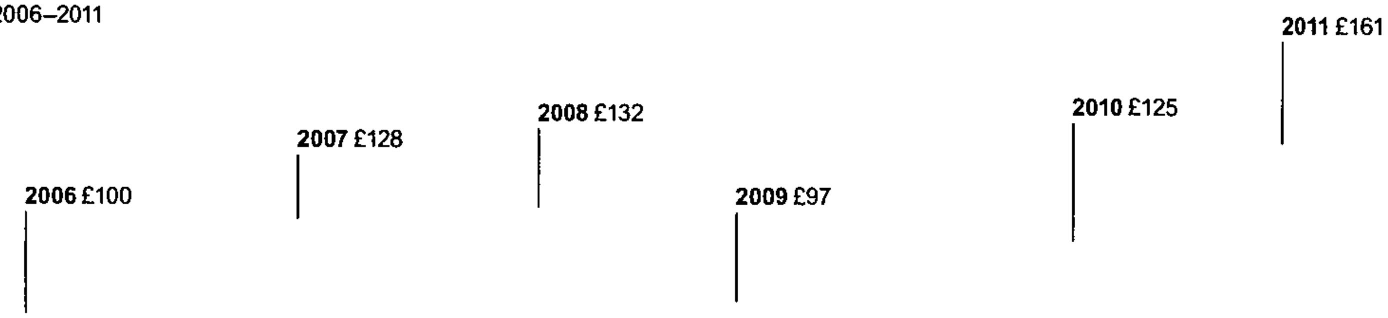
Looking ahead
At Severn Trent Water, with strong underlying performance and the right people, technology and AMP5 contracts in place, we are well placed to achieve our business plan and outperform our regulatory targets

In Severn Trent Services, the prospects for long term growth remain good, but the first half of the coming year is likely to see the same market conditions that prevailed at the end of last year With a good portfolio of business and products, we are confident of returning to profitable and sustainable growth once the public finances start to recover and the political and regulatory uncertainty in key markets subside

In terms of prospects for regulatory and industry change, Severn Trent remains at the forefront of industry thinking and our ideas for a sustainable future for our industry have been widely published and well received

Throughout our operations, our goal continues to be to deliver long term sustainable growth This strategy, underpinned by a clear focus on customers, environmental performance, people and shareholder value will continue

Total shareholder return
2006–2011



Our strategy
Sustainable growth

Sustainable

We need to strike the right balance to maintain a healthy business. We do this by:

Providing high standards of service to our customers, strong environmental performance, a fair return for investors and a great place to work for our people
Running a sustainable business, balancing the needs of all our stakeholders, along with the needs of the environment in which our businesses operate

Making sure our business is efficiently financed, with a flexible and sustainable balance sheet
As well as ensuring we are securely funded we work to manage our balance sheet sensibly and keep our credit ratings stable We keep our refinancing needs under constant review to take advantage of favourable market conditions

Acting responsibly, operating safely and doing the right things
The very nature of our business makes corporate responsibility part and parcel of our everyday business activities What we do affects the environment, local and regional communities, our people and society at large Acting responsibly, operating safely and doing the right thing also play important roles in enhancing our reputation with our stakeholders It therefore makes sense to make ethical and responsible business practices an integral part of our strategy, incorporated into our business planning and risk management

Severn Trent Water

Our vision is to be the best water and waste water company in the UK. We aim to achieve this by providing the highest standards and lowest charges and through great people. We focus on four key areas – customers, environment, people and value.

Customers
Our customers have the lowest, on average, bills in England and Wales But keeping customers satisfied is not just about low charges and value for money We also need to reflect their needs and priorities in our plans, communicate clearly, keep our promises and apologise if things go wrong

Environment
Our operations depend on the environment in which we operate Our activities can have a significant impact and we take our stewardship of the environment very seriously, looking for innovative ways to manage our river catchments, and minimise pollution and our carbon footprint

People
Our drive to work safer, better and faster is the cornerstone of our business transformation initiatives Making sure we have the right processes and systems in place, underpinned by a strong safety culture, is a fundamental part of our drive for operational excellence and continuous improvement

Value
The more efficiently we work, the higher our standards In turn this improves our ability to keep our costs low and generate progressive, sustainable returns which earns the trust of our shareholders

Our key focus

Customers	Environment	People	Value
Delivering quality services at prices customers can afford	Reducing pollution and our carbon footprint	Investing in the right people with the right skills	Making our business attractive to investors

Key Strategic Intentions

Our strategy is based on eight Key Strategic Intentions (KSIs) which reflect what matters to our customers and wider stakeholder groups We measure our performance within each KSI against our 18 Key Performance Indicators (KPIs)

1 Providing a continuous supply of quality water
2 Dealing effectively with waste water
3 Responding to customers' needs
4 Minimising our carbon footprint
5 Having the lowest possible charges
6 Having the right skills to deliver
7 Maintaining investor confidence
8 Promoting an effective regulatory regime

Growth

We create and release value by focusing on water and waste water. We achieve this by:

Growing Severn Trent Water in the UK through investment in our networks and services
We are committed to reaching the highest standards in the industry and to continually improving our performance in every area of our business, from the resilience of our networks to the energy we consume and the way we interact with our customers For that reason the improvement targets we set ourselves are ambitious, and often more challenging than our regulatory requirements

Winning in a changing world – positioning Severn Trent to capitalise on opportunities in a new regulatory framework
Our industry has delivered significant benefits in the two decades since privatisation However, we believe that changes to the regulatory and policy framework are now needed in order to make the industry sustainable Our strategy of continually improving our operational and financial performance, backed by a significant programme of change, puts us in a strong position to prosper from future changes to the way we are regulated

Deploying our Severn Trent Services business into new markets
This business operates at the forefront of the demand for water and waste water services We achieve growth in this business by expanding the scope of our existing markets, entering new high growth markets and investing in innovative technologies

Developing new treatment technologies
Our research and development teams investigate treatment technologies to improve our efficiency and continually reduce our environmental impacts By challenging traditional approaches we are able to introduce groundbreaking solutions that require less capital investment and lower operational costs

Severn Trent Services

We aim to maintain strong operational performance through cost control and revenue growth and by capitalising on the right opportunities for growth in the higher return, unregulated market sectors.

Severn Trent Services is one of the leading water and waste water businesses in the world To achieve our strategy we focus on

- Expanding the scope of our operating services to existing clients around the world
- Continuing the geographic expansion of our products
- Enhancing products and operations to improve our effectiveness and efficiency
- Developing new technologies at the forefront of water and waste water solutions

Operational performance
As a competitive business, it is crucial that we build on our strengths in order to secure new business and maintain high levels of contract renewals in Operating Services For our Water Purification (Products) business this means continuing innovation to develop high-end products taking advantage of market opportunities while staying focused on water We also aim to preserve our operational margins through efficiency gains

We are always looking for ways to improve our standards and operate more efficiently We achieve this through supply chain cost reduction in component sourcing and lower cost locations for engineering and assembly, and by improving our environmental and health and safety performance

Key Strategic Initiatives

Eight Key Strategic Initiatives define our strategy and set out how we intend to achieve our objectives

1 Deliver what customers value
2 Establish long term contracts and strong sales channel relationships
3 Expand our global technology programme
4 Continuously improve quality, health, safety and environmental performance
5 Invest in strategic partnerships to supplement organic growth
6 Optimise processes and organisational capabilities
7 Continue to build a strong, coherent and respected brand
8 Increase employee engagement

Business review Severn Trent Water
Performance

Underlying improvements in operational performance were affected by a challenging business and economic environment, together with the coldest December in 100 years. However, overall progress remains strong with significant business change resulting in the delivery of planned efficiencies.

Our aim is to deliver the highest standards and lowest prices for customers and one of the best standards of drinking water in the UK At an average of £298, Severn Trent Water customers also paid the lowest average combined water and sewerage bill in England and Wales over the last year For those customers struggling to pay, we helped to manage their payments, whilst reducing our own bad debt risk

The harsh December had a significant impact on our operations, particularly on our leakage performance, with a sharp peak in leakages at the height of the freeze/thaw events The severe weather also meant that our capital programme got off to a slower start than we had aimed for

We are particularly pleased with progress in our work to tackle sewer flooding, one of the biggest causes of disruption and distress to our customers We also halved the total number of pollution incidents in the category 1 and 2 bands, with none in the most serious, category 1 classification

Our business also underwent change during the year as we set up to deliver our ambitious AMP5 programme Our streamlined new supply chain is now in place and major improvements in technology and ways of working have been implemented, including the move to a state of the art operational centre in Coventry

Customers

Our customers' combined average water and sewerage bills are the lowest in England and Wales and the quality of the water we provide is amongst the best in the industry We also score well on the process side of dealing with our customers – we aim to deal with customer issues at first point of contact Although we solve problems efficiently, we need to improve the way we engage with our customers Our challenge is to maintain our efficiency whilst making our customers feel more valued

We worked with customer focus groups to redesign our customer bills so they fit our customers' needs.

Our challenge is to keep continually improving how we engage with our customers. We need to maintain our efficiency while making our customers feel more valued.

8.2m
We serve 8 2 million people

82p
Average customer pays just 82 pence per day

£298
Lowest combined average water and sewerage bill in England and Wales at £298

Customer experience
We are committed to providing the best customer experience possible Ofwat's Service Incentive Mechanism (SIM), a new way of measuring the customer experience, will help us keep track of our performance It measures whether our customers feel valued when we interact with them, as well as how well we respond to their telephone and written communications The 2010/11 financial year is our first full year of data We are using the information we gather to put together a Customer Experience programme that covers recruitment, training, our telephone performance and improving every single touch point customers have with Severn Trent

At times, and especially during the harsh winter, our customers found it difficult to contact us as we were inundated with calls from people with frozen domestic pipes This has increased complaints which we are working hard to resolve

A continuous supply of quality water
In 2010 we delivered 99 98% overall mean zonal compliance with DWI drinking water quality regulatory standards However, our unplanned interruptions to supply performance over the year was not at the level we expect Three major events caused significant disruption and regrettably a number of our customers were without water for some time We have a dedicated programme in place to improve performance

Flooding and pollution
We are ahead of our target for reducing the number of properties on the sewer flooding risk register, thanks to investments in our network and our proactive monitoring, which allows us to identify and fix problems before they result in failure We have reduced the number of network failure-related repairs by 15%, resulting in less disruption to customers and reduced flooding and pollution

Managing debt
Our challenge is to reduce bad debt while helping people who genuinely want to pay, but are finding it difficult to meet their payments In 2010 we introduced a new credit management system that helps us target our efforts more efficiently Along with our Relationships team, which works with social housing landlords to track tenants moving in and out of rented accommodation and stay on top of debt in this sector, we reduced bad debt to 2 3% of sales Our region is still feeling the effects of the economic change the country is currently experiencing and for this reason our outlook on debt reduction is cautious

To help people on lower incomes who want to be good payers but have fallen into debt, we are piloting the new Together Tariff, where we match payments made by customers We have contributed £4 5 million to the Severn Trent Trust Fund, helped over 4,800 customers through our WaterSure tariff and signed up 43,549 people to Water Direct

Case study
Transferring sewer ownership

We anticipate the transfer of private drains and sewers (PDAS) will take place in October 2011 At the moment home owners are responsible for everything up to the main sewer, including the connection After the transfer we will own around 37,000km of sewers which are currently privately owned, and be responsible for their repair and maintenance We also expect roughly 4,000 pumping stations to be transferred in stages over the following five years We believe this will benefit some customers in a number of ways such as reducing their liability and repair costs, but will lead to higher bills in general to fund the necessary continued investment Our plans for the transition are well advanced and we have been engaging with regulators and government to make sure we provide customers with an efficient service after the transfer

Customer written complaints per 1,000 properties

5.73 2011 | **4.95** 2010

First time call resolution for billing

90% 2011 | **89%** 2010

Properties at risk of low pressure per 1,000 properties

0.07 2011 | **0.12** 2010

For more information on KPIs see page 123

Business review
Severn Trent Water
Performance (continued)

Environment

Our customers should have confidence that we will take away waste water and treat it to the highest environmental standards before returning it to our region's rivers We also strive to run our operations in a sustainable way and reduce our carbon footprint

During the year we made good progress in protecting our environment and dealing with waste water, whilst continuing to lead the industry in the production of renewable energy However, severe winter weather impacted our leakage performance in what was otherwise a year of improved environmental performance

Dealing with waste water

During the past 12 months we have had a strong focus on continuous improvement which has resulted in us halving the number of serious pollution incidents from eight to four in the year, with no category 1 pollutions We have been working on improved processes for identifying, monitoring and reporting pollution and our self reporting has increased by 11% We are confident that this is helping us to focus on the right things and whilst this has led to an overall increase from 322 to 378 reported pollution incidents, we are confident that this is due to raising our standards of working and improving our understanding, such that in the longer term we will deliver better overall performance

An £8 2 million investment to resolve pollution from our sewers overflowing in rivers and streams will lead to a further significant improvement in river quality in the region

Our sewage treatment works failing consent limit was 1 69% (2010 1 80%) We are working to improve this as part of our Environmental Improvement plan which we put in place this year Our plan, developed alongside Ofwat, supports our aim of raising the standards of our watercourses to benefit local communities and those who use our rivers for recreation

One of our challenges is striking a balance between river water quality and carbon production We invest in plant to eliminate nitrates and pesticides in order to improve water quality in our rivers and comply with the Water Framework Directive (WFD) To reduce the number of new treatment works we need to build, we work in partnership with farmers and industries to encourage them to discharge less effluent and waste into watercourses through the use of Catchment Management Investigations (CMI) Severn Trent is currently engaged in 47 CMIs, more than any other water company We have also developed a joint initiative with the Environment Agency to balance carbon emissions and river ecology

Case study
Improving river water quality

A £9 million project to upgrade our sewerage network and improve the water quality of the River Tame unearthed several hurdles at the feasibility study stage These included contaminated ground, buried concrete structures, the presence of great crested newts and a complex geology with a past history of deep coal mining and high groundwater levels We worked with the Environment Agency and the local authority to secure an agreement to re-use all excavated material on site, delivering a huge reduction in the project's carbon footprint Collaborating with our contractor also enabled us to introduce several innovations, such as specialist covers to the tank, and control of groundwater

KPI	2011	2010
Jobs resolved first time	97.5%	96.5%
Net energy use – gigawatt hours (GWh)	706	714
Leakage – megalitres per day (Ml/d)	497	497
Pollution incidents (cat 1, 2 and 3)	378	322

For more information on KPIs see page 123

Protecting the biodiversity of our region
The scale and scope of our operations puts us in a unique position to protect and often enhance the biodiversity of our region, particularly its aquatic ecosystem There are over 800 Sites of Special Scientific Interest (SSSI) in our region, a number of which are nominated as sites of European importance for the conservation and protection of endangered species We own or partly manage 37 SSSIs and work in partnership with Natural England, Countryside Council for Wales, our tenants and other partners to safeguard the special interest of these sites

Reducing leakage
We experienced the coldest December in 100 years with significant snowfall and a prolonged freeze across our region The graph below shows how leakage increased sharply compared to previous years This caused severe operational difficulties but we kept customers on supply throughout the winter However, two freezes followed by two thaws caused leakage to rise to unprecedented levels We were able to maintain leakage at last year's levels of 497 megalitres per day (Ml/d) However, despite deploying additional resources we were unable to achieve our leakage target of 483 Ml/d as a direct result of the weather We have reduced leakage significantly since the winter and we have plans in place to achieve our targets in 2011/12 Our long term trend on leakage is good and we are confident of hitting our targets in future years

Customers also have a part to play and our water conservation and efficiency programme has resulted in one of the lowest per capita water usages in the UK Severn Trent Water customers use an average of 126 litres per day, compared to the national average of 146 litres

Reducing our carbon footprint
In 2010/11 we met our target of producing 22% of Severn Trent Water's energy requirements from renewables, reinforcing our leading position in the production of renewable electricity from sewage The group also delivered the UK's first commercial scale 'energy crop' power plant, using maize and wheat to generate 15 gigawatt hours (GWh) of electricity per annum, enough to power 4,500 homes The group has recently received permission to build its first wind turbine which will help us achieve the goal of 30% of Severn Trent Water's power requirements being generated from our own renewables by 2014/15

As well as reducing our carbon impact, renewables will also offer protection against rising energy prices, reducing our exposure in volatile energy markets and saving around £28 million over the next five years

In addition to generating our own energy, we also set targets and monitor energy use across every area of our business Our people take every opportunity to reduce energy from turning off lights to reducing unnecessary journeys We continue to invest in trackers and software that routes vehicles to make job scheduling more efficient, leading to reduced mileage and an improvement in productivity

Case study
Saving water and energy

Thanks to the efforts of our customers we continue to lead the industry in water efficiency Nottingham couple Gary and Clare Blissett are a good example by making a few practical changes they virtually halved their water consumption – and energy bills – in a year As Gary explains, "It's about small behavioural changes such as turning off the tap when brushing our teeth, only putting a full load into the washing machine and dishwasher and taking showers instead of baths " They also ordered free water saving devices, such as a ShowerSave device, from Severn Trent Our work with customers, energy companies and schools helps us have the lowest per capita consumption of water in the UK

15 GWh
of electricity from 37,000 tonnes of converted maize sludge

9%
increase in our production of renewable energy

126 litres
Customers used on average just 126 litres of water per day

Business review
Severn Trent Water
Performance (continued)

People
Over the past 12 months we have taken significant steps to transform the way we work, from the environment our people work in to the processes and technologies we use This is a vital part of our strategy to improve our performance and operational efficiency, and the service we provide to our customers Any change on this scale is bound to be challenging but overall our people are embracing the new working arrangements, and once again showed exceptional commitment over a difficult winter period

A new way of working
In October we moved to the Severn Trent Centre in Coventry One of the most energy efficient buildings in Europe, it reflects our ethos of openness, team working, high standards and low charges We also transformed our technology infrastructure Virtual desktops allow our employees to access their PCs and business systems from any desk at a large proportion of our sites It also allows us to form teams dynamically to resolve specific problems For example, during the extreme cold weather the technology allowed our people to rapidly form work groups and share information We are now using these working arrangements as a template to modernise the rest of our sites through our ongoing workplace improvement plan

Severn Trent Centre in Coventry

Improving our technology and business processes
Throughout the year we continued to invest strategically in new technology completing the implementation of our new SAP workforce management systems, refreshing our desktop technology, providing high bandwidth telecoms infrastructure and new data centres The adoption of new, lower running cost technology has increased reliability and performance at a lower operating cost

The new SAP workforce scheduling technology and processes are starting to make our operational teams more productive and our investment in SAP's asset management systems is contributing to improved capital programme efficiencies

Our new systems and technology are fundamentally changing the way we work and so we have invested heavily in training our people to equip them with the right skills to exploit the new technology and systems

Throughout our business, our teams are improving their performance by changing the way they work using our 'Safer Better Faster' approach to continuous improvement With more than two thirds of the organisation now upskilled in the tools and techniques, managers and their teams are equipped to improve their processes to deliver higher standards of performance to our customers in the most cost effective ways they can The approach is now being introduced into our business support areas The success of this programme is due to the involvement and engagement of our people in making the improvements for themselves – taking ownership of their performance, learning new tools and techniques, and working more collaboratively with colleagues in different functions to solve problems

Lost time incidents per 100,000 hours worked

0.37 2011 | **0.36** 2010

For more information on KPIs see page 123

Engaging our people
Although our people went through considerable changes during the year, those changes led to upskilling, simplified processes, and a better workplace and technologies Our employee engagement survey revealed that 74% of employees across the organisation remain positively engaged Positively engaged means employees are committed to the organisation and have the desire to go above and beyond the call of duty to achieve success People support the need for the improvements and changes we are making (86%) and think their colleagues give them the support they need to do their job (87%) A high percentage (88%) are also happy to go the extra mile when required

However, only 33% of employees felt that changes which affected their job had been well implemented In response to this we introduced a module on change management to our line manager development programme

We share the results of the employee engagement survey with our teams and trades union partners in order to find more productive and co-operative ways to work together in the future

A safe and healthy workforce
During the year our health and safety performance, despite remaining at upper quartile and leading the sector, did not improve This is the first time in a number of years that we have not seen a year on year improvement and we are seeking to address the identifying causes to enable the business to attain further progress in this important performance measure Importantly, we have a strong culture of people taking personal responsibility for their own health and safety, and that of others This year 95% of our workforce agreed that health and safety is taken seriously, and 87% said we give them the right support to do their job safely

We have introduced better health surveillance processes as part of improving our employees' wellbeing but recognise that while we have made positive progress, we have more to do in this area

Recruitment and training
Having the right people with the right skills is more important than ever We are working to make sure we have a more diverse workforce, with a particular focus on attracting more female candidates for operational and senior roles In 2010 we continued to provide regular diversity-related training and communications to managers, employees and new joiners and worked to embed the importance of diversity within our business With the help of ACAS we have designed and are implementing diversity training events that will eventually train 500 Water Distribution employees

To develop succession plans, we identify and mentor future leaders through our talent review process which assessed 893 managers and potential leaders this year Current managers have access to our Line Manager Journey which includes a suite of training modules such as change management and coaching for performance We continue to develop the training programme package and add new modules when a need is identified

A concept known as Safety Improvement Teams, set up by our Waste Water Services Team to increase employee engagement around health and safety, won a RoSPA Silver Award in 2010.

Employee motivation

74% 2011 | **74%** 2010

For more information on KPIs see page 123

Business review
Severn Trent Services
Performance

A challenging economic environment and social and political uncertainty impacted negatively on performance, especially in the second half. However, we made good progress in reducing our costs and improving our environment and health and safety performance. We are also investing in specific segments, both in our Products business and Operating Services, to capture growth opportunities and deliver longer term profitability.

The wider social and economic environment remained challenging, particularly in the second half of the year, with delays to financing of capital projects, the Gulf coast deep well drilling moratorium in the US, and political unrest in the Middle East There were a few visible signs of recovery in the majority of our markets post the financial crisis, although a few markets, China for example, were more robust The impact was felt most acutely in our Products business, particularly disinfection products in the US, and in Operating Services the impact was mainly in Europe, particularly Italy

Water Purification (Products)
Industry publications and trade associations reported market contractions in the range of 4% for water equipment Despite the slower than anticipated market recovery, we were able to grow some product lines, mainly in filtration, while disinfection, particularly electrochlorination, was impacted by the moratorium on the Gulf of Mexico deep well drilling The US water business was particularly impacted, with the budget crises experienced by municipal establishments rippling out to the market In the future we expect recovery in this market to be slow and gradual

'Despite the slower than anticipated market recovery, we were able to grow some product lines.'

In Europe, after a slow start, activity picked up towards the end of the year In the UK, more projects were commissioned as water companies settled into the new regulatory period Delays in financing in our other European markets led to a slowdown in product shipments However, while projects were delayed, none were cancelled

With the exception of China, which remained healthy for most of the year, uncertainties around the economy and funding also affected our business in Asia Pacific, although in the final quarter of the year there were some signs of improvement

Case study
Growing business in Spain

Our acquisition of PS Apliclor SA near Barcelona in 2009 has resulted in several new orders in the country, such as a contract to supply Spain's largest electrochlorination plant in Tarragona The plant will improve water management in the region, which supplies 140,000 residents with drinking water This is a good working example of our acquisition strategy to create a European hub from which we can bring new Water Purification business to the rest of the region

New project orders (turnover)

Denitrification plant in China

£1m

Electrochlorination in India

£1.3m

Electrochlorination in Egypt

£2.8m

Filtration blocks in Mexico

£2.8m

South America remains relatively strong with 36% year on year growth and a number of attractive orders, including two orders for filtration blocks in Mexico worth over £2 8 million

In the Middle East and North Africa (MENA) region the global economic slowdown continued to adversely impact our business and several large projects were postponed due to delays in financing During the last quarter the region was also impacted by social and political unrest

Operating Services
Forced to find cost efficiencies, municipal utilities will sometimes look to public private partnerships They need to make real savings from any outsourcing strategy, so our focus is on cost efficiency and continually improving our processes In the US we increased our market position and were one of just two companies to report year on year revenue growth

To support new business we have continued to selectively add people to our business development, new project proposals and technical support service teams We expect to accelerate the investment in these same departments in the coming year to take advantage of the medium term growth potential in the US market

We also developed our presence in Ireland this year – an operate and maintain project in Limerick has been running for almost a year, and we have won and started work on a new contract for a waste water treatment plant in Letterkenny In the rest of Europe, financing delayed some larger design-build-operate projects in the UK and Italy, which negatively impacted performance in the second half, although we continue to develop the project pipeline in both countries

Analytical Services
Our business continued to feel the effects of the UK slowdown, particularly in the commercial sector We have just reached the end of the first full year of our 10 year contract with Yorkshire Water, using our new laboratory in Wakefield During the year our Wakefield laboratory also took on some work from our Bridgend facility, where some testing was temporarily suspended following a DWI audit The facility at Bridgend is fully operational, and with new accreditation following corrective action

Continuous improvement

Operational efficiency
In a more challenging market environment our focus is on being more efficient Our Products division has been moving our production to lower cost regions closer to our markets, rather than shipping them from the UK and US This year we exceeded our target and made supply chain savings of £2 4 million on the previous year

One of the ways we deal with price pressures in our Operating Services business is by offering energy management plans to our US customers At no extra cost we review their energy use This enables our customers to alter their processes and operating procedures and improve efficiency, benefiting both our customers and Severn Trent Services

Operating Services adds £2 1 million through hub and spoke

We operate on a hub and spoke approach, looking for new business in the areas surrounding existing contracts This proved particularly successful in Oklahoma where we expanded our presence in the area by signing three new multi year Operating Services contracts during the year, bringing in over £2 1 million revenue annually

£336.1m
turnover in 2010/11

£0.4m
down on 2009/10

£25.7m
(down 10 5%) profit before interest, tax and exceptional items

Business review
Severn Trent Services
Performance (continued)

Environment
As part of a global water company we understand the need to find innovative ways to reduce our impact on the environment and in turn, those of our clients and customers We achieve this through careful management of our resources and waste water discharges, the way we operate our treatment sites and development of technologies For the third consecutive year, we completed Site Energy Management Plans (SEMPs) for five major plants in our US Operating Services business Our SEMPs evaluate several operating conditions to determine the most energy efficient treatment process Several of our businesses are certified under ISO 14001 2004, the international standard for environmental management systems, which we use to manage and minimise our impacts

Many of our products and services help our customers improve their environmental performance and operate more efficiently In the first year of our public private partnership to operate sewerage and waste water treatment plants for the City of Clinton, Oklahoma, we saved the city approximately £100,000 in operating expenses, improved compliance, got the plants operating more efficiently and made significant reductions in energy usage In Italy we completed a green energy plant to generate electricity from biogas, produced by sewage sludge We use the energy to run the treatment plant and sell any excess to the national energy grid

People, health and safety
To meet the aims of our growth strategy, we need to recruit and develop a talented and motivated workforce and provide them with a safe and rewarding place to work We were therefore delighted that in our employee engagement survey, Severn Trent Services outperformed many other industry and country benchmarks Results of the independently run survey show that the majority of our employees are proud to work for us, and 90% feel we meet the needs of our customers

Given our strategy to embed health and safety in all areas of our business we were particularly pleased that 95% of our employees take personal responsibility for working safely and 90% are aware of their responsibility to protect the environment In January we set up a multi level task team to suggest ways we could continue to improve our health and safety performance, incorporating their recommendations into our health and safety plans for 2011/12

'Our organisation serves more than 38,000 families in Haiti through our household water treatment programmes. Severn Trent Services' donation of water disinfection equipment will improve our capacity to serve each of these families in an ongoing, sustainable way.'

Michael Ritter
Co Founder and CEO of Deep Springs International

90%
of employees feel we meet the needs of our customers

Case study
Assisting in the effort to provide safe drinking water to the residents of Haiti

As part of a humanitarian campaign to enable ordinary citizens to treat their drinking water at the point of consumption, we donated 11 portable electrolytic water disinfection systems to agencies working in Haiti The units, which convert saltwater and energy into liquid sodium hypochlorite, are being used to disinfect drinking water

Ten portable Sanilec® systems and one ClorTec® unit were donated to three humanitarian agencies working in Haiti Operation Blessing International, Deep Springs International (DSI) and St Damien Hospital DSI seeks to alleviate poverty, illness and unemployment through an integrated and sustainable safe water programme Operation Blessing International provides strategic disaster relief, medical aid, hunger relief, clean water and community development around the world, and St Damien Hospital is a free paediatric hospital in Haiti

The equipment allowed DSI to quickly set up bulk distribution of sodium hypochlorite solution in response to the cholera outbreak In addition to the equipment, we provided technical support to optimise production This support allowed DSI to treat over 86 million litres of water

In the UK, Operating Services won two Gold awards from the Royal Society for the Prevention of Accidents (RoSPA)

Sustainability and growth
As a global leader in advanced water and waste water technology, it is vital we develop a strong pipeline of new technologies that meet a specific need in the market It is equally important that our product portfolio meets and anticipates future regulatory standards To that end we have been centralising product development across Severn Trent Services, ensuring that we focus our efforts on developing the right products in the right areas around the world Our recent developments include two groundbreaking new products

- BALPURE® is a ballast water treatment system that received approval from the Marine Environment Protection Committee (MEPC) in October (see case study, right)
- MicroDynamics® microwave ultraviolet technology uses microwave technology in the disinfection of waste water We are the only company selling this kind of patented microwave technology, which is more efficient and leads to longer bulb life

We plan to continue to invest in the development of new products, to meet changing market demands and improve performance

'With a three year lamp life guarantee, the MicroDynamics® system offered the lowest overall operational costs and maintenance requirements of any UV technology we evaluated.'

Jim Newton,
Environmental Programme Manager,
Regional Waste Water Treatment Plant,
Kent County, Delaware

Outlook
The second half of the year saw significant impacts from project delays in Europe, unrest in the Middle East and the impact from the Gulf of Mexico drilling moratorium Although some countries in the Middle East are now moving forward and the moratorium has lifted, shipments are only slowly returning to normal Financing will continue to be an issue in the coming year

The opportunity for sustained future growth in Severn Trent Services remains Around 60 ATOs in Italy are expected to move from the public to private sector in the medium term and the market for municipality outsourcing in the US is expected to double to c $3 billion In the Products arena MicroDynamics® and BALPURE® offer attractive medium and longer term growth As a result, in 2011/12 we will be investing around £5 million in total, in our business development resources in the USA and Italy, and building our market and technology resources to support the launch of our BALPURE® and MicroDynamics® product lines Our base business of Operating Services and Water Purification is expected to deliver increased top line growth year on year in 2011/12, despite current difficult market conditions, although the first six months may still be challenging At the PBIT level, growth in the base business is expected to be offset by the investment in new opportunities, leaving Severn Trent Services PBIT in 2011/12 lower year on year Investment in these growth areas will, in the medium term, enable Severn Trent Services to deliver higher levels of sustainable growth

Legislation in Italy will drive market activity for private partners investing in the country's integrated water services (ATO) segment. We believe that our strong market presence gives us a great foundation to work from and expect to see an increase in our business here over the next several years.

Case study
Tapping into a new market opportunity

International Maritime Organisation (IMO) regulations will soon require the treatment of ballast water before it is brought into ports worldwide We have developed the patented BALPURE® system for the treatment of ballast water The result is highly desirable technology that puts us at the forefront of ballast treatment solutions for larger vessels in an addressable market that is expected to be worth around £7 billion up to 2020 and around £450 million annually beyond that

Business review
Looking forward

Since privatisation our industry has experienced two decades of improvement. But the world today is a very different place and if we are to meet our vision of creating a sustainable water industry, we need some changes. We are playing an active role in shaping the future of the water industry in the UK.

Severn Trent continues to address the medium and longer term challenges facing the industry and published its views in its publication 'Changing Course' This document is available for shareholders to read and copies may be obtained from the Company Secretary or electronically at www severntrent com Some of the key highlights from that document are presented below

Over the past 20 years our industry has seen improved customer standards, environmental performance and service quality, and become more efficient Water companies have also successfully funded an investment programme valued at around £85 billion However, these improvements have come at a cost

Customer bills have risen, energy use has increased by 113% and the industry as a whole is managing debts of some £33 billion On top of that, the reality of climate change is already having an impact on our business To carry on in the same way would not be sustainable That is why we published our document Changing Course in 2010, setting out our position and outlining the six key changes we believe are needed to address the challenges we face

Later this year the UK government is due to publish its White Paper While we do not know what recommendations it will contain, we are pleased with the response to Changing Course and encouraged by the development of the debate over water trading and policy making

Climate change
Whether it's the energy we use, the water we supply to our customers, or the quality of the diverse environment under our stewardship, our business both contributes to, and is affected by, climate change On the question of water scarcity, our strategy is to reduce demand and improve the flexibility of our network before developing new sources For instance, by encouraging our customers to use water sensibly we have one of the lowest per capita consumptions of water in the UK

However valuable these measures, they are not enough on their own Water companies need to think differently in order to tackle climate change and arrive at more sustainable solutions

Water trading
Changing weather patterns are predicted to lead to hotter, drier summers and wetter winters This will mean less water being available at different times of the year Our last Water Resources Management Plan showed that, over the next 25 years, Severn Trent will face a shortfall of 232 million litres a day because of climate change and population growth if we do not do things differently

'We're beyond the point of whether you believe in climate change or not. The reality is we are experiencing more extremes and we have to find ways to cope.'

Tony Wray,
Chief Executive

'The debate over the next 20 years will be about security of supply.'

Michael McKeon,
Finance Director

But this is not just a problem for Severn Trent, it is one for the nation as a whole One change we would like to see is more water trading Water companies could trade resources nationally using water from areas of lower cost to higher cost With the right regulatory regime we believe it would be possible to use existing networks to move water from one region to another

Intelligent funding
There is no doubt that over the next 20 years, the water industry will need to maintain significant investment in infrastructure in order to improve network resilience and reach higher environmental standards

Initiatives like water trading and more flexible outcome-based regulation will help avoid unnecessary capital investment, but the sector's continuing ability to deliver its investment programmes relies on its being able to fund them We believe that continuing to finance the programme entirely from borrowing is unsustainable, putting pressure on credit ratings and passing on risk to customers Equity participation remains as important as ever Long term sustainable returns need to reflect this reality

A digital version of the Changing Course report is available at www stwater co uk

'...we are looking at how we can better reveal the true value of water to enable the sectors to make better, more sustainable decisions. For example, we are exploring how abstraction and water trading can contribute to this.'

Regina Finn, Chief Executive, Ofwat
Ofwat Annual Report 2009/10

Competition and consolidation
Bringing about the kind of changes we believe our industry needs would require a change in the structure and regulation of the water sector The framework of incentives and output setting under the existing regime can mean that more sustainable solutions are overlooked in favour of capital intensive solutions Faced with the choice of sourcing low-cost water elsewhere or building a reservoir, companies often opt to build a reservoir This then becomes part of the regulated asset base, allowing water companies to increase pricing

We believe it would be better to encourage sustainable solutions that benefit customers and the environment A gradual move towards a market-based framework and competition within the sector would enable water companies to make best use of resources nationally rather than regionally Such a move would help maintain investors' confidence in our industry and avoid an increase in the cost of capital

As a water company we are unusual in that we are already able to supply water to large commercial and industrial companies across England and Wales through Severn Trent Services Our expertise in commercial markets, together with our confidence about embracing the future and our operational, financial and strategic strength mean we are well placed to adapt to any structural or regulatory changes in our industry Indeed, we are looking forward to the opportunities the future will bring, both in the regulated and commercial spheres

'The companies will need to plan, innovate and deliver services in new and more sustainable ways. And that means the regulatory environment we provide needs to change as well.'

Phillip Fletcher, Chairman, Ofwat
Ofwat Annual Report 2009/10

Changing course – six key changes required to meet future challenges

Policy changes
- More flexible implementation of EU Directives to ensure a better trade off between costs and carbon emissions
- Developing competition through water trading, this would also optimise resources nationally rather than just regionally

Regulatory changes
- A more flexible approach to environmental consents to allow for more cost effective approaches
- An improved price setting process to provide the right incentives for sustainable financing, more sustainable solutions and increased innovation

Industry changes
- Companies must take the lead in driving innovation, both in terms of the strategic and technical solutions they pursue and in shaping the wider direction the sector takes

Changes to the institutional framework
- Government should prioritise national policy outcomes and ensure the regulatory framework is set up to deliver them

Business review
Financial review

Group financial performance

We are now some two years on from the full effect of the financial crisis and many, but not all, financial activities and markets have returned to what may be considered normal levels However, we are yet to see the return of a fully functioning commercial paper market and have continued to support our liquidity position by holding cash reserves from earlier bond market issuances In other areas, we are yet to see any material effect on the finances of our customer base from the package of measures the UK Government has announced on public spending Indeed, we have improved our customer collections performance year on year The ability of domestic and commercial customers alike to support their water bills in this new environment has yet to be seen, though we remain confident that our debt recovery processes are in good shape to address any challenge that may arise

PBIT is profit before interest and tax, underlying PBIT is PBIT excluding exceptional items as set out in note 8

Group turnover was £1,711 3 million (£1,703 9 million), an increase of 0 4% over last year Severn Trent Water's prices were reduced by an average of 0 7% but measured consumption increased so that turnover was broadly similar to the prior year

Underlying group PBIT decreased by 6 8% to £519 1 million (£557 1 million) The primary factors affecting underlying PBIT are described in the commentary on Severn Trent Water and Severn Trent Services below There were net exceptional charges of £21 4 million (£49 7 million) Group PBIT decreased 1 9% to £497 7 million (£507 4 million)

Severn Trent Water

Turnover in Severn Trent Water increased by 0 3% in 2010/11 to £1,389 8 million Sales prices decreased by 0 7% (including inflation) from 1 April 2010 In the first half of the year consumption was higher period on period, as a result of strong household and robust commercial consumption The second half of the year showed a more normal period on period declining trend, leading to the 0 3% increase in turnover over the full year

Underlying PBIT decreased by 6 9% on the previous year to £503 7 million Beyond the increase in turnover of £4 5 million, a number of factors impacted underlying PBIT Employee costs decreased by £8 1 million as lower headcount offset higher pension costs but hired and contracted services were £9 8 million higher Depreciation increased by £16 4 million due to the growing asset base and write down of £6 4 million on one experimental sludge dryer There was a reduction in infrastructure renewals expenditure of £7 6 million Own work capitalised was £21 2 million lower in line with the lower levels of capital expenditure in the year Bad debts were £1 4 million lower and other costs increased by £11 8 million

During the financial year, Severn Trent Water invested £405 3 million (UK GAAP net of grants and contributions) in fixed assets and maintaining and improving its infrastructure network Included in this total was net infrastructure renewals expenditure of £96 9 million, charged to the income statement under IFRS

Severn Trent Services

	2011 £m	2010 £m	Increase/ (decrease) %
Turnover			
Services as reported	**336.1**	336 5	(0 1%)
Impact of exchange rate fluctuations	**–**	(4 4)	
Like for like businesses in constant currency	**336 1**	332 1	1 2%

	2011 £m	2010 £m	Increase/ (decrease) %
Underlying PBIT			
Services as reported	**25 7**	28 7	(10 5%)
Impact of exchange rate fluctuations	**–**	(0 3)	
Like for like businesses in constant currency	**25 7**	28 4	(9 5%)

Reported turnover in Severn Trent Services was £336 1 million in 2010/11, a decrease of 0 1% vs the prior year, and reported underlying PBIT decreased by 10 5% to £25 7 million

After adjusting for the impact of exchange rate fluctuations, turnover on a constant currency basis increased 1 2% but underlying PBIT measured on the same basis was down 9 5% The first half year saw profits rise period on period but the second half was impacted by the factors mentioned in the operating review

Operating Services
Turnover for the year was £201 3 million, a decrease of 3 2% compared to the prior year on a constant currency basis In the US and UK the Operating Services businesses broadly maintained their levels of activity from the previous year However, the business was impacted by project delays in Italy and reduced activity in our metering services and searches businesses in the UK, both of which are driven to some extent by the housing market

Water Purification
Turnover for the year was £105 6 million, an increase of 9 2% compared to the prior year on a constant currency basis However, the strong growth experienced in the first half of the year did not continue into the second half of the year and turnover in the second half of 2010/11 was at broadly the same level as the same period in the previous year

Analytical Services
Turnover for the year was £29 2 million, an increase of 6 2% This represented an improvement due to growth in revenue from new contracts

Corporate and other
Corporate overheads amounted to £9 2 million (£12 7 million) Our captive insurance company and other businesses generated a loss of £0 6 million (loss of £2 3 million) The group's captive insurance company insures Severn Trent group risks only and does not write any external business

Exceptional items
There were net exceptional charges in the year to 31 March 2011 of £21 4 million (£49 7 million) comprising

Restructuring costs

- a charge of £13 0 million in Severn Trent Water arising from programmes to restructure and realign the business, and
- a charge of £0 7 million in Severn Trent Services from the programmes to restructure the Water Purification and Analytical Services businesses

Regulatory matters

- a charge of £3 8 million in Severn Trent Services arising from the group's response to an audit in September 2010 by the Drinking Water Inspectorate (DWI) of aspects of the services provided by Severn Trent Laboratories Limited from its Bridgend laboratory, and
- a charge of £3 9 million in Corporate overheads arising from the group's response to a request from Ofwat to provide certain information under the Competition Act in connection with Severn Trent Laboratories Limited's contracts with Severn Trent Water Limited and certain other water companies

Net finance costs
The group's net finance costs were £230 6 million, compared to £218 8 million in the prior year The group has fixed the interest rate of its non index-linked debt for the five year period to March 2015 The group's cost of index-linked debt is however linked to the movement in the Retail Prices Index (RPI) This debt provides an economic hedge for Severn Trent Water's revenues and regulatory asset values that are also RPI linked under its regulatory regime The increase in the full interest charge is therefore largely due to higher interest charges on index-linked debt as inflation was higher than the prior year and in addition, average group net debt increased during the year The effective interest rate for 2010/11 was 6 4% (5 8%) of which cash interest cost is 5 0% vs 5 4% in the prior year

Profit before tax
Underlying group profit before tax decreased by 14 7% to £288 6 million (£338 4 million) Group profit before tax was £253 0 million (£334 4 million)

Taxation
The total tax credit for the full year was £21 5 million (charge of £82 9 million), of which current tax represented a charge of £32 1 million (£40 7 million) and deferred tax was a credit of £53 6 million (£42 2 million)

A prior year tax credit amounting to £34 4 million arose during the year, mainly as a result of the agreement of open tax positions covering a number of years

The effective rate of current tax, excluding prior year items and exceptional items, calculated on profit before tax, exceptional items and gains/(losses) on financial instruments was 24 4% (22 6%) The change in effective rate is as a result of lower capital allowances in Severn Trent Water

Going forward, we expect the effective current tax rate for 2011/12 to be in the range of 26% to 27%

Profit for the period and earnings per share
Profit for the period was £274 5 million (£251 5 million)

Basic earnings per share were 115 2 pence (105 6 pence) Adjusted basic earnings per share (before exceptional items, gains/(losses) on financial instruments and deferred tax) were 105 6 pence (122 8 pence)

Cash flow

	2011 £m	2010 £m
Cash generated from operations	**753 0**	708 0
Net capital expenditure	**(399.5)**	(487 8)
Net interest paid	**(180 3)**	(194 2)
Tax (paid)/received	**(32 4)**	(53 8)
Other cash flows	**(1.5)**	(1 6)
Free cash flow	**139.3**	(29 4)
Acquisitions and disposals	**–**	(11 0)
Dividends	**(169 4)**	(159 7)
Net issue of shares	**2.7**	2 4
Change in net debt from cash flows	**(27 4)**	(197 7)
Non cash movements	**(80.0)**	(3 8)
Change in net debt	**(107 4)**	(201 5)
Net debt 1 April	**(3,761 4)**	(3,559 9)
Net debt at 31 March	**(3,868 8)**	(3,761 4)
Net debt comprises		
Cash and cash equivalents	**315 2**	227 8
Cross currency swaps hedging debt	**160 4**	187 3
Bank loans	**(846 8)**	(689 8)
Other loans	**(3,230 9)**	(3,185 9)
Finance leases	**(266.7)**	(300 8)
	(3,868 8)	(3,761 4)

Business review
Financial review (continued)

Cash generated from operations was £753 million (£708 million) Capital expenditure net of grants and proceeds of sales of fixed assets was £399 5 million (£487 8 million) Net interest paid decreased to £180 3 million (£194 2 million)

Net debt at 31 March 2011 was £3,868 8 million (£3,761 4 million) Balance sheet gearing (net debt/net debt plus equity) at the year end was 77 8% (79 9%) Net debt, expressed as a percentage of Regulatory Capital Value at 31 March 2011 was 57% (58%) The group's net interest charge, excluding gains/(losses) on financial instruments and net finance costs from pensions, was covered 3 5 times (3 9 times) by profit before interest, tax, depreciation and exceptional items, and 2 3 times (2 7 times) by underlying PBIT

The fair value of the group's borrowings at 31 March 2011 is estimated to be £4,671 8 million (£4,267 9 million) compared to the book value of £4,344 4 million (£4,176 5 million) The group's debt instruments are not traded in an active market and hence the fair value disclosed above is based on a theoretical discounted cash flow calculation and does not represent an estimate of the amount for which the debt could be settled

Treasury management and liquidity
The group continues to monitor liquidity carefully At 31 March 2011 the group had £315 2 million in cash and cash equivalents The group also has an undrawn £500 million committed bank facility of which £41 7 million expires in 2012 with the balance maturing in 2013 Average debt maturity is around 16 years The group is funded for its investment and cash flow needs up to March 2013

Cash is invested in deposits with highly rated (A+) banks and liquidity funds and the list of counterparties is regularly reviewed and reported to the board

Treasury policy and operations
Our treasury affairs are managed centrally and in accordance with our Treasury Procedures Manual and Policy Statement The treasury operation's role is to manage liquidity, funding, investment and our financial risk, including risk from volatility in interest and (to a lesser extent) currency rates and counterparty credit risk The board determines matters of treasury policy and its approval is required for certain treasury transactions

Our strategy is to access a broad range of sources of finance to obtain both the quantum required and lowest cost compatible with the need for continued availability Our principal operating subsidiary, Severn Trent Water, is a long term business characterised by multi year investment programmes Our strategic funding objectives reflect this and the liquidity position and the availability of committed funding are essential to meeting our objectives and obligations We therefore aim for a balance of long term funding or commitment of funds across a range of funding sources at the best possible economic cost

The group's current policy for the management of interest rate risk requires that no less than 45% of the group's borrowings should be at fixed interest rates, or hedged through the use of interest rate swaps or forward rate agreements At 31 March 2011, interest rates for some 76% of the group's net debt of £3,868 8 million were fixed in this way

We use financial derivatives solely to manage risks associated with our normal business activities We do not hold or issue derivative financial instruments for financial trading

Except for debt raised in foreign currency, which is fully hedged, our business does not involve significant exposure to foreign exchange transactions We have investments in various assets denominated in foreign currencies, principally the US dollar and the euro Our current policy is to hedge an element of the currency translation risk associated with certain foreign currency denominated assets

We have entered into energy swaps that fix the cost of substantially all of Severn Trent Water's expected net electricity consumption for the next three years and part of its anticipated consumption for the following year The price fixed in these swaps is lower than the amount assumed in the Final Determination for AMP5

The group issues notes in foreign currency under its EMTN programme and uses cross currency swaps to convert the proceeds to sterling The effect of these swaps is that interest and principal payments on the borrowings are denominated in sterling and hence the currency risk is eliminated The foreign currency notes and the cross currency swaps are recorded in the balance sheet at their fair values and the changes in fair values are taken to gains/(losses) on financial instruments in the profit and loss account Since the terms of the swaps closely match those of the underlying notes, such changes tend to be broadly equal and opposite

The group holds interest rate swaps with a net notional principal amount of £462 3 million and cross currency swaps with a net notional principal amount of £536 6 million which economically act to hedge the interest rate risk on floating rate debt or the exchange rate risk on certain foreign currency borrowings However, the swaps do not meet the hedge accounting rules of IAS 39 and therefore these swaps are carried in the balance sheet at fair value The changes in fair value are taken to gains/(losses) on financial instruments in the profit and loss account During the period there has been a decrease of £15 7 million in the fair value of these instruments

It is important to note that we intend to, and typically do hold these swaps to maturity Further, this is not a cash movement and, over the life of the swaps, these changes in fair value will net out

Credit ratings
Our long term credit ratings are

Long term ratings	Severn Trent Plc	Severn Trent Water
Moody's	Baa1	A3
Standard and Poor's	BBB-	BBB+

Further details of our borrowings, investments and financial instruments are contained in note 32 to the financial statements

Pensions
The group operates two defined benefit pension schemes, of which the Severn Trent Pension Scheme (STPS) is by far the largest Formal triennial actuarial valuations and funding agreements for the STPS are in the course of being renewed as at 31 March 2010 The key actuarial assumptions from these valuations have been updated for the accounts as at 31 March 2011 with overall contribution levels remaining unchanged, including deficit reduction payments of £10 million per annum, until new agreements are agreed

On an IAS 19 basis, the estimated net position (before deferred tax) of the group's defined benefit pension schemes was a deficit of £292 1 million as at 31 March 2011 This compares to a deficit of £354 9 million as at 31 March 2010

On an IAS 19 basis, the funding level has increased from around 79 7% at 31 March 2010 to around 83 5% at 31 March 2011

	2011 %	2010 %
Price inflation	**3 50**	3 60
Salary increases	**4 00**	4 10
Pension increases in payment	**3 50**	3 60
Pension increases in deferment	**3 50**	3 60
Discount rate	**5 60**	5 70
Long term rate of return on equities	**7 85**	8 00
Age to which current pensioners aged 65 are expected to live		
– men	**87.4**	85 3
– women	**91.0**	88 6
Age to which future pensioners aged 45 at the balance sheet date are expected to live		
– men	**88 0**	86 5
– women	**91.8**	89 6

The following table summarises the estimated impact on scheme liabilities resulting from changes to key actuarial assumptions whilst holding all other assumptions constant

Assumption	Change in assumption	Impact on scheme liabilities
Discount rate	Increase/decrease by 0 1%	Decrease/increase by £30 million
Price inflation	Increase/decrease by 0 1%	Increase/decrease by £25 million
Mortality	Increase in life expectancy by 1 year	Increase by £45 million

On 11 May 2011, Severn Trent announced it is consulting with its 6,000 plus UK employees on proposed changes to its pension arrangements, which would see all existing pensions replaced by one new defined contribution scheme Under the new proposals, the defined benefit schemes would close to future accrual, whilst protecting the benefits already built up by members The existing defined contribution scheme would also be replaced by the new pension arrangements The proposal is to automatically enrol new employees into the new pension from 2012 and automatically enrol those employees who are not currently members of a Severn Trent scheme from 2013 Severn Trent is consulting with its employees from June for three months, with changes introduced no earlier than April 2012

Accounting Policies and presentation of the financial statements
Our consolidated financial statements are prepared in accordance with International Financial Reporting Standards that have been endorsed by the European Union

Governance Directors' report

The directors present their report, together with the audited financial statements of the group, for the year ended 31 March 2011

Principal activity

The principal activity of the group is to provide and treat water and remove waste water in the UK and internationally

Details of the principal joint ventures, associated and subsidiary undertakings of the group at 31 March 2011 appear in notes 19, 20 and 40 to the financial statements on pages 83 and 111

Business review

The Chairman's statement, the Chief Executive's review, the report and performance reviews for the group's main businesses and the financial review on pages 10 to 25 provide detailed information relating to the group and its strategy, the operation of its businesses and the results and financial position for the year ended 31 March 2011

Details of the principal risks and uncertainties facing the group are set out in the risk and assurance section on pages 56 to 58

All of the above are incorporated by reference in (and are deemed to form part of) this report

Directors and their interests

Biographies of the directors currently serving on the board are set out on pages 30 and 31

Details of changes to the board during the year and of the directors offering themselves for reappointment at the Annual General Meeting (AGM) are set out in the Chairman's letter on pages 33 to 38

Details of directors' service agreements are set out in the Directors' remuneration report on page 50 The interests of the directors in the shares of the company are shown on pages 52 to 55 of that report

Directors' indemnities

The company's articles of association provide that directors of the company shall be indemnified by the company against any costs incurred by them in carrying out their duties, including defending any proceedings brought against them arising out of their positions as directors in which they are acquitted or judgment is given in their favour or relief from any liability is granted to them by the court

Employees

The average number of employees within the group is shown in note 9 to the financial statements on page 76

Severn Trent believes that a diverse and inclusive culture is a key factor in being a successful business Apart from ensuring an individual has the ability to do the job we do not discriminate in any way and make every effort to ensure that those with disabilities are able to be employed by us We ensure that training, career development and promotion opportunities are available for all our employees irrespective of their gender, race, age or disability

The group actively encourages employee involvement and consultation and places emphasis on keeping its employees informed of its activity and financial performance by way of briefings and publication to staff of all relevant information and corporate announcements To help develop employees' interest in the company's performance, Severn Trent offers two employee share plans The Severn Trent Sharesave Scheme, an HM Revenue and Customs approved SAYE plan, is offered to UK employees on an annual basis The Severn Trent Share Incentive Plan, approved by HM Revenue and Customs, makes an annual award of shares to Severn Trent Plc and Severn Trent Water Limited employees, based on performance against the KPIs

Research and development

Expenditure on research and development is set out in note 7 to the accounts on page 75

Treasury management

The disclosures required under the EU Fair Value Directive in relation to the use of financial instruments by the company are set out in note 32 to the accounts on pages 92 to 103 Further details on our treasury policy and management are set out in the financial review on page 24

Post balance sheet events

Details of post balance sheet events are set out in note 38 to the group financial statements on page 110

Dividends

An interim dividend of 26 04 pence per ordinary share was paid on 14 January 2011 The directors recommend a final dividend of 39 05 pence per ordinary share to be paid on 29 July 2011 to shareholders on the register on 24 June 2011 This would bring the total dividend for 2010/11 to 65 09 pence per ordinary share (2010 72 32 pence) The payment of the final dividend is subject to shareholder approval at the AGM

Capital structure

Details of the company's issued share capital and of the movements during the year are shown in note 29 to the financial statements on page 91 The company has one class of ordinary shares which carries no right to fixed income Each share carries the right to one vote at general meetings of the company The issued nominal value of the ordinary shares is 100% of the total issued nominal value of all share capital

There are no specific restrictions on the size of a holding nor on the transfer of shares, which are both governed by the general provisions of the articles of association and prevailing legislation The directors are not aware of any agreements between holders of the company's shares that may result in restrictions on the transfer of securities or on voting rights

Details of employee share schemes are set out in note 33 to the financial statements on pages 103 to 107 For shares held by the Severn Trent Employee Share Ownership Trust, the trustee abstains from voting

No person has any special rights of control over the company's share capital and all issued shares are fully paid

With regard to the appointment and replacement of directors, the company is governed by its articles of association, the Combined Code on Corporate Governance, the Companies Act 2006 and related legislation The articles may be amended by special resolution of the shareholders The powers of directors are described in the Board Governance document, the articles and the Chairman's letter on pages 33 to 38

Under its articles of association, the directors have authority to allot ordinary shares, subject to the aggregate nominal amount limit set at the 2010 AGM

There are a number of agreements that take effect after, or terminate upon, a change of control of the company, such as commercial contracts, bank loan agreements, property lease arrangements and employee share plans. None of these is considered to be significant in terms of their likely impact on the business of the group as a whole. There are no agreements between the company and its directors or employees that provide for compensation for loss of office or employment that occurs because of a takeover bid.

Substantial shareholdings

As at 23 May 2011 the company had been notified in accordance with chapter 5 of the Disclosure and Transparency Rules of the following major shareholdings.

Name of holder	Percentage of voting rights and issued share capital	No. of ordinary shares of $97^{17}/_{19}$p each
Norges Bank	3.98%	9,438,492
Legal & General Group Plc	3.97%	9,403,273
Aegon Asset Management	3.04%	7,214,266

Percentages rounded to two decimal places.

Authority to purchase shares

The company was given authority at its AGM in 2010 to make market purchases of ordinary shares up to a maximum number of 23,697,346 shares. Similar authority will again be sought from shareholders at this year's AGM. No market purchases were made by the company during the year ended 31 March 2011.

Supplier payment policy

Individual operating companies within the group are responsible for establishing appropriate policies with regard to the payment of their suppliers. The companies agree terms and conditions under which business transactions with suppliers are conducted. It is group policy that provided a supplier is complying with the relevant terms and conditions, including the prompt and complete submission of all specified documentation, payment will be made in accordance with agreed terms. It is also group policy to ensure that suppliers know the terms on which payment will take place when business is agreed. Details of supplier payment policies can be obtained from the individual companies at the addresses shown in note 40 to the financial statements on page 111. Trade creditors for the group at the year end are estimated as representing 24.4 days' purchases (2010: 44.1 days' purchases).

Contributions for political and charitable purposes

Donations to charitable organisations during the year amounted to £181,843 (2010: £326,382). Donations are given to charities whose projects align closely with our aim to promote the responsible use of water resources and waste water services which provide the opportunity for longer term partnerships. In addition we provide donations to employee nominated charities through a matched funding scheme and health and safety reward schemes. We are also committed to supporting WaterAid, the UK's only major charity dedicated to improving access to safe water, hygiene and sanitation in the world's poorest countries.

In 2008/09 a provision of £5 million was established for additional contributions to the Severn Trent Charitable Trust as agreed with Ofwat. Severn Trent Water paid £2 million additional contributions in that year and a further £2 million in 2009/10. The remaining £1 million was paid in 2010/11 (provided for in previous years), to the Severn Trent Trust Fund which helps people out of poverty and debt.

Severn Trent's policy is not to make any donations for political purposes in the UK, or to donate to EU political parties or incur EU political expenditure. Accordingly neither Severn Trent Plc nor its subsidiaries made any political donations or incurred political expenditure in the financial year under review.

Under the provisions of the Political Parties Elections and Referendums Act 2000 (the relevant provisions of which are now contained in Part 14 of the Companies Act 2006), shareholder authority is required for political donations to be made or political expenditure to be incurred by the company or any of its subsidiaries in the EU and disclose any such payments in the annual report. The legislation gives a wide definition of what constitutes political donations and political expenditure including sponsorship, subscriptions, payment of expenses, paid leave for employees fulfilling public duties and support for bodies representing the business community in policy review or reform. The company has therefore obtained limited authority from shareholders as a precautionary measure to allow the company to continue supporting the community and such organisations without inadvertently breaching the legislation.

At the 2010 AGM, shareholders gave the company authorities to make political donations or to incur political expenditure in the EU (which would not ordinarily be regarded as political donations) up to an aggregate annual limit of £50,000 for the company and its subsidiaries. Pursuant to those authorities, during the year ended 31 March 2011 the group incurred costs of £nil (2010: £nil). Those authorities will expire at the 2011 AGM and, in line with market practice to renew the authorities on an annual basis, the board has decided to put forward a resolution to this year's AGM to renew the authorities to make donations to political organisations and to incur political expenditure up to a maximum of £50,000 per annum. As permitted under the Companies Act 2006, this resolution also covers any political donations made, or political expenditure incurred, by any subsidiaries of the company.

Analysis of shareholdings at 31 March 2011

Category	Number of shareholders	% of shareholders	Number of shares	% of shares
Individual and joint accounts	67,072	90.83	26,250,821	11.07
Other*	6,774	9.17	210,891,713	88.93
Total	**73,846**	**100.00**	**237,142,534**	**100.00**

* Includes insurance companies, nominee companies, banks, pension funds, other corporate bodies, limited and public limited companies.

Size of holding	Number of shareholders	% of shareholders	Number of shares	% of shares
1–500	54,416	73.69	10,730,367	4.52
501–1,000	12,947	17.53	9,353,906	3.94
1,001–5,000	5,452	7.38	9,932,847	4.19
5,001–10,000	311	0.42	2,162,766	0.91
10,001–25,000	196	0.27	3,214,558	1.36
25,001–50,000	138	0.19	5,157,229	2.17
Over 50,000	386	0.52	196,590,861	82.91
Total	**73,846**	**100.00**	**237,142,534**	**100.00**

Governance
Directors' report (continued)

Internal controls
The board is responsible for the group's system of internal control and for reviewing its effectiveness The board reviews the effectiveness of the system of internal control, including financial, operational and compliance and risk management, at least annually in accordance with the requirements of the Combined Code for effectiveness and adequacy The internal control system can only provide reasonable and not absolute assurance against material misstatement or loss, as it is designed to manage rather than eliminate the risk of failure to achieve business objectives

The Audit Committee reviews the group's risk management process and the effectiveness of the system of internal control on behalf of the board and keeps under review ways in which to enhance the control and audit arrangements The Audit Committee receives reports every six months from the Chief Executive detailing the significant risks and uncertainties faced by the group, an assessment of the effectiveness of controls over each of those risks and an action plan to improve controls where this has been assessed as necessary During the course of its review of the system of internal control in 2010/11, the Audit Committee has not identified nor been advised of any failings or weaknesses which it has determined to be significant Therefore a confirmation in respect of necessary actions has not been considered appropriate

The Internal Audit department provides objective assurance and advice on risk management and control The external auditor also reports on significant financial control issues to this committee

The board confirms that procedures providing an ongoing process for identifying, evaluating and managing the principal risks and uncertainties faced by the group have been in place for the year to 31 March 2011 and up to the date of approval of the Annual Report, which is in accordance with the revised guidance on internal control published in October 2005 (the Turnbull Guidance)

External auditor
In the case of each of the persons who were directors of the company at the date when this report was approved

- so far as each of the directors is aware, there is no relevant audit information of which the company's auditor is unaware, and
- each of the directors has taken all the steps that he/she ought to have taken as a director to make himself/herself aware of any relevant audit information and to establish that the company's auditor is aware of that information

Relevant audit information means information needed by the company's auditor in connection with preparing its report

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006

Deloitte LLP have indicated their willingness to continue as auditor A resolution to reappoint Deloitte LLP will be proposed at this year's AGM

The Audit Committee has recommended to the board the reappointment of Deloitte LLP and a resolution to that effect will be on the agenda at the AGM The Audit Committee will also be responsible for determining the audit fee on behalf of the board

Accounts of Severn Trent Water Limited
Regulatory accounts for Severn Trent Water Limited are prepared and sent to Ofwat A copy of these accounts will be available from the website of Severn Trent Water Limited (www stwater co uk) or on written request to the Company Secretary (at the address given on the back cover) There is no charge for this publication

Going concern
The group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Chief Executive's review on pages 6 and 7 and the business reviews of Severn Trent Water and Severn Trent Services on pages 8 to 19 The financial position of the group, its cash flows, liquidity position and borrowing facilities are described in the Financial review on pages 22 to 25 The group's objectives, policies and processes for managing its capital and its financial risk management objectives are described in the Financial review and in the Governance report on pages 26 to 58 Details of the group's financial instruments, hedging activities and exposure to credit risk and liquidity risk are described in note 32 to the group financial statements

The group's principal operating subsidiary, Severn Trent Water, is a regulated long term business characterised by multi year investment programmes The group's strategic funding objectives reflect this The group therefore seeks to attain a balance of long term funding or commitment of funds across a range of funding at the best possible economic cost Average debt maturity is 16 years and the effective average interest cost during the year was 6 4% The group is in a strong liquidity position with £315 2 million in cash and liquid reserves and £500 million of undrawn committed bank facilities, which are expected to be sufficient to fund its investment and cash flow needs until March 2013 in the normal course of business

Severn Trent Water operates in an industry that is currently subject to economic regulation rather than market competition Ofwat, the economic regulator, has a statutory obligation to set price limits that it believes will enable the water companies to finance their activities As a consequence the directors believe that the group is well placed to manage its business risks successfully despite the current uncertain economic outlook

After making enquiries, the directors have a reasonable expectation that the company and the group have adequate resources to continue in operational existence for the foreseeable future Accordingly, they continue to adopt the going concern basis in preparing the Annual Report and Accounts

Annual general meeting
The AGM of the company will be held at the International Convention Centre, Broad Street, Birmingham B1 2EA at 11am on Wednesday 20 July 2011 The notice convening the meeting, together with details of the business to be considered and explanatory notes for each resolution, is distributed separately to shareholders It is also available on the company's website (www severntrent com)

By order of the board

Fiona Smith

Fiona Smith
General Counsel and Company Secretary
26 May 2011

Governance
Directors' responsibility statement

The directors are responsible for preparing the Annual Report, Directors' remuneration report and the financial statements in accordance with applicable law and regulations

Company law requires the directors to prepare such financial statements for each financial year Under that law the directors are required to prepare group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and Article 4 of the IAS Regulation and have chosen to prepare the parent company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law) Under company law the directors must not approve the accounts 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 the parent company financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and accounting 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, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business

In preparing these financial statements, International Accounting Standard 1 requires that the directors

- properly select and apply accounting policies,
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information,
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance, and
- make an assessment of the company's ability to continue as a going concern

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 are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of 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 United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions

We confirm that to the best of our knowledge

- the financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole, and
- the management report, which is incorporated into the directors' report, includes a fair review of the development and performance of the business and the position of the company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face

Andrew Duff
Chairman

Michael McKeon
Finance Director

Governance
Board of directors

Severn Trent Plc board of directors as at 31 March 2011

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9

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11

Board committees

A

Audit Committee
Baroness Noakes (C)*
Dr Bernard Bulkin*
Richard Davey*
Kerry Porritt (S)

R

Remuneration Committee
Richard Davey (C)*
Dr Bernard Bulkin*
Andrew Duff*
Martin Lamb*
Fiona Smith (S)

C

Corporate Responsibility Committee
Dr Bernard Bulkin (C)*
Andrew Duff*
Gordon Fryett*
Tony Wray
Kerry Porritt (S)

N

Nominations Committee
Andrew Duff (C)*
Dr Bernard Bulkin*
Richard Davey*
Gordon Fryett*
Martin Lamb*
Baroness Noakes*
Tony Wray
Fiona Smith (S)

(C) Chairman
(S) Secretary
(•) Non-executive director

Management committee

E

Executive Committee
Tony Wray (C)
Dr Tony Ballance
Simon Cocks
Evelyn Dickey
Len Graziano
Myron Hrycyk
Martin Kane
Michael McKeon
Alec Richmond
Andy Smith
Fiona Smith

Senior independent non-executive director
Richard Davey*

General Counsel and Company Secretary
Fiona Smith

1. Dr Tony Ballance BSc (Hons) MA (Econ) PhD (46)
Director, Strategy and Regulation
Appointed to the board in October 2007
Tony s extensive experience in utility policy and regulation working for Ofwat as Chief Economist and then as an economic consultant leaves him ideally placed to lead the company s strategic and regulatory work **Other directorships and offices** Chief Economist, Office of Water Services (Ofwat) (1996–1999), director of London Economics (1999–2000), director of Stone and Webster Consultants (2000–2005)

E

2 Dr Bernard Bulkin* BS PhD FRSC FRSA FIE (69)
Independent non-executive director
Appointed to the board in January 2006 Bernard is the Chairman of the Corporate Responsibility Committee
Bernard s involvement in both innovation and policy on climate change and renewable energy, together with an understanding of how to guide improved performance on safety and environmental operational issues enables him to contribute significantly to the board **Other directorships and offices** Chairman of Chemrec AB, a Swedish company, non-executive director of REAC AB in Sweden and of Ze-gen Corporation in Boston, Venture Partner at Vantage Point, an international venture capital firm, Chair of the Office of Renewable Energy Deployment, UK Department of Energy and Climate Change, was Chief Scientist at BP Plc (2000–2003)

A C R N

3 Richard Davey* BA (62)
Senior independent non-executive director
Appointed to the board in January 2006 Richard is Chairman of the Remuneration Committee
Richard has an investment banking background and was formerly Head of Investment Banking at NM Rothschild and Sons With extensive experience of the financial services sector having run Rothschild s Financial Services Group and working with a number of high street banks and insurers, Richard brings valuable financial expertise to the board and Audit Committee and as chair of the Remuneration Committee **Other directorships and offices** non-executive Chairman of London Capital Holdings Plc, Vice Chairman of Yorkshire Building Society, non-executive director of Amlin Plc, non-executive director of Freeserve Plc (1999–2001) non-executive director of Scottish Widows Fund and Life Assurance Society (1996–2000)

A R N

4 Andrew Duff* BSc FEI (52)
Non-executive Chairman
Appointed to the board in May 2010
Andrew s strong track record working in regulated business gives him the relevant experience to make him the right Chairman to lead the group through the next phase of development **Other directorships and offices** Senior independent director of Wolseley Plc Member of the board of trustees of Macmillan Cancer Support, Group Chief Executive Officer, RWE npower (2003–2009) Fellow of the Energy Institute

N R C

5. Gordon Fryett* (57)
Independent non-executive director
Appointed to the board in July 2009
Gordon s extensive experience working in and with international businesses, accountability for managing large areas of capital expenditure and a broad range of executive and operational experience in a highly customer facing environment, enables him to bring a great deal of experience and expertise to the board **Other directorships and offices** Group Property Director of Tesco, CEO of Tesco Ireland (2001–2006), Director of International Support for Tesco (1997–2001), Alumnus of INSEAD

C N

6. Martin Kane BSc CEng CEnv MICE MIWEM FIW (58)
Director of Customer Relations
Appointed to the board in October 2007 Martin has been Director of Customer Relations, Severn Trent Water, since May 2006
Martin joined Severn Trent Water in 1975 and has held various senior posts giving him an extensive understanding of the design, construction and operation of water and waste water treatment plants, water distribution networks and sewerage systems **Other directorships and offices** board member of UK Water Industry Research Limited board member of Utilities and Service Industries Training Limited

E

7. Martin Lamb* BSc MBA (51)
Independent non-executive director
Appointed to the board in February 2008
Martin has extensive experience of managing and developing large engineering businesses in all parts of the world His strong commercial acumen, experience of managing complex projects, and familiarity with current market pressures as a serving Chief Executive leave him well placed to add value to the Severn Trent business **Other directorships and offices** Chief Executive of IMI plc, non-executive director of Spectris plc (1999–2006)

R N

8 Michael McKeon MA CA (54)
Finance Director
Appointed to the board in December 2005
Michael has extensive international business experience having worked overseas for CarnaudMetalbox, Elf Atochem and Price Waterhouse He also held various senior roles with Rolls-Royce Plc from 1997 to 2000 including Finance Director of Aerospace Group and was Finance Director of Novar Plc from 2000 to 2005 Michael is a Chartered Accountant and a Member of the Institute of Chartered Accountants of Scotland **Other directorships and offices** non-executive director and Chairman of the Audit Committee of The Merchants Trust Plc, Finance Director of Novar Plc (2000–2005)

E

9. Baroness Noakes* DBE LLB FCA (61)
Independent non-executive director
Appointed to the board in February 2008 Sheila Noakes is the Chairman of the Audit Committee
Sheila is a Fellow of the Institute of Chartered Accountants in England and Wales and served as its President from 1999–2000 She was a senior partner of KPMG from 1983 to 2000 She is an experienced audit committee chairman and currently chairs the Carpetright Plc Audit Committee **Other directorships and offices** senior independent director of Carpetright Plc, director of the Thomson-Reuters Founder Share Company, non-executive director of Imperial Chemical Industries Plc (2004–2008), non-executive director of Hanson Plc (2001–2007), Member of the Court of the Bank of England (1994–2001)

A N

10 Andy Smith BTech (Hons) (50)
Director of Water Services
Appointed to the board in October 2007
Andy has worked in the UK and overseas with BP Mars and Pepsi in engineering and operational management roles, and as group HR director and a member of the board at Boots Andy brings a broad range of executive and operational experience from different sectors to the board **Other directorships and offices** director of Boots Group Plc (2002–2003)

E

11. Tony Wray BSc (Hons) (49)
Chief Executive
Appointed to the board in March 2005 and became Chief Executive in October 2007
Tony's experience of a wide range of operational and strategic leadership roles in the Energy, Telecoms, Water and Waste industries enables him to bring a multi disciplined approach to the board **Other directorships and offices** non-executive director – Energy and Utility Skills the sector skills council, Member of the Business Advisory Board for Living with Environmental Change, director of Networks at Eircom, the Republic of Ireland's telephone operation (2003–2005) director roles within Transco and National Grid Transco (1997–2003)

C N E

Governance
Executive Committee

The Chief Executive is supported in his role by the executive management team and together they comprise the Executive Committee During the year, the Executive Committee comprised the executive directors and senior executive managers responsible for key operational and central functions Photographs of the members of the committee, together with their biographies are set out below

The Executive Committee oversees the development and execution of the Severn Trent strategy It also has accountability for achieving business results The terms of reference of the Executive Committee are available on the company's website (www severntrent com) or from the Company Secretary

During the year, the Executive Committee met to consider strategy, business management, policy and planning, and operational performance

Members of the Executive Committee are delegated responsibility to sit on steering groups that oversee the delivery of our strategy and business management During the year, steering groups were set up to oversee areas such as our move to Severn Trent Centre, the integrated delivery of our year end results and annual June Return to Ofwat and our leadership development

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1 Tony Wray BSc (Hons) (49) Chief Executive
Please see full biography on page 31

2 Martin Kane BSc CEng CEnv MICE MIWEM FIW (58) Director of Customer Relations
Please see full biography on page 31

3. Michael McKeon MA CA (54) Finance Director
Please see full biography on page 31

4. Fiona Smith LLB (52) General Counsel and Company Secretary

Joined Severn Trent in February 2006 Fiona is a Solicitor and was previously General Counsel and Company Secretary at National Grid plc, where she worked for 15 years, before becoming General Counsel at Transport for London for two years prior to joining Severn Trent

5 Alec Richmond BSc (Econ) FCA FIIA (53) Director of Internal Audit

Joined Severn Trent in June 2007 Prior to that, he worked for Cadbury Schweppes Plc leading the company's global internal audit service from 2000-2005 Before joining Severn Trent, he worked for RSM Robson Rhodes as a Director and a member of the management board responsible for Risk Assurance Services Alec is a fellow of the ICAEW

6 Andy Smith BTech (Hons) (50) Director of Water Services
Please see full biography on page 31

7 Dr Tony Ballance BSc (Hons) MA (Econ) PhD (46) Director, Strategy and Regulation
Please see full biography on page 31

8 Simon Cocks BA (Hons) (45) Waste Water Services Director

Joined Severn Trent in July 2009 Simon is an electrical engineer by training and began his career in military communications working for Plessey and then GEC He previously worked for London Electricity in various operational and management roles and, more recently for National Grid where he was Head of UK Operations Performance and Planning, then Commercial Director for the gas and electricity business in the UK and Europe, and more recently held the position of Chief Procurement Officer before joining Severn Trent

9 Myron Hrycyk MBA (54) Chief Information Officer

Joined Severn Trent in April 2008 Myron has delivered major IT strategic programmes reorganised corporate IT units and deployed high performance IT practices in previous roles for NYK Logistics and Unipart Myron is the executive sponsor of the company's SAP/ERP transformation programme

10 Leonard Graziano MBA BEng (65) President and Chief Executive Officer, Severn Trent Services

Joined Severn Trent in January 2000 Prior to joining Severn Trent Services Len served as President of Chemineer, Inc , a unit of Robbins & Myers Inc , a global leader in industrial mixing and agitation equipment and technology He also served as a President of Johnston Pump Company, a full line vertical pump, parts and repair company

11 Evelyn Dickey BSc (Hons) (48) Director of Human Resources

Joined Severn Trent in November 2006 Evelyn has wide HR experience leading design and delivery of major change programmes, business restructuring, employee relations, resourcing organisational capability and performance management initiatives Before joining Severn Trent Evelyn worked in HR consultancy and as HR Director (HR Operations) for Boots the Chemists

Governance
Chairman's letter

Andrew Duff
Chairman

Governance in Severn Trent

The way we are structured
- Our organisation is structured to allow for effective and efficient decision making with clear accountabilities

The way we choose to behave
- Our Code of Conduct sets out our approach to responsible business behaviours
- The Code of Conduct is supported by 14 group policies and our behaviour model Further details of the Code of Conduct can be found on our website (www severntrent com)

The way we assure our performance
- Management assurance is provided by a combination of effective management processes and risk and compliance activities
- Independent assurance is provided primarily by Internal Audit, by our external auditors and other external bodies

Dear Shareholder

Introduction
I want to set out in this letter how governance underpins our activities in Severn Trent and describe how we apply the principles of good corporate governance as set out in the Combined Code on Corporate Governance issued by the Financial Reporting Council (FRC) in 2008 (Combined Code)

Compliance with the Combined Code
The Combined Code sets out standards of good practice that listed companies are expected to follow in areas such as how we structure the board appropriately and develop its members, how we pay and reward our executive team, our accountability and audit, and our relationship with our shareholders

For the whole of the financial year ended 31 March 2011, Severn Trent was fully compliant in its application of the Combined Code

Our compliance with the Combined Code demonstrates our commitment to the highest standards of governance and corporate behaviour The Combined Code has been replaced during the financial year by the UK Corporate Governance Code The events in our corporate markets over the previous two years necessitated a review of the Combined Code and your board encouraged and supported the changes that the new Code has introduced Our response to the consultation on the review of the Combined Code is available for you to view on the website of the Financial Reporting Council, www frc org uk The UK Corporate Governance Code applies to accounting periods beginning on or after 29 June 2010 Our formal obligation for 2011 is to report how we have applied the principles of the Combined Code

Board membership
From 10 May 2010 the board has consisted of me, your non-executive Chairman, five executive directors and five independent non-executive directors Together, as a unified board, I believe we bring an appropriate balance of innovation, experience, independence and challenge to ensure effective decision making

Photographs of the members of the board, together with their biographies and a description of the skills that they bring to bear, can be found on pages 30 and 31

Further to the publication of the Davis Report, 'Women on Boards', in February this year, boards of FTSE 350s have been encouraged to promote greater female representation on corporate boards Recent guidance from the Financial Reporting Council has also highlighted the importance of greater diversity of psychological profile around the board table

I consider that diversity in the board room is essential to good business, helping companies better to meet the needs of their stakeholders

As part of our ongoing board membership renewal we will ensure that our recruitment and appointment processes continue to ensure that all appointments are meritocratic and that our board represents the best interests of shareholders

Role of the Chairman
I joined the board in May 2010 and was appointed Chairman from the end of the AGM, on 20 July 2010, replacing Sir John Egan

The role of the Chairman is to lead a unified board, facilitating its members at its meetings, and to be responsible for ensuring that the principles and processes of the board are maintained in line with the Board Governance document

Agendas for our meetings are agreed in consultation with the Chief Executive and Company Secretary, although any director may request that an item be added to the agenda I have authority to act and speak for the board between its meetings, including engaging with the Chief Executive I report to the board and committee chairmen as appropriate on decisions and actions taken between meetings of the board I also meet with the non-executive directors without the executive directors present, to consider the performance of the executive directors and to provide feedback

Governance
Chairman's letter (continued)

Group Authorisation Arrangements
The Group Authorisation Arrangements (GAA) are the framework through which the Severn Trent Plc board authorises the right people, at the right level, to take important decisions as we manage legal, financial and administrative issues throughout the group The GAA are designed to facilitate good control, efficient decision making and demonstrable compliance

The flow of authority is from the Severn Trent Plc board to the Chief Executive In respect of certain issues, the delegated authority is subject to an obligation to work with specialist business services areas (such as Tax, Treasury, Finance and Company Secretariat) that provide additional expertise and a group wide perspective

Governance of subsidiaries
The board of the listed company, Severn Trent Plc, is the same as that of its subsidiary, Severn Trent Water Limited This structure was implemented in 2007 when it was decided to integrate the management of the companies to gain greater focus, transparency and effectiveness around Severn Trent Water

The two companies operate as distinct legal entities The boards have regard to the Severn Trent Plc Board Governance document and the Severn Trent Water Limited Matters Reserved to the Board They are assisted through the management of separate agendas, meetings and minutes by the Company Secretariat and advised in their meetings by the Company Secretary where appropriate

Subsidiary company boards are required to be managed scrupulously with respect to all legal, fiscal and administrative matters In particular, the relationships between Severn Trent Water Limited and our other businesses such as Severn Trent Services are monitored and controlled to ensure that we comply with our Ofwat obligations on arm's length transactions

Senior independent non-executive director
Richard Davey is the senior independent non-executive director He chairs the Remuneration Committee and is a member of the Audit and Nominations Committees The board has agreed that Richard Davey will act as Chairman of the board in the event that I am unable to do so for any reason

Non-executive directors
Your non-executive directors are appointed to the board to contribute their external expertise and experience in areas of importance to the group such as corporate finance, general finance, corporate strategy, environmental matters, general management and supply chain management They also provide independent challenge and rigour in the board's deliberations and are encouraged to make independent assessments of the group's competencies The non-executive directors, led by Richard as the senior independent non-executive director, meet without me at least once a year, where there is an opportunity for them to appraise my performance

Your board has reviewed the status of the non-executive directors and considers them all to be independent in character and judgement and within the definition of this term in the Combined Code and the UK Corporate Governance Code

Chief Executive
The board has delegated all responsibility beyond its matters reserved to the Chief Executive to achieve the company's strategy The Chief Executive, Tony Wray, is empowered to take all decisions and actions that further the company's strategy and which in his judgement are reasonable, having regard to the Chief Executive limits set out in the company's Group Authorisation Arrangements (GAA)

Executive directors
The executive directors support Tony in driving strategy forward in Severn Trent They are committed to implementing strategy in a responsible way that takes account of our commitment to long term responsible stewardship of the business, the environment, our customers and the communities in which we live and work

Role of the Company Secretary
All directors have access to the advice and services of the Company Secretary, Fiona Smith, and the Company Secretariat team The Company Secretary is responsible for ensuring that the board operates in accordance with the governance framework it has adopted and that there are good information flows to the board and its committees and between senior management and the non-executive directors

Fiona retires from her role at the AGM in July 2011 We wish her a long and happy retirement and on behalf of the board, I offer her our thanks for her services over the past five years

Bronagh Kennedy will succeed Fiona Bronagh is a qualified solicitor and until recently was the Company Secretary and General Counsel at Mitchells and Butlers plc

The appointment and resignation of the Company Secretary is a matter for consideration by the board as a whole

Induction
On joining the board, directors are evaluated and then provided with a comprehensive and individualised induction pack that includes notes on the group structure, the regulatory framework of the operating businesses within the group, financial reports and business plans and information on our governance framework

Meetings are arranged with members of the executive management team and external advisers who provide support to the relevant board committees the directors may serve on Visits to operational and office sites across the group are also arranged for directors joining the board

Shareholders
The board recognises the importance of representing and promoting the interests of its shareholders and that it is accountable to shareholders for the performance and activities of the company

Retail shareholder engagement strategy
The board has an active shareholder engagement strategy, the main elements of which are set out below

The Annual Report and Accounts is the principal means of communicating with shareholders The group adopted e-communications after they were approved by shareholders as an alternative means of receiving company information at the 2007 annual general meeting As at 5 May 2011, 39,723 shareholders receive company communications via electronic methods whilst 28,521 shareholders continue to receive communications by post

The company's website (www severntrent com) contains an archive of annual reports together with other information relevant to investors This includes comprehensive share price information, financial results and financial calendars

The company offers a Dividend Reinvestment Plan (DRIP) Details of the DRIP are available on the company website and the website of Equiniti, our registrar

Further shareholder information can be found on pages 124 to 125

Financial calendar

22 June 2011	Ex-dividend date for 2010/11 final dividend
24 June 2011	Record date for 2010/11 final dividend
20 July 2010	AGM
29 July 2011	Payment date for proposed 2010/11 final dividend
24 November 2011	Announcement date for 2011/12 interim results
13 January 2012	Payment date for proposed 2011/12 interim dividend

Continuing professional development
The directors received updates throughout the year on matters such as the Flood and Water Management Act and the impacts of the proposals on private drains and sewers There was also an opportunity to review and understand the outcomes of an exercise to evaluate our business plan for AMP5

We are creating individual programmes for learning and development The programmes will be reviewed by me with each director as part of the annual performance and effectiveness reviews undertaken by the board

Performance and effectiveness reviews
Last year Sir John Egan, my predecessor as Chairman, carried out an internal review on the effectiveness of the board and its committees The board discussed the outcomes of that review in July 2010 and the outcomes gave me some insights into the operations of the board and its committees that have been helpful to me during my first year as Chairman

July 2011 marks my first full year as Chairman I will commence an external review of the board, committees and the directors in November 2011 and will report back to you on the outcomes of that review in next year's report

Board processes
We have processes in place regarding

- our tasks and activities (board membership and administration),
- the matters specifically reserved for our decision making, the authority delegated to the Chief Executive, the accountability of the Chief Executive for that authority, and guidance on managing the relationship between us and the Chief Executive, and
- the boundaries on Chief Executive action (Chief Executive limits)

An approved Board Governance document outlines those processes and is available on our website (www severntrent com)

The board has reserved the following for its own consideration

- the appointment of the Chief Executive, directors, the Company Secretary and the Director of Internal Audit,
- the strategy and budgets of the company,
- the GAA which set out the group's delegated approval limits,
- decisions regarding the company and its subsidiaries required to be made by the company's GAA, constitutional documents, statute or external regulation, and
- the approval or adoption of documents (including the publication of reports and statements to shareholders), required to be made by the board by the company's GAA, constitutional documents, statute or external regulation

Board meetings
We have regular scheduled meetings throughout the year

Papers, including minutes of board committees held since the previous board meeting and performance reports, are circulated in advance of each meeting

There is an agreed procedure in place which allows directors to take independent professional advice in the course of their duties and all directors have access to the advice and services of the Company Secretary Where a director has a concern over any unresolved matter he/she is entitled to require the Company Secretary to minute that concern Should the director later resign over the issue, I, as Chairman, will bring it to the attention of the board

Governance
Chairman's letter (continued)

Reporting obligations

As a publicly listed company, the company has a range of reporting obligations to meet that are set out by law and regulation The company is committed to the promotion of investor confidence by taking steps within its power to ensure that trade in its securities takes place in an efficient and informed market

The company recognises the importance of effective communication as a key part of building shareholder value and that, to prosper and achieve growth, it must (among other things) earn the trust of security holders, employees, customers, suppliers and communities, by being open in its communications and consistently delivering on its commitments

The company announces its results on a half yearly basis and complies with the requirement to make interim management statements

The Chief Executive has established a Disclosure Committee, chaired by the Finance Director, with specific responsibilities for the delivery of the year end reporting processes The Committee oversees the delivery of an integrated plan incorporating all elements of the year end reporting process, namely the group's final results announcement and report and accounts, the company's AGM, the statutory and regulatory accounts of Severn Trent Water Ltd and the June Return to Ofwat

Board attendance in 2010/11

Sir John Egan	3/3	Martin Kane	7/7
Tony Ballance	7/7	Martin Lamb	6/7
Dr Bernard Bulkin	7/7	Michael McKeon	7/7
Richard Davey	7/7	Baroness Noakes	7/7
Andrew Duff	5/6	Andy Smith	7/7
Gordon Fryett	7/7	Tony Wray	7/7

In addition to the formal board meetings, your board attended two full day strategy sessions this year, where the board and executive management team together considered Severn Trent Services and also the most significant risks facing the company During the financial year, five ad hoc meetings of the board were convened to consider such matters as Severn Trent Plc's preliminary and interim results and interim management statements

Board committees

We have established committees of the board to deal with specific issues or approvals, as and when necessary

The four permanent committees of the board assist in the execution of its responsibilities and the board delegated some of its responsibilities to those board committees The committees assist the board by focusing on their specific activities, fulfilling their roles and responsibilities, reporting to the board on decisions and actions taken, and making any necessary recommendations

The terms of reference of the Audit, Remuneration and Nominations Committees comply with the provisions of the Combined Code and are available for inspection, together with the terms of reference of the Corporate Responsibility Committee, on the company's website (www severntrent com) or may be obtained on written request from the Company Secretary at the address given on the back cover

Each of the committees has reviewed its effectiveness and terms of reference during the year and any necessary actions have been identified and reported to the board

Reports from the Chairmen of these committees are set out on pages 39 to 55 of this report

Terms and conditions of appointment

We have made the terms and conditions of appointment of the directors available for inspection by any person at the company's registered office during normal business hours They will also be available at the AGM The letters of appointment of the directors can also be seen on our website (www severntrent com)

Remuneration

The Directors' remuneration report is set out on pages 43 to 55

Insurance and indemnities

Severn Trent purchases directors' and officers' liability and indemnity insurance to cover its directors and officers against the costs of defending themselves in civil proceedings taken against them in that capacity, and in respect of damages resulting from the unsuccessful defence of any proceedings

Interests

No director had a material interest at any time during the year in any contract of significance with the company or any of its subsidiary undertakings

Institutional shareholders and analysts
Presentations are made to shareholders and analysts following the release of the interim and year end results The Chief Executive and Finance Director meet shareholders during the year The Chairman and, if appropriate, the senior independent non-executive director are available to meet shareholders if required The board receives written feedback following meetings with institutional shareholders and monitors shareholder activity on a quarterly basis at its meetings

In December 2010, 50 people attended the Severn Trent Investor Day, entitled 'Winning in a changing world', hosted by the Chief Executive and Finance Director at our offices in Coventry

Conflicts of interests – update
The board has a full process in place to authorise situational conflicts in accordance with the provisions of the Companies Act 2006

For any actual or potential conflicts, the following procedure has been adopted by the board to consider and, if it sees fit, to authorise situations where a director has an interest that conflicts, or may possibly conflict, with the interests of the company

- the director will notify the Chairman and Company Secretary of the actual or potential conflict,
- the Nominations Committee will consider the notification and determine whether it needs to be proposed to a board meeting for authorisation, and
- the conflict will be considered by the board at a scheduled board meeting

Full details of the conflict will be sent to directors in advance of the meeting If there is a major conflict or it is decided that authorisation should not wait until the next scheduled meeting, the board would be asked to authorise the conflict by way of written resolution

In addition to reviewing any conflicts notified and proposing them for authorisation by the board, the Nominations Committee monitors changes to previously notified conflicts and any conditions imposed Half yearly reports are made to the board of all directors' conflicts and directors are reminded from time to time of their obligations An annual review of conflicts is carried out and this is incorporated into the year end process of verifying directors' interests

Annual general meeting
The AGM of the company will be held at the International Convention Centre, Broad Street, Birmingham B1 2EA at 11am on Wednesday 20 July 2011

The AGM is shareholders' opportunity to feedback to the company on performance, management and the way we work in a very direct fashion – through the way they vote – either in favour of the resolution, against the resolution or by withholding their vote so that it does not count either for or against It is also shareholders' opportunity to meet informally with directors and senior management before and after the meeting and ask formal questions during the meeting

The board encourages shareholders to attend the company's AGM and exercise their right to vote The notice of meeting and related papers are sent to shareholders at least 20 working days before the meeting Separate resolutions are proposed on each substantially separate issue

Presentations are made on the group's activities and performance prior to the formal business of the meeting Shareholders have the opportunity to ask questions of the board and present their views The Chairmen of the Audit, Corporate Responsibility, Remuneration and Nominations Committees, together with all other directors, will attend the AGM

The company uses electronic voting at the AGM, allowing shareholders present at the meeting to register one vote per share held Results of the poll on each resolution, including details of the votes for and against registered prior to and at the meeting, proxy votes and the number of abstentions will be displayed at the meeting

The poll results and a list of questions and answers from the AGM will be made available on our website after the meeting

At the 2010 AGM, over 50 shareholders registered for Severn Trent's Shareholder Networking Programme which took place on 30 March 2011 The aim of the programme is to offer retail shareholders the opportunity to learn more about the company, through a combination of site visits and talking to staff

Governance
Chairman's letter (continued)

The event was hosted by Martin Kane, Director of Customer Relations and a member of the board Twenty participants were taken to Minworth, to our Sewage Treatment Works, for a tour and presentation on renewable energy This was followed by a visit to our new headquarters at the Severn Trent Centre

Positive feedback was given on the organisation and content with strong support for the company continuing the programme, both from shareholders and employees who enjoyed the positive interest shown in their work and their part in explaining what work they did

Your board encourages those shareholders attending the 2011 AGM to register for this year's visit

Reappointment
Under the company's articles of association, all directors are required to retire and submit themselves for appointment or reappointment if they have been appointed by the board since the previous Annual General Meeting or if it is the third Annual General Meeting following that at which they were appointed or last reappointed

However, the UK Corporate Governance Code now requires that all directors of companies in the FTSE 350 index such as the company should be subject to annual election by shareholders Accordingly, the directors will all retire at this year's Annual General Meeting and submit themselves for reappointment by the shareholders

Conclusions
At Severn Trent, we are committed to operational excellence and continuous improvement, supported by good governance We run our business in a manner which is responsible and consistent with our belief in transparency and accountability Good governance is not simply an exercise in compliance For Severn Trent it is a vital aspect forming a foundation for the sustainable growth of the business

I firmly believe that Severn Trent will continue to achieve profitable and sustainable growth for our company through the successful mix of good governance, a clear business plan and strategy and strong management team

Andrew Duff
Chairman

Governance
Nominations Committee

Andrew Duff
Chairman of the Nominations Committee

The main purpose of the Committee is to assist the board by keeping the composition of the board under review and conducting a rigorous and transparent process when making or renewing appointments of directors to the board It also advises the board on issues of directors' conflicts of interest and independence The full terms of reference for the Committee can be found on the company's website (www severntrent com) and are also available from the Company Secretary

Succession planning
When considering new appointments to the board, the Committee oversees the preparation of a position specification that is provided to an independent recruitment organisation retained to conduct a global search In addition to the specific skills, knowledge and experience deemed necessary, the specification contains criteria such as

- a proven track record of creating shareholder value,
- unquestioned integrity and a diversity of psychological mindset,
- a commitment to the highest standards of governance,
- having the required time available to devote to the job,
- strategic mindset, an awareness of market leadership, outstanding monitoring skills,
- a preparedness to question, challenge and openly assess, and
- an independent point of view

This report provides details of the role of the Nominations Committee and the work it has undertaken during the year

The Committee keeps under review the balance of skills on the board and the knowledge, experience, length of service and performance of the directors It also reviews their external interests with a view to identifying any actual, perceived or potential conflicts of interests, including the time available to commit to their duties to the company The Committee monitors the independence of each non-executive director and makes recommendations concerning such to the board The results of these reviews are important when the board considers succession planning and the election and reappointment of directors Members of the committee take no part in any discussions concerning their own circumstances

During the year the Committee reviewed the procedure for reporting and authorising, as appropriate, any actual or potential conflicts of interests, in accordance with the provisions of the Companies Act 2006

The members of the Nominations Committee in 2010/11 were the non-executive directors of the board and the Chief Executive, Tony Wray

In accordance with the requirements of the UK Corporate Governance Code, all members of the board will seek re-election at the annual general meeting in July 2011 In March this year the Nominations Committee formally reviewed the performance, contribution and commitment of each of the directors retiring at this year's AGM and seeking reappointment and supported and recommended their reappointment to the board The Committee has confirmed that each director continues to perform well on an individual and collective basis, making a valuable contribution to the board's deliberations and demonstrating commitment to the long term interests of the company

Nominations Committee attendance in 2010/11

Sir John Egan	2/2
Dr Bernard Bulkin	4/4
Richard Davey	4/4
Andrew Duff	3/3
Gordon Fryett	2/4
Martin Lamb	3/4
Baroness Noakes	4/4
Tony Wray	4/4

Each committee meeting complied with the terms of reference in that a minimum of five members were in attendance, with the majority being independent, non-executive directors

Governance
Audit Committee

Baroness Noakes DBE
Chairman of the Audit Committee

The Committee assists the board in discharging its responsibilities for the integrity of the company's financial statements, the assessment of the effectiveness of the systems of internal controls and monitoring the effectiveness and objectivity of the internal and external auditors The role and the responsibilities of the Committee are set out in written terms of reference These can be found on the company's website (www severntrent com) and are also available from the Company Secretary

This report provides details of the role of the Audit Committee and the work it has undertaken during the year

The members of the Audit Committee are Baroness Noakes DBE (Chairman), Dr Bernard Bulkin and Richard Davey whose experience and background are set out on pages 30 and 31 The board is satisfied that Baroness Noakes and Richard Davey have recent and relevant financial experience and that all members of the Committee remain independent The members of the Committee receive updates in financial reporting and the group's regulatory framework in various forms throughout the year

The Chairman, the Chief Executive, the Finance Director, the Director of Internal Audit, the Director of Strategy and Regulation, the Group Financial Controller, the Company Secretary and the external auditor normally attend, by invitation, all meetings of the Committee Other members of senior management are also invited to attend as appropriate In performing its duties, the Committee has access to the services of the Director of Internal Audit, the Company Secretary and external professional advisers

We met five times in 2010/11 and our work focused on four key areas financial statements and accounting policies, internal controls, oversight of internal and external audit, and the regulatory reporting obligations of our subsidiary Severn Trent Water Limited

Financial Statements and Accounting Policies
Reviewing the financial statements and accounting policies requires us to make certain judgements and we set out below some of the key issues we discussed in respect of 2010/11

- the implementation of accounting standards in the period, in particular IFRIC 18 (in respect of assets transferred from customers)
- the assumptions which underpin accounting for the group's retirement benefits schemes
- the rationale for items shown as exceptional in the accounts

In reviewing the financial statements, we receive input from the Executive Disclosure Committee and Deloitte The former is chaired by the Finance Director and considers the content, accuracy and tone of the financial statements and other public disclosures prior to their release

Deloitte reported to the Committee on their review of the half year interim results and on their audit of the year end financial statements

Internal Controls
We receive regular reports from Internal Audit in respect of their work on internal controls and we review management letters received from the external auditors We review Internal Audit's annual review of fraud prevention and mitigation as well as a regular fraud log

Technology controls and governance were areas of focus in 2010/11 and we received several reports on the control environment in this area, where we had previously identified the potential to enhance controls Much progress has been made in improving the control environment and we will continue to monitor progress into 2011/12

We reviewed the processes for and outputs from our enterprise risk management process, through which the principal risks and related controls are identified In addition, we monitored the ongoing development of our compliance and assurance processes in respect of the key risks

We discussed the new compliance requirement for Senior Accounting Officers to provide certification in respect of the accounting records and processes which underpin the calculation of tax liabilities for UK based companies owned by the group

A programme is under way to ensure the group is in compliance with the UK Bribery Act which is due to become effective in July 2011 We will receive further progress reports in 2011/12

Further details of our Internal Control Framework, including the main features of our internal control and risk management systems in relation to the financial reporting process, can be found in the Directors' Report on page 28

Oversight of Internal Audit and External Audit
We are responsible for overseeing the work of the internal audit function and also for managing the relationship with the group's external auditor We review the performance of

Policy on the provision of non-audit services

The company has approved a formal policy on the provision of non-audit services aimed at safeguarding and supporting the independence and objectivity of the external auditor

The policy sets out the approach to be taken by the group when using the services of the external auditor, including requiring that certain services provided by the external auditor are pre-approved by the Audit Committee or its Chairman

It distinguishes between those services where an independent view is required and that should be performed by the external auditor (such as statutory and non-statutory audit and assurance work), prohibited services where the independence of the external auditor could be threatened and they must not be used, and other non-audit services where the external auditor may be used

Non-audit services where the external auditor may be used include non-recurring internal controls and risk management reviews (i e excluding outsourcing of internal audit work), advice on financial reporting and regulatory matters, due diligence on acquisitions and disposals, project assurance and advice, tax compliance services, and employee tax services

The approval of the Audit Committee or its Chairman is always required if a non-audit service provided by the auditor is expected to cost more than £100,000 or if non-audit fees for the year would thereby exceed the amount of the audit fee

the internal and external auditor annually to ensure that they are effective and recommend to the board whether the external auditor should be reappointed

The Committee regularly holds discussions with both the internal and external auditors in the absence of management The Committee reports to the subsequent meeting of the board on the Committee's work and the board receives a copy of the minutes of each meeting of the Committee

Internal audit

The Director of Internal Audit and his Internal Audit team report on a day to day basis to management on the effectiveness of the group's systems of internal controls and the adequacy of these systems to manage business risk and to safeguard the group's assets and resources This work is summarised and reported to the Audit Committee on a regular basis and is a key element of the assurance that the Committee receives on the risks and controls in the group

The plans, the level of resources and the budget of the Internal Audit function are reviewed at least annually by the Audit Committee The Director of Internal Audit is free to raise any issues with the Committee or its Chairman at any time during the year

External auditor

Deloitte LLP (Deloitte) were appointed auditor of the company in 2005 The Audit Committee reviews the auditor's effectiveness each year prior to recommending to the board that they be proposed for reappointment at the AGM Deloitte audit all significant subsidiaries of the group

Annually, the committee reviews information provided by the external auditor confirming their independence and objectivity within the context of applicable regulatory requirements and professional standards The company does not have a policy of tendering the external audit at specific intervals but would initiate a tender process if there were any concerns about the quality of the audit or the independence and objectivity of the auditor There are no contractual obligations that act to restrict the Committee's choice of external auditor

Details of the amounts paid to Deloitte for audit and non-audit services are provided in note 7 to the accounts page 75

In accordance with the requirements for auditor independence, the lead partner stood down after the 2009/10 audit having served five years in that capacity Our new lead partner observed the 2009/10 audit to ensure continuity following the changeover

Severn Trent Water Limited

The regulated activities carried out by Severn Trent Water Limited result in other reporting requirements to Ofwat and these are also covered by the Audit Committee These regulatory reporting obligations include a comprehensive annual return on all of Severn Trent Water Limited's regulatory obligations, known as the June Return, and a statement that underpins the customer charges made by Severn Trent Water Limited, known as the Principal Statement

Deloitte make reports to Ofwat in respect of the June Return The June Return covers many aspects which are not financial and Severn Trent Water Limited appoints a Reporter, Atkins, to report on those aspects The Audit Committee receives reports from Deloitte and the Reporter on their work as part of its review of the returns

In June 2010, we held an additional meeting to consider and review the new Ofwat reporting requirements regarding the split of operating costs and fixed assets between different activities within Severn Trent Water Limited ('accounting separation')

Audit Committee attendance in 2010/11

Baroness Noakes	5/5
Dr Bernard Bulkin	4/5
Richard Davey	5/5

In April 2010, we conducted an annual review of our performance as part of the annual Board Effectiveness Review process and the board, as a whole, concluded that we continue to operate effectively

Governance
Corporate Responsibility Committee

Dr Bernard Bulkin
Chairman of the Corporate Responsibility Committee

The Committee provides guidance and direction to the group's corporate responsibility (CR) programme, reviews the group's key non-financial risks and opportunities and monitors progress The terms of reference for the Committee can be found on the company's website (www severntrent com) and are also available from the Company Secretary

The Committee reviews annually the group's formal whistleblowing policy that deals with allegations from employees relating to breaches of the Code of Conduct and reviews at each of its meetings the whistleblowing incident log

The purpose of the Corporate Responsibility (CR) Committee is to provide board oversight of the management of all non-financial risks to the group The structure for our CR policy and framework is based around the four areas of Workplace, Marketplace, Environment and Community, providing a common framework for both our businesses – regulated and non-regulated The framework remains under review as we continue to integrate corporate responsibility into our core business operations for both Severn Trent Water and Severn Trent Services For each of the areas, there are four goals within our CR policy which help to focus improvements in our performance

Within our CR framework, we have identified 10 focus areas that are critical to our management of risk and reputation These areas have been determined through stakeholder dialogue, risk assessment and benchmarking within the water industry and the FTSE 100 The 10 areas provide the focus of the forward agenda of our CR Committee

Workplace
Health, safety and wellbeing Employee skills, conduct and motivation. Diversity

Marketplace
Customer needs – including vulnerable customers Supply chain responsibility

Environment
Environmental stewardship Waste reduction and recycling Climate change – mitigation and adaptation

Community
Community engagement. Working with our customers – including pollution prevention and water efficiency

These focus areas also determine our approach to working in collaboration with other organisations who share mutual interests and objectives Further information is available on our corporate website (www severntrent com/corporateresponsibility)

Within Severn Trent Water we have an effective performance management system in place through 18 core business Key Performance Indicators (KPIs) and eight KSIs These are overseen by the Severn Trent Executive Committee and the board Many of the business KPIs relate directly to our CR focus areas and therefore contribute significantly to our CR performance

We report internally on our performance through both our Executive Committee and our CR Committee Externally, we report through a number of channels including our annual June Return (our regulatory submission to Ofwat), our websites and our Annual Report and Accounts

The members of the Corporate Responsibility Committee are Dr Bernard Bulkin (Chairman), Gordon Fryett and Tony Wray

Corporate Responsibility Committee attendance in 2010/11

Dr Bernard Bulkin	3/3
Gordon Fryett	3/3
Tony Wray	3/3

Governance
Remuneration Committee

This report sets out the remuneration policy for the directors of Severn Trent Plc and discloses the amounts paid to them in the year ended 31 March 2011

The report is subject to a shareholder vote and a resolution to approve this Directors' remuneration report will be proposed at the AGM The report has been prepared in accordance with the requirements of the Companies Act 2006, the principles of the Combined Code on Corporate Governance and best practice guidelines

During the year, the Committee undertook a thorough review of the variable arrangements for the executive directors and other members of the Severn Trent Executive Committee This review included an examination of both the quantum and structure of the variable pay arrangements and the measures used to assess performance The conclusions of this review were as follows

- The Committee determined that the structure of awards (cash bonus, deferred share bonus with matching and long term incentive plan awards) remained appropriate and the significant proportion of variable pay delivered in shares provided a strong alignment between the interests of management and shareholders
- The quantum of rewards remains competitive and no changes were proposed to current award levels
- The performance measures and weighting of the targets for the annual bonus plan (Severn Trent Water KPIs, personal performance and Severn Trent Services performance for the Chief Executive and Finance Director) continue to provide a strong and challenging assessment of the financial and operating performance of the business The annual bonus will therefore continue to operate on the same basis for 2011/12, save that Severn Trent Water performance will be measured by reference to 20 rather than 18 KPIs
- Relative TSR remains an appropriate measure of performance for the Share Matching Plan, providing alignment with the returns received by shareholders In the absence of a sufficient number of listed utility companies, the current FTSE 51-150 comparator group is considered the most relevant benchmark for measuring performance However, to address the share price volatility caused by the uncertainty of the five year pricing review, rather than measuring performance over a single three year period, a multi-point measurement basis will be applied to future grants (20% over 0-18 months, 30% over 0-27 months and 50% over 0-36 months) The awards will continue to be subject to the Committee being satisfied with the financial performance over the performance period and, further, there being no compromise to the commercial integrity of Severn Trent over the performance period This approach should reduce the impact of price uncertainty in the run up to new asset management periods and reward for sustainable and steady shareholder returns
- To provide a stronger focus on the long term financial performance of the business, future awards under the Long Term Incentive Plan (LTIP) will be subject to a performance measure based on the company's return on regulatory capital value (RoRCV) compared to the Ofwat Final Determination (current awards under this plan are subject to a relative TSR performance condition) RoRCV was chosen as the measure of performance because it directly targets management's delivery of the business plan For awards granted in 2011, 0% of the shares will vest if RoRCV equals the Final Determination, increasing on a straight line basis to 50% vesting if RoRCV exceeds the Final Determination by 2% p a and 100% vesting for outperformance of 7% p a or more Performance will be based on the average RoRCV over three financial years, starting in the year in which the award is granted Further details on the performance measure for the 2011 award are set out on page 48

The Committee believes that the new performance measures for the Share Matching Plan and Long Term Incentive Plan will provide a more rounded assessment of the overall financial and operational performance of the business and will provide a clearer line of sight for executives between performance and reward

Richard Davey
Chairman of the Remuneration Committee

The Committee assists the board by focusing on the activities detailed below, reporting to the board on decisions and actions taken, and making any necessary recommendations

- the remuneration policy and its application to the Chief Executive and executives reporting to the Chief Executive,
- the adoption of annual and longer term incentive plans,
- determination of levels of reward to the Chief Executive and approval of reward to executives reporting to the Chief Executive,
- setting the Chairman's fee, and
- the communication to shareholders on remuneration policy and the Committee's work on behalf of the board

The full terms of reference for the Committee can be found on the company's website (www severntrent com) and are also available from the Company Secretary

Governance
Remuneration Committee (continued)

Remuneration Committee
The Committee determines, on behalf of the board, the company's policy on the remuneration of executive directors, other members of the Executive Committee and the Chairman of the board The Committee determines the total remuneration packages and contractual terms and conditions for these individuals The policy framework for remunerating all senior executive managers is consistent with the approach taken for executive directors

The Committee is comprised exclusively of independent non-executive directors of the company, with the exception of Andrew Duff, the company Chairman, who was independent on his appointment to the board

The members of the Committee during the year were Dr Bernard Bulkin, Richard Davey (Committee Chairman), Andrew Duff, Sir John Egan and Martin Lamb

Remuneration Committee attendance in 2010/11	
Richard Davey	4/4
Andrew Duff (appointed to the Committee 20 July 2010)	3/4
Dr Bernard Bulkin	3/4
Sir John Egan (retired from the Committee 20 July 2010)	1/1
Martin Lamb	4/4

With the exception of the company Chairman, the Committee members have no personal financial interest, other than as shareholders, in the matters to be decided As company Chairman, Andrew Duff's fees are set by the Committee but he is not party to this discussion In setting performance related remuneration, the Committee has regard to the provisions set out in Schedule A to the Combined Code

Advisers
To ensure that the company's remuneration practices are market competitive, the Committee has access to detailed external research on market data and trends from experienced specialist consultants

Hewitt New Bridge Street (a trading name of Aon Corporation) is the independent advisor to the Committee Neither Hewitt New Bridge Street nor any other part of the Aon Corporation provided other services to the company during the year

The Chief Executive (Tony Wray), the Human Resources Director (Alec Luhaste until December 2010, Evelyn Dickey thereafter) and the Reward and HR Systems Manager (Marilyn Gillert) also attended the Committee meetings to provide advice and respond to specific questions Such attendances specifically excluded any matter concerning their own remuneration The Company Secretary, Fiona Smith, acts as secretary to the Committee

Remuneration Committee activity
During the year ended 31 March 2011, the Committee met four times to discuss the key remuneration issues arising, the operation of the remuneration policy and the market updates by its advisers The following table sets out what the Committee covered at each of the meetings over the course of the year

Date	Key agenda items
May 2010	Agree the vesting results for the 2009/10 annual bonus scheme and the 2007 LTIP awards Approve the incentive plan targets for the 2010/11 annual bonus scheme (including personal performance targets) and the 2010 LTIP awards Approve the 2010 Directors' Remuneration Report
November 2010	Strategic review of the annual bonus plan and LTIP (including performance metrics) Update on executive pension provision
January 2011	Review of salaries and benefits for 2011 for the executive directors and other senior executives Consider proposed changes to the annual bonus plan and LTIP Review of the executive directors shareholding requirements
March 2011	Incentive plan performance update Review of good leaver plan statements

Remuneration policy
Each year, the Committee reviews the remuneration policy for executive directors and other senior executive managers, taking into account both the external market and the company's strategic objectives over the short and the medium term

The company's continuing remuneration policy for executive directors is to provide remuneration in a form and amount which will attract, retain, motivate and reward high calibre individuals The remuneration package is based on the following principles

Principle	Rationale
Incentives are aligned with the interests of shareholders and seek to reward the creation of long term value	Executives must be adequately focused on the long term strategy and make decisions that lead to the creation of long term value
Reward elements are designed to reinforce the link between performance and reward Performance related elements should form a significant proportion of the total remuneration package and typically comprise at least 50% of total remuneration, if paid at the maximum	The performance of the business is key and the package should be appropriately geared towards performance related pay
The total remuneration package for on target performance should be fully competitive, but not excessive, in the relevant market	The Committee wishes the executives to be appropriately remunerated for the challenges they face and ensure that the right structure and levels are in place to take the business forward
Packages are structured flexibly to meet critical resource needs and retain key executives	Package flexibility allows the Committee to take decisive action with issues of recruitment and retention in the best interests of business continuity and shareholder value

The charts below show, as a proportion of the package, firstly, the expected values of salary, bonus and long term incentives for target performance and, secondly, the maximum values of salary, bonus and long term incentives for the executive directors based on the proposed remuneration policy for 2011/12 The Committee considers the mix between fixed and performance related pay to be appropriate

The Committee takes seriously the issue of balancing risk and reward During the year, the Committee undertook a detailed review of the variable pay arrangements for the executive directors and other members of the Executive Committee The Committee concluded that the schemes were appropriately managed and the choice of performance measures and targets did not encourage undue risk taking by the executives The schemes incorporate a range of internal and external performance metrics, measuring both operational and financial performance providing a rounded assessment of overall company performance The Committee retains ultimate approval for the executive incentive schemes and all share plans across the company and has the final discretion as to how they are applied Furthermore, the rules of the annual bonus scheme and long term incentive schemes provide that the Committee may reclaim ('clawback') some or all of the after tax part of any award to executive directors if it transpires that the award was based on calculations which are subsequently demonstrated to be materially incorrect

Personal shareholdings
The company operates shareholding guidelines under which executive directors are expected to build and maintain a minimum holding of shares in the company The Chief Executive is expected to build and maintain a holding of shares to the value of 1 5 x base salary and other executive directors 1 x base salary Executive directors are expected to retain at least half of the shares they receive through the Long Term Incentive Plan and other share based plans until they meet the guideline holdings Details of the current shareholdings of the executive directors are set out on page 52

External directorships
Executive directors are permitted to take on external non-executive directorships, though normally only one other FTSE 100 appointment In order to avoid any conflicts of interest, all such appointments are subject to the approval of the Nominations Committee Executive directors are normally only permitted to retain the fees arising from one such appointment

Michael McKeon was appointed as a non-executive director of The Merchants Trust Plc on 1 May 2008 and in respect of the appointment for the year ended 31 March 2011 he was paid fees of £20,115 He has retained these fees in accordance with the above policy

No other executive directors currently hold any external fee earning non-executive directorships

Base salaries and benefits
Base salaries for individual directors are reviewed annually by the Committee and take effect from 1 July Salaries are set with reference to individual performance, experience and contribution, together with developments in the relevant employment market (having regard to the market median for similar roles in publicly quoted companies of a comparable size and practice in other water companies) and internal relativities

The Committee gives due consideration to the current economic climate and current market practice regarding executive salary reviews and the broader employee salary review policy at the company The Committee has not set a specific policy on the relationship between executive directors' pay and that of the rest of the workforce but aims to pay all employees fairly, taking into account their respective roles and responsibilities

With this in mind, the Committee adopted a policy of a zero increase for the base salaries of the executive directors in 2009/10 and a 2% increase in 2010/11 Against a backdrop of economic recovery, it has chosen to adopt a general policy of 3% increase for the base salaries of the executive directors in 2011/12 This is in line with the policy of all employees of a 3% increase for base salaries

At the time of the Chief Executive's appointment, his salary reflected the fact that he was new to the role and, accordingly, the Committee gave a commitment to review his performance each year and if appropriate increase the base salary over time to align it with the market median The Committee agreed that the Chief Executive's base salary should be reviewed again this year Giving due consideration to the performance of the company and the individual and the internal relativity with the other executive directors and market alignment, the Committee agreed that the Chief Executive's base salary will be increased from £500,000 to £550,000 on 1 July 2011

The non-salary benefits for executive directors comprise

- a car allowance
- private medical insurance
- life assurance
- an incapacity benefits scheme

Private medical insurance and some other benefits may be flexed under the company's flexible benefits scheme

Governance
Remuneration Committee (continued)

Remuneration arrangements for executive directors

The remuneration arrangements for the executive directors comprise the following elements

- Base salary and benefits
- Annual bonus scheme
- Long Term Incentive Plan (LTIP) and Share Matching Plan (SMP)
- Pension

Details of each of the above elements follow but the table below summarises the proposed packages of each of the executive directors

Component	Tony Wray Chief Executive	Michael McKeon Finance Director	Tony Ballance Director, Strategy and Regulation	Martin Kane Customer Relations Director	Andy Smith Director of Water Services
Base salary from 1 July 2011	£550,000	£446,500	£202,100	£220,600	£262,600
On target bonus (% of salary)	60%	60%	60%	60%	60%
Maximum bonus (% of salary)	120%	120%	120%	120%	120%
% of bonus earned deferred into shares	50%	50%	50%	50%	50%
LTIP award (% salary)	70%	50%	50%	50%	50%
SMP award – ratio of matching shares to deferred shares	0 5 1	0 5 1	0 5 1	0 5 1	0 5 1
Pension arrangement	Final salary occupational scheme	Cash allowance	Defined contribution scheme	Cash supplement	Final salary occupational scheme
Benefits	A car allowance, private medical insurance, life assurance and an incapacity benefits scheme				

Annual bonus scheme

Executive directors are eligible for annual bonuses to encourage improved performance, with targets established by the Committee to align executive directors' interests with shareholders The annual bonus opportunity for all the executive directors is 120% of salary For the achievement of target performance (which requires satisfaction of challenging goals), 60% of salary could be earned

The following charts show how the annual bonus metrics are weighted for the executive directors

The bonus outturn in respect of Severn Trent Water performance was operated by reference to a balanced scorecard of measures, based on the 18 KPIs The Committee believes that the use of the Severn Trent Water KPIs continues to be both an effective and challenging annual bonus metric and meets the needs of the business The bonus entitlement was determined by reference to the aggregate number of points awarded across all the KPIs The targets taken together are considered by the board to have an impact on the longer term financial performance of the company and a number of them are reported to Ofwat

The table below shows the points awarded by the Committee for bonus purposes under each of the 18 KPIs in relation to the 2010/11 annual bonus scheme Four of the 18 KPI points have been adjusted upwards This was only done after detailed consideration and in making this decision we recognised that management had done the right thing when faced with exceptional operational challenges over the winter period They also maintained overall financial performance As a consequence the bonus awarded for the Severn Trent Water portion of the annual bonus was 40 0% of its bonus element maximum

The Chief Executive and Finance Director have 10% of their bonus linked to the performance of Severn Trent Services Performance is measured against the profit before interest and tax (before exceptional items) of Severn Trent Services, a measure which is a fully disclosed KPI of the Severn Trent Services business, as shown in the Business review section Performance is measured against budgeted profit, reflecting the desired growth of Severn Trent Services, subject to adjustment by the Committee based on its assessment of overall performance of the business Severn Trent Services performance over the year did not reach its target and therefore resulted in a bonus award of 0%

In addition, each director has 10% of their bonus opportunity measured against a set of personal performance metrics The metrics for 2010/11 include

- supporting the business change and transformation process – focusing on the ongoing improvements to optimise the performance of the business (e g process improvements, technology and systems to support the processes and location, training and development of people to operate in the new environment), and
- developing people – focusing on the individual's contribution to ensuring that the talent management processes help to develop future leaders and therefore support succession planning and business continuity

Half of any bonus paid is deferred into shares to be held for three years following payment If the executive is summarily dismissed without notice under his/her employment contract then the deferred bonuses are forfeited In all other cases of cessation of employment the deferred bonus is not lost and the shares automatically vest on the dealing day after the cessation of employment

The rules of the annual bonus scheme provide that the Committee may reclaim ('clawback') some or all of the after tax part of any bonuses awarded to executive directors if it transpires that the bonus calculation was based on calculations which are subsequently demonstrated to be materially incorrect

KPI 1	Lost time incidents	KPI 8	First time job resolution	KPI 15	Pollution incidents
KPI 2	Employee motivation	KPI 9	Non-performance of regulatory obligations	KPI 16	Sewer flooding incidents
KPI 3	Water quality	KPI 10	Capex versus Final Determination	KPI 17	Sewage treatment works - failing consents
KPI 4	Customer written complaints	KPI 11	Capex process quality (not measured for bonus)	KPI 18	Supply availability
KPI 5	First time call resolution for billing	KPI 12	Debtor days	KPI 19	Net energy use
KPI 6	Unplanned interruptions	KPI 13	Opex	KPI 20	Leakage Ml/d
KPI 7	Properties at risk of low pressure	KPI 14	Ofwat efficiency billing factor (not measured for bonus)		

For the purpose of the annual bonus calculation KPIs – Ofwat efficiency billing factor and capex process quality are not included

Governance
Remuneration Committee (continued)

Annual bonus payments to executive directors are not pensionable

The Committee has reviewed the operation of the plan and concluded that it should operate on the same basis for 2011/12 However, for 2011/12 Severn Trent Water performance will be measured by reference to 20 KPIs as set out on page 47

Long term incentives
As disclosed on page 43, the Committee undertook a thorough review of the incentive arrangements during the year and determined that some changes should be made to the operation of the long term incentive schemes to encourage a greater focus on operational performance and to provide a fairer method of assessing performance In this section, we set out details of both the long term incentives in place for the year under review and the proposed long term incentive arrangements for 2011/12 and beyond

During the year under review, the executive directors participated in two long term incentive schemes (i) a Long Term Incentive Plan and (ii) a Share Matching Plan

a) Long Term Incentive Plan
The Long Term Incentive Plan (LTIP) was approved by shareholders at the 2005 AGM Under the LTIP, annual conditional awards of performance shares may be made to executive directors and senior staff, up to an annual maximum limit of shares worth 125% of base salary In 2010, a share award equivalent to 70% of salary was made to the Chief Executive and 50% of salary to the other executive directors

The number of shares subject to an award will be increased to reflect dividends paid through the performance period on the basis of such notional dividends being reinvested at the then prevailing share price Awards will normally vest as soon as the Committee determines that the performance conditions have been met provided that the participant remains in employment at the end of the performance period

Vesting of awards granted under the LTIP since 2006 has been subject to TSR performance, measured relative to those companies ranked 51–150 in the FTSE by market capitalisation (excluding investment trusts) 25% of awards vesting at median performance, and 100% vesting for performance in the upper quartile In addition, for awards to vest, the Committee must be satisfied that the company's TSR is reflective of the company's underlying performance This is the same performance condition as applying to the awards granted in 2010 under the Share Matching Plan

At the end of the performance period for each award, the TSR performance condition will be measured and independently verified by Hewitt New Bridge Street on behalf of the Committee

As disclosed on page 43 of this report, during the year the Committee undertook a review of the variable pay arrangements for executives and determined to change to the performance targets applying to future LTIP awards to provide a stronger alignment between the long term financial and operational performance of the group and the rewards delivered to management

Vesting of awards granted in 2011 and beyond will be based on return on regulatory capital value (RoRCV), with a sliding scale of targets linked to outperformance of the Ofwat Final Determination

The targets for awards granted in 2011 will be as follows

Severn Trent average annual RoRCV outperformance against the Ofwat Final Determination expectation	Vesting level for performance shares
Less than or equal to Final Determination (≤100%)	0%
102%	50%
107% or higher	100%

Performance will be measured over the three financial years ending 31 March 2012, 2013 and 2014 The Committee reserves the discretionary power to change the result if it is 0% or greater than 50% If it is greater than 50% it can reduce the vesting to not less than 50% If it is 0% it can increase the vesting to not more than 50% The use of this discretion is expected to be exceptional, but may be invoked by the Committee in order to take into account of any of the following factors (not an exhaustive list)

- Actual RPI compared to the Ofwat assumed RPI figure – even though the regulatory capital value is adjusted each year for RPI a significant swing in inflation during the year can result in substantial under or over performance on the return on regulatory capital value target
- Changes to the financing of the company as approved by the board during the performance period – for example a significant change to the level of gearing of the balance sheet would result in partially meeting this performance condition
- Policy changes that occur during the performance period – there is much discussion on the future shape of the water industry in the UK and if enacted we would wish to ensure that any changes have a neutral impact on existing awards

b) Share Matching Plan
Under the Share Matching Plan executives can receive up to one matching share for each share deferred under the annual bonus plan For awards made in 2010 (the first set of awards granted under the plan), the ratio was limited to 0 5 matching share for each deferred share The performance condition requires the company's TSR to be measured relative to those companies ranked 51–150 in the FTSE Index by market capitalisation (excluding investment trusts) This is considered to be the most suitable comparator group since the number of comparable regulated utilities against which to compare the company's performance remains too small to enable meaningful analysis The FTSE 51–150 comparator group allows for the company's performance to be measured against a broader market without any one sector overly impacting the group 25% of the matching awards will vest at median performance and 100% will vest for performance in the upper quartile In addition, for awards to vest, the Committee must be satisfied that the TSR is reflective of the company's underlying performance This replicates the LTIP performance condition for the 2010 awards

As with the LTIP, the number of shares subject to an award will be increased to reflect dividends paid through the performance period on the basis of such notional dividends being reinvested at the then prevailing share price Awards will normally vest as soon as the Committee determines that the performance conditions have been met provided that the participant remains in employment at the end of the performance period

After careful review, the Committee concluded that relative TSR remains the most appropriate performance measure for the Share Matching Plan since it provides alignment between the rewards received by management and the returns received by shareholders The FTSE 51-150 comparator group will be retained and the same vesting schedule will apply (25% vesting at median performance, increasing on a straight line basis to 100% vesting for performance in the upper quartile) However, rather than measure performance over a single three year period, the Committee concluded that for future awards performance would be measured on a multi-point basis (20% over 0-18 months, 30% over 0-27 months and 50% over 0-36 months) The awards will continue to be subject to the Committee being satisfied with the financial performance over the performance period and, further, there being no compromise to the commercial integrity of Severn Trent over the performance period

The Committee has the authority to reclaim ('clawback') some or all of the after tax part of any shares awarded to executive directors under the Long Term Incentive Plan and Share Matching Plan and if it transpires that the vesting calculation was based on calculations which are subsequently demonstrated to be materially incorrect

Performance graph
This graph shows the value, by 31 March 2011, of £100 invested in Severn Trent Plc on 31 March 2006 compared with the value of £100 invested in the FTSE 100 Index The FTSE 100 was chosen as the comparator because the company is a constituent of that index The intermediate points show the value at intervening financial year ends

Below board remuneration
In 2010/11 there were fifteen executives immediately below board level who were paid salaries of between £100,000 and £300,000 per annum

Salary £000	Number of executives
100–150	10
151–200	2
201–250	1
251–300	2

The below board level executives also participate in the same incentive arrangements as the executive directors, albeit at lower award levels

All employee share plans
Through a variety of share schemes, employees are encouraged to hold shares in the company

This includes an all employee Share Incentive Plan Awards are currently made which include a performance condition based on the award of points for the KPIs Employees of Severn Trent Plc and Severn Trent Water Limited participate in the plan For the year 2010/11, awards of shares to the value of £300 will be made to all eligible employees

The company also offers an all employee HMRC approved SAYE plan on an annual basis and periodically reviews the use of other all employee incentive vehicles

Hedging of awards
Details of the company's shares that are held in trust on behalf of participants of certain of the employee share schemes are given on pages 53 and 54 In respect of the LTIPs, deferred share awards (under the Annual Bonus Scheme) and the Share Matching Plan the company's policy is to purchase, and hold in trust, 50% of the total number of shares that could potentially vest from all outstanding awards The requirement to purchase shares is calculated, and the purchase carried out, shortly after each annual award

In respect of awards made under the company's Share Incentive Plan, all the shares taken up by employees at each invitation are normally purchased and placed in trust immediately

The company grants SAYE options over unissued shares, always operating within the dilution limits contained in the scheme rules

The Committee is satisfied that the overall dilution limits provide sufficient headroom for all the company's share schemes

Pensions
Severn Trent Executives receive retirement benefits from a variety of pensions arrangements including defined benefit, defined contribution, payments made direct to personal plans and cash in lieu As a result of the changes in pension legislation for high earners, Severn Trent will introduce the following options from April 2011 for any individuals who are affected by the tax changes

For defined contribution members

- Continue in the scheme and meet any tax liabilities as they fall due, or
- Continue in the scheme up to the Annual Allowance (£50,000 for 2011/12 tax year) and receive a cash alternative (equivalent to the level of employer contributions made to the scheme) above the Annual Allowance

For defined benefit members

- Continue in the scheme and meet any tax liabilities as they fall due
- Opt out of future defined benefit accrual and join the defined contribution section with the same options as above

Of the current executive directors, Andy Smith and Tony Wray participate in the Severn Trent Pension Scheme The scheme is a funded HMRC registered final salary occupational pension scheme which provides

Governance
Remuneration Committee (continued)

- a normal retirement age of 60 years,
- an overall pension at normal retirement age of two thirds of final pensionable salary, which for executive directors is defined as base salary only, subject to the completion of 20 years' pensionable service,
- life cover of 4 x pensionable earnings,
- a pension payable in the event of retirement on grounds of ill health, and
- a dependant's pension on death of two thirds of the member's pension

Andy Smith and Tony Wray participate up to the level of the scheme specific earnings cap which in 2010/11 was £129,600 They are provided with a cash supplement in lieu of pension entitlement above this scheme cap at 40% of their respective salaries

Members' contributions are payable at the rate of 6% of pensionable earnings Early retirement is available after the age of 55 with the consent of the company Any pension would be subject to a reduction that the Trustees consider appropriate, acting on actuarial advice, to reflect the expected longer payment of the pension In the event of incapacity, early retirement is available on an unreduced basis allowing for pensionable service to age 60

Under the Trust Deed and Rules, pension payments in excess of any Guaranteed Minimum Pension are guaranteed to increase in line with price inflation subject to a maximum of 5% each year In the calculation of individual cash equivalent transfer values, allowance is made for such increases

It is the policy of the Committee to offer new executives an allowance, expressed as a percentage of base salary, to fund their own pension provision The individual is able to choose whether the allowance is paid to the company's registered defined contribution scheme, taken as cash or paid to a personal pension arrangement This reflects the wish of the committee to remove future exposure to defined benefit schemes for senior executives These arrangements apply to Michael McKeon at 40% of base salary

Martin Kane is a member of the Severn Trent Pension Scheme (WPS Section) but opted out of the scheme in June 2007 He receives a cash supplement of 30% of his basic salary in lieu of accrual for future service from that date While he no longer accrues additional years of service for pension purposes, consistent with the legislation, Martin Kane's accrued benefits generally continue to be linked to his final salary (or £161,000 plus RPI from 30 June 2007 to the date of his retirement, if higher) and scheme benefits are preserved in relation to ill health, retirement and death in service The normal retirement age for the scheme is 65 although early retirement is possible prior to age 65 with the consent of the company, but any benefits relating to service accruing after 1 December 2006 would be subject to an actuarial reduction

Tony Ballance is a member of the Severn Trent Pension Scheme (Pension Choices section) which is the company's defined contribution scheme He currently contributes 3% of salary and the company contributes at 30%, plus a further 2 5% in respect of death in service and ill health benefits The normal retirement age for the scheme is 65 although retirement prior to 65 is possible with the consent of the company

Directors' service agreements and letters of appointment
A model service contract was approved by the Committee in 2004 and updated during 2007/08 The main terms of the contracts are summarised in the table below

Provision	Policy		
Notice period	12 months from either party		
Termination payment	Maximum payment in the case of redundancy or termination in breach of the agreement by the company of up to and capped at 175% of base salary which is calculated as a conservative estimate of the value of salary, fixed benefits and on target bonus Any payment will not include amounts in respect of awards which have been made under the company's Long Term Incentive Plan over which the Committee retains discretion		
Mitigation	Any termination payment will not be made automatically but will be subject to both phasing and mitigation unless, in the circumstances, the Committee considers it appropriate to achieve a clean break through payment of a lump sum, in which case it will require some discount for early payment		
Change of control	There are no specific contractual payments or benefits which would be triggered in the event of a change in control of the company		
Contract dates	Executive directors	Date of agreement	Effective date
	Tony Wray	20 May 2008	7 March 2005
	Michael McKeon	6 December 2005	13 December 2005
	Tony Ballance	2 June 2008	23 July 2005
	Martin Kane	2 June 2008	30 September 1975
	Andy Smith	2 June 2008	1 January 2005

The Committee believes that the contracts provide as much scope as is feasible to protect the interests of shareholders when negotiating a termination, at which time it would address the duty of mitigation

The Committee recognises that, in line with current best practice guidelines, any termination payment should be based upon an estimate of salary and fixed benefits only Accordingly, the Committee will adopt this policy in the service agreements of future executive directors

In accordance with the UK Corporate Governance Code, all the directors are subject to reappointment as directors at the forthcoming AGM

Chairman and other non-executive directors
The remuneration policy for non-executive directors, other than the Chairman, is determined by the board, within the limits set out in the articles of association

Remuneration for non-executive directors, other than the Chairman, comprises an annual fee for acting as a non-executive director of the company and additional fees for the senior independent director and chairmanship or membership of the committees

The annual fee, last increased in 2010, is £43,350 The additional fees, unchanged since 2008 are as follows

	Senior independent director	Audit Committee Chairman	Audit Committee Member	Remuneration Committee Chairman	Remuneration Committee Member	Corporate Responsibility Committee Chairman	Corporate Responsibility Committee Member	Nominations Committee
Additional fee per annum	£10,000	£15,000	£3,000	£15,000	£3,000	£10,000	£3,000	No fee paid

The Chairman receives a fee of £250,000 per annum He does not receive any additional fees for committee memberships He does not participate in any of the company's pension arrangements, share or bonus schemes

The board does not require directors to take a proportion of their fees in shares and, instead, leaves decisions regarding the holding of shares to individual non-executive directors

Non-executive directors do not participate in share or bonus schemes, nor is any pension provision made

Non-executive directors normally serve three terms of three years They do not have service contracts but their terms of engagement are regulated by letters of appointment, details of which are shown below

Chairman and non-executive directors	Initial appointment	Current appointment	Current expiry date*
Sir John Egan (Chairman – retired)	1 October 2004	1 January 2008	–
Dr Bernard Bulkin	1 January 2006	1 January 2009	31 December 2011
Richard Davey	1 January 2006	1 January 2009	31 December 2011
Andrew Duff (Chairman)	10 May 2010	10 May 2010	9 May 2013
Gordon Fryett	1 July 2009	1 July 2009	30 June 2012
Martin Lamb	29 February 2008	22 February 2011	28 February 2014
Baroness Noakes	29 February 2008	22 February 2011	28 February 2014

* subject to the requirements of the company's articles of association for the reappointment of directors at AGMs

All of the directors are subject to reappointment as directors at the 2011 AGM

The text and tables that follow comprise the auditable part of the Directors' remuneration report, being the information required by the UKLA Listing Rules 9 8 6 and 9 8 8

Directors' emoluments	Basic salary and fees Cash £000	BIKs £000	Annual bonus[1] £000	Other[2] £000	**Total 2010/11 £000**	Total 2009/10 £000
Chairman and other non-executive directors						
Sir John Egan (Chairman – retired)	76 1	–		4 5	80 6	262 5
Dr Bernard Bulkin	59 4	–	–	0 0	59 4	58 6
Richard Davey	71 4	–	–	0 1	71 5	70 6
Andrew Duff (Chairman)	224 2	–	–	–	224 2	–
Gordon Fryett	46 4	–	–	–	46 4	34 1
Martin Lamb	46 4	–	–	–	46 4	43 1
Baroness Noakes	58 4	–	–	0 3	58 7	57 5
Executive directors						
Tony Ballance	190 2	3 3	103 6	15 0	312 1	291 5
Martin Kane	213 3	3 1	118 2	79 0	413 6	411 3
Michael McKeon	430 9	5 6	218 5	15 1	670 1	701 8
Andy Smith	252 8	3 7	133 1	67 1	456 7	470 2
Tony Wray	486 2	6 3	252 0	160 6	905 1	878 1
	2,155 7	22 0	825 4	341 7	3,344 8	3,279 3

1 The directors receive 50% of their bonus in cash and 50% is deferred into shares to be held for three years

2 Other emoluments include expenses chargeable to income tax, car allowances, travel allowances, telephone allowances, payments made under the group's flexible benefits arrangements and amounts paid in lieu of pension contributions Included in other emoluments are

- Sir John Egan car allowance £4,545
- Dr Bernard Bulkin expenses £41
- Richard Davey expenses £69
- Baroness Noakes expenses £301
- Tony Ballance flexible benefits payments £983 and car allowance £15 000
- Martin Kane pension supplement £63,945, flexible benefits payments £126 car allowance £15,000 and expenses £12
- Michael McKeon car allowance £15 000 and expenses £113
- Andy Smith pension supplement £52,060, car allowance £15,000
- Tony Wray pension supplement £145,560 and car allowance £15 000

Governance
Remuneration Committee (continued)

Directors' pension provisions

Name	Service completed in years (including transferred in service credits)	Accrued pension at 31 March 2011 £pa	Increase in accrued pension during the year £pa	Increase in accrued pension during the year (net of inflation) £pa	Transfer value of accrued pension at 31 March 2011 £000	Transfer value of accrued pension at 31 March 2010 £000	Increase/ (decrease) in transfer value over the year, net of directors' contributions £000
Andy Smith	6	25,736	4,120	2,931	434 2	328 9	97 9
Tony Wray	6	25,002	4,120	2,971	404 8	303 7	93 7
Martin Kane	35	126,829	5,593	(1,075)[1]	2,000 6	1,751 2	249 4

Name	Accrued pension at 31 March 2011 £pa	Increase in accrued pension during the year £pa	Increase in accrued pension during the year (net of inflation) £pa	Transfer value of accrued benefits net of directors contributions £000
Andy Smith	25,736	4,120	2,931	62 1
Tony Wray	25,002	4,120	2,971	59 3
Martin Kane	126,829	5,593	(1,075)[1]	88 5

Notes

Relevant directors confirmed by Severn Trent Plc

Accrued pension figures and transfer value calculations provided by Towers Watson

There have been no changes to the transfer value basis since last year s disclosures

Allowance has been made for changes in market conditions over the year by applying the relevant Market Value Adjustment

Inflation figure used in respect of year is to February 2011 (5 5%) as the latest available figure prior to the year end

1 Martin Kane has an increase in accrued pension from £121 236 to £126 829 equating to 4 6% inflation level used (February 2011) is 5 5% producing a negative net of inflation figure Therefore the benefit increase is due to a change in salary not from additional accrual earned over the reporting period

The following contributions were paid to defined contribution pension arrangements in respect of directors

Name	2011	2010
Tony Ballance	£67,175	£59,640
Michael McKeon	£172,550	£170,000

Directors' share interests

The directors of the company at 31 March 2011 and their beneficial interests in the shares of the company were as follows

(i) Beneficial holdings

	At 1 April 2010 (or date of appointment if later) Number of ordinary shares of 97 17/19p each	At 31 March 2011 Number of ordinary shares of 97 17/19p each	At 23 May 2011 Number of ordinary shares of 97 17/19p each
Chairman and other non-executive directors			
Dr Bernard Bulkin	554	554	554
Richard Davey	588	588	588
Andrew Duff (Chairman)	–	3,500	3,500
Martin Lamb	3,012	3,012	3,012
Baroness Noakes	4,018	4,018	4,018
Gordon Fryett	1,000	1,018	1,018
Executive directors			
Tony Ballance	2,032	3,149	3,149
Martin Kane[1]	8,189	9,699	10,013
Michael McKeon	67	4,231	4,231
Andy Smith	5,217	7,516	7,516
Tony Wray	7,057	10,158	10,158

Notes

1 Martin Kane acquired 314 shares on 5 May 2011 following the exercise of his 2008 three year Sharesave scheme option

(ii) Long Term Incentive Plan

The executive directors have further interests in the company's ordinary shares of 97 17/19p each by virtue of having received contingent awards of shares under the Severn Trent Plc Long Term Incentive Plan (LTIP) The LTIP operates on a three year rolling basis The Severn Trent Employee Share Ownership Trust is operated in conjunction with the LTIP Awards do not vest until they have been held in trust for three years and specific performance criteria have been satisfied

Executive directors have a technical interest in 552,019 shares held by the Employee Share Ownership Trust The details of the performance criteria are explained on page 48 of this report The individual interests, for the above named directors, which represent the maximum aggregate number of shares to which each individual could become entitled, are as follows

	Awards granted	Maximum award	Awards vested	Awards lapsed	Maximum outstanding awards as at 31 March 2011
Tony Ballance	18 July 2007	3,261	1,966	1,295	–
	14 July 2008	5,486	–	–	5,486
	7 July 2009	7,405	–	–	7,405
	21 June 2010	6,803	–	–	6,803
Martin Kane	18 July 2007	3,475	2,095	1,380	–
	14 July 2008	6,001	–	–	6,001
	7 July 2009	8,154	–	–	8,154
	21 June 2010	8,504	-	-	8,504
Michael McKeon	18 July 2007	12,363	7,454	4,909	–
	14 July 2008	13,717	–	–	13,717
	7 July 2009	18,733	–	–	18,733
	21 June 2010	17,211	–	–	17,211
Andy Smith	18 July 2007	5,881	3,546	2,335	–
	14 July 2008	8,230	–	–	8,230
	7 July 2009	11,019	–	–	11,019
	21 June 2010	10,124	-	-	10,124
Tony Wray	18 July 2007	9,189	5,540	3,649	–
	14 July 2008	19,684	–	–	19,684
	7 July 2009	27,769	–	–	27,769
	21 June 2010	25,512	–	–	25,512

The market price on the date of the 2010 award was 1,235 pence The market price at the date of 2007 vesting was 1,221 pence

The performance period for awards granted on 18 July 2007 ended on 31 March 2010 The TSR result and the level of vesting achieved for this award is shown below

LTIP award	Ranking	Vesting %
2007	33 out of 85	60 3%

The performance period for awards granted on 14 July 2008 ended on 31 March 2011 The Committee has subsequently determined the TSR result and the level of vesting achieved for this award is shown below

LTIP award	Ranking	Vesting %
2008	48 out of 89	0%

Governance
Remuneration Committee (continued)

(iii) Annual Bonus Scheme

Since 2008, half of any bonus paid has been deferred into shares The table below shows the directors' deferred share awards and the vesting dates

Name	Date of grant	Annual bonus deferred into shares	Number of shares	Deferred share award vests
Tony Ballance	27 June 2008	£24,554	1,818	26 June 2011
	7 July 2009	£62,294	5,669	6 July 2012
	21 May 2010	£51,448	4,139	20 May 2013
Martin Kane	27 June 2008	£26,245	1,957	26 June 2011
	7 July 2009	£68,598	6,243	6 July 2012
	21 May 2010	£64,310	5,173	20 May 2013
Michael McKeon	27 June 2008	£85,667	6,345	26 June 2011
	7 July 2009	£157,590	14,343	6 July 2012
	21 May 2010	£128,724	10,355	20 May 2013
Andy Smith	27 June 2008	£37,732	2,794	26 June 2011
	7 July 2009	£92,700	8,437	6 July 2012
	21 May 2010	£75,810	6,098	20 May 2013
Tony Wray	27 June 2008	£76,029	5,631	26 June 2011
	7 July 2009	£166,680	15,187	6 July 2012
	21 May 2010	£138,996	11,182	20 May 2013

(iv) Share Matching Plan

The Share Matching Plan received shareholder approval at the 2009 AGM Under the Share Matching Plan executives can receive, subject to performance, matching shares for each share deferred under the annual bonus plan For awards made in 2010 (the first set of awards granted under the plan), the ratio was limited to 0 5 matching share for each deferred share The details of the performance criteria are explained on pages 48 and 49 of this report The individual interests, for the directors under the Share Matching Plan, are as follows

	Date of grant	Maximum award	Awards vesting	Award lapsing	Maximum outstanding awards as at 31 March 2011
Tony Ballance	21 May 2010	2,069	–	–	2,069
Martin Kane	21 May 2010	2,586	–	–	2,586
Michael McKeon	21 May 2010	5,177	–	–	5,177
Andy Smith	21 May 2010	3,049	–	–	3,049
Tony Wray	21 May 2010	5,591	–	–	5,591

The number of shares subject to an award will be increased to reflect dividends paid through the performance period on the basis of such notional dividends being reinvested at the then prevailing share price Awards will normally vest as soon as the Committee determines that the performance conditions have been met, provided that the participant remains in employment at the end of the performance period

(v) Sharesave options over ordinary shares

	At the start of the year (No of shares)	Exercised during the year (No of shares)	Cancelled during the year (No of shares)	Granted during the year (No of shares)	At the end of the year (No of shares)	Year of grant of option	Exercise price (p)	Date from which exercisable	Expiry date
Sharesave[1]									
Tony Ballance	556	–	–	–	556	2009	862	May 2012	Oct 2012
	561				561	2010	808	May 2013	Oct 2013
Martin Kane	322	(322)	–	–	–	2007	1172	May 2010	Oct 2010
	314	–	–	–	314	2008	1221	May 2011	Oct 2011
	222	–	–	–	222	2009	862	May 2012	Oct 2012
	449				449	2010	808	May 2013	Oct 2013
	–	–	–	316	316	2011	1137	May 2014	Oct 2014
Michael McKeon	1,943	–	–	–	1,943	2009	862	May 2014	Oct 2014
Andy Smith	1,123				1,123	2010	808	May 2013	Oct 2013
Tony Wray	1,123				1,123	2010	808	May 2013	Oct 2013

1 The executive directors in common with all eligible UK employees of the group are entitled to participate in the company's HMRC approved Sharesave Scheme

The terms and conditions applicable to these options are those provided in that scheme The options have no performance conditions as such conditions are not permitted by legislation

a) No executive share options in respect of executive directors were granted or lapsed during the year At 31 March 2011 there were two other executives participating in the group's historical executive Share Option Scheme (31 March 2010 five other executives)

b) At the close of business on 31 March 2011 the mid-market price of the company's shares was 1461p and the range during the year was 1086p to 1513p

Signed on behalf of the board which approved the Directors' remuneration report on 26 May 2011

Richard Davey
Chairman of the Remuneration Committee

Governance
Risk and assurance

Enterprise Risk Management

Our established Enterprise Risk Management (ERM) process as illustrated above is used for the identification and assessment of risks to significant business objectives This includes consideration of the effectiveness of existing controls and identification, prioritisation and tracking of actions needed to reduce the risk and/ or improve controls Our assessment also considers both financial and reputational impact of risks in order to give a holistic view

During the year we have continued to work to fully embed the process across the business, including rolling out the process to Severn Trent Services We have continued to keep the process fresh through the introduction of new tools and challenges and are working to better integrate with the processes used by business teams to monitor their performance

The key business risks are formally reported to the Severn Trent Executive Committee and Audit Committee every six months and to the board annually Reviews of risk generally take place within the business on a quarterly basis to monitor that our key risks are identified, that controls and mitigating actions continue to be effective and to confirm that focus is maintained on the most critical risks requiring attention

During the year we have also held a risk workshop with the board which looked at their views on the most significant risks facing the organisation in order to give greater visibility of their view on risk The key focus of these discussions was around the inter-relationships between risks, and the board recognised that whilst some risks may not be catastrophic on their own, an aggregation of smaller risks occurring simultaneously or in close succession could become very significant

In response to the discussions at the board we are now conducting a series of workshops aimed at challenging the robustness of controls in order to help us withstand even the most catastrophic scenario These workshops will consider the inter-relationships between risks to enable us to obtain maximum value from the risk information held

Over the coming year we will continue to work to maintain and improve our ERM process with a particular emphasis on closer integration with the business planning process This will include clearer articulation of our willingness to accept risk as part of the prioritisation of business activity

Principal Risks

The following table illustrates the principal risks facing our business. However, as part of our regular reporting, other risks have also been considered and discussed by the Severn Trent Audit, Corporate Responsibility and Executive Committees and the board during the year.

Examples of how we are managing our risks can also be found in the table.

Principal risk and business impact	Examples of controls, procedures and future plans
Strategic	
We continue to manage the risks associated with the delivery of the strategic objectives of Severn Trent Water including our ability to influence the regulatory framework towards creating a sustainable Water Industry in England and Wales and our ability to continue to develop a sustainable water company. Additionally, in the current and ongoing challenging economic climate, we continue to address risks which may affect the strategic objective to grow Severn Trent Services such as the political situations in some of our markets and the threat of new competitors.	With regard to Severn Trent Water • We have a strategy to be the leading water and waste water company in the UK that is supported by a robust approach to legal and regulatory compliance. • We have an appropriate organisational design to support the achievement of the strategy. • We engage with key regulatory and government stakeholders to understand and influence the direction of future regulatory and public policy development within the Water Industry. With regard to Severn Trent Services • We have a clearly articulated strategy in place for products and markets to be targeted. See pages 16 and 19 for details. • We are implementing a plan to deliver the anticipated growth. • We have business partners in place to provide local support in target markets.
Stakeholder	
We continue to manage the risks associated with meeting the needs and expectations of key stakeholders (investors, regulators, customers, staff and suppliers) in order to protect and enhance our financial position, brand, reputation and investor confidence.	• We promote and protect the reputation of Severn Trent Water through effective internal and external communications and robust crisis management plans that include a clear communications plan and responsibilities. • We maintain performance across a range of corporate responsibility issues to increase confidence of our key stakeholders and to enhance and protect our reputation. • We maintain close relationships with our regulators and other stakeholders. • We continue to build on Changing Course and demonstrate thought leadership within the industry. See page 21 for details. • We continue to work with our staff to ensure our people have the right skills. • We monitor closely the performance of our One Supply Chain contractors involved on the AMP5 programme.

Governance
Risk and assurance (continued)

Principal risk and business impact

Examples of controls, procedures and future plans

Operational and asset related

We continue to manage the risks associated with our daily operations, including the failure of assets, processes or systems which in turn may affect our ability to serve our customers, could impact on health and safety or security at our sites and on our ability to meet regulatory targets

- We have asset management plans in place for key assets and investment governance boards to prioritise capital investment
- We have initiated an 'Always On' improvement programme to improve controls in relation to investment, training, and the processes and equipment to maintain our distribution network
- We conduct contingency planning and 'what if' analyses to ensure our assets, systems and processes are robust to withstand significant disruption events
- We have safety improvement programmes in place at all sites driven by local employee groups to continuously improve performance See page 15 for details
- We run awareness campaigns to ensure security issues are appropriately considered
- We have developed a close working relationship with government departments and emergency forces to maintain appropriate levels of security required at all critical sites

Financial

We continue to manage the risks associated with our financial activities including our ability to effectively manage counterparty risk, attract funding at commercially attractive rates, fund pensions promises sustainably and meet the challenging stretch targets we have set ourselves within our Severn Trent Water and Severn Trent Services businesses

- We have regular detailed counterparty and investment reporting processes and monitoring
- Through planning and monitoring we ensure the group has access to funds to meet its ongoing business needs
- We have an effective Pension Trustee structure, investment policy and investment performance monitoring process in place in addition to regular board reviews of pension affordability
- We ensure external audits are conducted of processes and departments
- We establish business plans and budgets and continually monitor the financial performance of our businesses against those targets

Legal, regulatory and compliance

We continue to manage the risks associated with potential non-compliance with the numerous and increasingly demanding obligations reflecting the international spread of our operations Management of these is often dispersed throughout the organisation We pay particular attention to risks in areas subjected to changing legal and regulatory requirements

Current areas of focus include

- The UK Bribery Act
- The taking on of private sewers and lateral drains (PDAS)
- The introduction of Service Incentive Mechanism (SIM) by Ofwat

- We have established a compliance management framework, as part of the corporate governance framework for the group, for Severn Trent Water
- We plan to undertake a legal risk review of our Severn Trent Services business
- We are currently in the process of updating our existing Anti Bribery and Anti Fraud Policy and supporting standards to reflect the Bribery Act 2010 guidance
- We have a change programme in place to effectively manage the transfer of private sewers and lateral drains See page 11 for details

Independent auditor's report to the members of Severn Trent Plc

We have audited the group financial statements of Severn Trent Plc for the year ended 31 March 2011 which comprise the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity, the consolidated balance sheet, the consolidated cash flow statement, and the related notes 1 to 40 The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union

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' responsibility statement, the directors are responsible for the preparation of the group 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 group 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 Ethical Standards for Auditors

Scope of the audit of the financial statements
An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error This includes an assessment of whether the accounting policies are appropriate to the group'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 financial statements In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report

Opinion on financial statements
In our opinion the group financial statements

- give a true and fair view of the state of the group's affairs as at 31 March 2011 and of its profit for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation

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 group financial statements are prepared is consistent with the group financial statements

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

Under the Companies Act 2006 we are required to report to you if, in our opinion

- 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

Under the Listing Rules we are required to review

- the directors' statement, contained within the Directors' report, in relation to going concern,
- the part of the Chairman's letter relating to the company's compliance with the nine provisions of the June 2008 Combined Code specified for our review, and
- certain elements of the report to shareholders by the Board on directors' remuneration

Other matters
We have reported separately on the parent company financial statements of Severn Trent Plc for the year ended 31 March 2011 and on the information in the Remuneration Committee report that is described as having been audited

Carl D Hughes (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
London, UK
26 May 2011

Consolidated income statement

For the year ended 31 March 2011

	Notes	2011 £m	2010 £m
Turnover	6, 5	**1,711 3**	1,703 9
Operating costs before exceptional items	7	**(1,192 2)**	(1,146 8)
Exceptional restructuring costs	8	**(13.7)**	(48 0)
Exceptional charge relating to regulatory matters	8	**(7 7)**	–
Total operating costs	7	**(1,213 6)**	(1,194 8)
Exceptional loss on disposal of businesses	8	**–**	(1 7)
Profit before interest, tax and exceptional items	5	**519 1**	557 1
Exceptional items	8	**(21 4)**	(49 7)
Profit before interest and tax		**497 7**	507 4
Finance income	10	**100 7**	80 9
Finance costs	11	**(331.3)**	(299 7)
Net finance costs		**(230 6)**	(218 8)
(Losses)/gains on financial instruments	12	**(14 2)**	45 7
Share of results of associates and joint ventures		**0.1**	0 1
Profit before tax, (losses)/gains on financial instruments and exceptional items		**288 6**	338 4
Exceptional Items	8	**(21 4)**	(49 7)
(Losses)/gains on financial instruments	12	**(14.2)**	45 7
Profit on ordinary activities before taxation		**253 0**	334 4
Taxation on profit on ordinary activities			
Current tax	13	**(32 1)**	(40 7)
Deferred tax	13	**(14 1)**	(42 2)
Exceptional deferred tax credit arising from rate change	13	**67 7**	–
Total taxation	13	**21.5**	(82 9)
Profit for the period		**274 5**	251 5
Attributable to			
Equity holders of the company		**272 6**	249 2
Non-controlling interests		**1 9**	2 3
		274 5	251 5
Earnings per share (pence)			
Basic	15	**115 2**	105 6
Diluted	15	**114 6**	105 5

Consolidated statement of comprehensive income

For the year ended 31 March 2011

	2011 £m	2010 £m
Profit for the period	**274 5**	251 5
Gains/(losses) on cash flow hedges taken to equity	**16.0**	(13 2)
Deferred tax on gains/losses on cash flow hedges taken to equity	**(4.1)**	3 7
Amounts on cash flow hedges transferred to the income statement in the period	**4 5**	7 6
Deferred tax on transfers to income statement	**(1 2)**	(2 1)
Exchange movement on translation of overseas results and net assets	**(6 3)**	(9 0)
Tax on exchange differences on foreign currency	**(0 4)**	(0 4)
Actuarial gains/(losses) on defined benefit pension schemes	**50 7**	(124 4)
Tax on actuarial gains/losses	**(13 2)**	34 8
Deferred tax movement arising from rate change	**0 7**	–
Other comprehensive income/(loss) for the period	**46 7**	(103 0)
Total comprehensive income for the period	**321 2**	148 5
Attributable to		
Equity shareholders of the company	**319.7**	146 5
Non-controlling interests	**1 5**	2 0
	321 2	148 5

Consolidated statement of changes in equity

For the year ended 31 March 2011

	Share capital £m	Share premium £m	Other reserves £m	Retained earnings £m	Equity attributable to equity holders of Severn Trent Plc £m	Non-controlling interests £m	Total £m
At 1 April 2009	231 0	71 9	468 7	174 5	946 1	6 0	952 1
Profit for the period	–	–	–	249 2	249 2	2 3	251 5
Losses on cashflow hedges taken to equity	–	–	(13 2)	–	(13 2)	–	(13 2)
Deferred tax on losses on cashflow hedges taken to equity	–	–	3 7	–	3 7	–	3 7
Amounts on cash flow hedges transferred to the income statement	–	–	7 6	–	7 6	–	7 6
Deferred tax on transfers to the income statement	–	–	(2 1)	–	(2 1)	–	(2 1)
Exchange movement on translation of overseas results and net assets	–	–	(8 7)	–	(8 7)	(0 3)	(9 0)
Tax on exchange differences	–	–	(0 4)	–	(0 4)	–	(0 4)
Actuarial losses	–	–	–	(124 4)	(124 4)	–	(124 4)
Tax on actuarial losses	–	–	–	34 8	34 8	–	34 8
Total comprehensive income for the period	–	–	(13 1)	159 6	146 5	2 0	148 5
Share options and LTIPs							
- proceeds from shares issued	0 6	4 0	–	–	4 6	–	4 6
- value of employees' services	–	–	–	5 1	5 1	–	5 1
- free shares issued	–	–	–	(2 2)	(2 2)	–	(2 2)
Current tax on share based payments	–	–	–	0 3	0 3	–	0 3
Dividends paid	–	–	–	(159 7)	(159 7)	(1 7)	(161 4)
At 31 March 2010	231 6	75 9	455 6	177 6	940 7	6 3	947 0
Profit for the period	–	–	–	272 6	272 6	1 9	274 5
Gains on cashflow hedges taken to equity	–	–	16 0	–	16 0	–	16 0
Deferred tax on gains on cashflow hedges taken to equity	–	–	(4 1)	–	(4 1)	–	(4 1)
Amounts on cash flow hedges transferred to the income statement	–	–	4 5	–	4 5	–	4 5
Deferred tax on transfers to the income statement	–	–	(1 2)	–	(1 2)	–	(1 2)
Exchange movement on translation of overseas results and net assets	–	–	(5 9)	–	(5 9)	(0 4)	(6 3)
Tax on exchange differences	–	–	(0 4)	–	(0 4)	–	(0 4)
Actuarial gains	–	–	–	50 7	50 7	–	50 7
Tax on actuarial gains	–	–	–	(13 2)	(13 2)	–	(13 2)
Deferred tax arising from rate change	–	–	–	0 7	0 7	–	0 7
Total comprehensive income for the period	–	–	8 9	310 8	319 7	1 5	321 2
Share options and LTIPs							
- proceeds from shares issued	0 6	4 1	–	–	4 7	–	4 7
- value of employees' services	–	–	–	4 6	4 6	–	4 6
- free shares issued	–	–	–	(2 0)	(2 0)	–	(2 0)
Current tax on share based payments	–	–	–	0 3	0 3	–	0 3
Deferred tax on share based payments	–	–	–	1 2	1 2	–	1 2
Dividends paid	–	–	–	(169 4)	(169 4)	(1 5)	(170 9)
At 31 March 2011	**232 2**	**80 0**	**464 5**	**323 1**	**1,099 8**	**6 3**	**1,106 1**

Consolidated balance sheet

At 31 March 2011

	Note	2011 £m	2010 (Restated see note 3) £m
Non-current assets			
Goodwill	16	**68 3**	70 6
Other intangible assets	17	**134 9**	138 5
Property, plant and equipment	18	**6,427 0**	6,302 0
Interests in joint ventures	19	**0 2**	0 3
Interests in associates	20	**4 8**	4 6
Derivative financial instruments	32	**188 1**	203 8
Available for sale financial assets	32	**0 1**	0 1
		6,823 4	6,719 9
Current assets			
Inventory	21	**27.1**	26 5
Trade and other receivables	22	**478 5**	472 8
Derivative financial instruments	32	**4 3**	2 9
Cash and cash equivalents	23	**315.2**	227 8
		825 1	730 0
Total assets		**7,648.5**	7,449 9
Current liabilities			
Borrowings	32	**(23 9)**	(260 9)
Derivative financial instruments	32	**(0 1)**	(4 4)
Trade and other payables	25	**(391 2)**	(464 4)
Current income tax liabilities		**(67 0)**	(67 2)
Provisions for liabilities and charges	28	**(12 6)**	(25 5)
		(494.8)	(822 4)
Non-current liabilities			
Borrowings	32	**(4,320 5)**	(3,915 6)
Derivative financial instruments	32	**(122 4)**	(140 3)
Trade and other payables	25	**(367 8)**	(284 9)
Deferred tax	26	**(919 4)**	(956 4)
Retirement benefit obligations	27	**(292 1)**	(354 9)
Provisions for liabilities and charges	28	**(25 4)**	(28 4)
		(6,047 6)	(5,680 5)
Total liabilities		**(6,542 4)**	(6,502 9)
Net assets		**1,106 1**	947 0
Capital and reserves attributable to the company's equity shareholders			
Called up share capital	29	**232 2**	231 6
Share premium account	30	**80 0**	75 9
Other reserves	31	**464 5**	455 6
Retained earnings		**323 1**	177 6
Equity attributable to the company's equity shareholders		**1,099 8**	940 7
Non-controlling interests		**6 3**	6 3
Total equity		**1,106 1**	947 0

Signed on behalf of the board who approved the accounts on 26 May 2011

Andrew Duff
Chairman

Michael McKeon
Finance Director

Company Number 2366619

Consolidated cash flow statement

For the year ended 31 March 2011

	Note	2011 £m	2010 £m
Cash generated from operations	34	**753 0**	708 0
Tax paid		**(32 4)**	(53 8)
Net cash generated from operating activities		**720 6**	654 2
Investing activities			
Interest received		**10.3**	10 5
Dividends received from associates and joint ventures		**–**	0 1
Net cash inflow from sale of investments		**–**	2 2
Acquisition of subsidiaries		**–**	(13 2)
Proceeds on disposal of property, plant and equipment		**5 1**	6 9
Purchases of intangible assets		**(20 9)**	(47 8)
Purchases of property, plant and equipment		**(403 1)**	(464 9)
Contributions and grants received		**19 4**	18 0
Net cash used in investing activities		**(389 2)**	(488 2)
Financing activities			
Interest paid		**(179 8)**	(194 7)
Closed out swap		**20 5**	–
Interest element of finance lease payments		**(10.8)**	(10 0)
Dividends paid to shareholders of the parent		**(169 4)**	(159 7)
Dividends paid to non-controlling interests		**(1 5)**	(1 7)
Repayments of borrowings		**(28 7)**	(180 0)
Repayments of obligations under finance leases		**(47 3)**	(43 2)
New loans raised		**171 2**	1 0
Issues of shares		**4 7**	4 6
Purchase of own shares		**(2.0)**	(2 2)
Net cash used in financing activities		**(243 1)**	(585 9)
Increase/(decrease) in cash and cash equivalents		**88 3**	(419 9)
Net cash and cash equivalents at beginning of period		**227 8**	648 1
Effect of foreign exchange rates		**(0 9)**	(0 4)
Net cash and cash equivalents at end of period		**315 2**	227 8

The increase in cash and cash equivalents is reconciled to the movement in net debt in note 34

Notes to the group financial statements

For the year ended 31 March 2011

1 General information

The Severn Trent group has a number of operations These are described in the segmental analysis in note 5

Severn Trent Plc is a company incorporated and domiciled in the United Kingdom The address of its registered office is shown on the back of the cover of the annual report and accounts

Severn Trent Plc is listed on the London Stock Exchange

2 Accounting policies

a) Basis of preparation
The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), International Accounting Standards (IAS) and IFRIC interpretations issued and effective and ratified by the European Union as at 31 March 2011

The financial statements have been prepared on the going concern basis (see Directors' report on page 28) under the historical cost convention as modified by the revaluation of certain financial assets and liabilities (including derivative instruments) at fair value

The preparation of financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses for the reporting period Although these estimates are based on management's best knowledge of the amount, event or actions, actual results may ultimately differ from those estimates

b) Basis of consolidation
The financial statements include the results of Severn Trent Plc and its subsidiaries, joint ventures and associated undertakings The results of subsidiaries, joint ventures and associated undertakings are included from the date of acquisition or incorporation, and excluded from the date of disposal

The results of subsidiaries are consolidated where the group has the power to control a subsidiary

The results of joint venture undertakings are accounted for on an equity basis where the company exercised joint control under a contractual arrangement

The results of associates are accounted for on an equity basis where the company holding is 20% or more or the company has the power to exercise significant influence

Non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the group's equity therein Non-controlling interests consist of the amount of those interests at the date of the original business combination and the non-controlling interest's share of changes in equity since that date Losses attributable to the non-controlling interest in excess of its interest in the subsidiary's equity are allocated against the interests of the group except to the extent that the non-controlling interest has a binding obligation and is able to make an additional investment to cover the losses

All intra-group transactions, balances, income and expenses are eliminated on consolidation

c) Revenue recognition
Revenue represents the fair value of consideration receivable, excluding value added tax, trade discounts and inter-company sales, in the ordinary course of business for goods and services provided

Revenue is not recognised until the service has been provided to the customer, or the goods to which the sale relates have either been despatched to the customer or, where they are held on the customer's behalf, title has passed to the customer

Turnover includes an estimate of the amount of mains water and waste water charges unbilled at the year end The accrual is estimated using a defined methodology based upon a measure of unbilled water consumed by tariff, which is calculated from historical billing information

In respect of long term contracts, revenue is recognised based on the value of work carried out during the year with reference to the total sales value and the stage of completion of these contracts

Interest income is accrued on a time basis by reference to the principal outstanding and at the effective interest rate applicable Dividend income from investments is recognised when the group's rights to receive payment have been established Interest and dividend income are included in finance income

d) Exceptional items
Exceptional items are income or expenditure, which individually or, if of a similar type, in aggregate should, in the opinion of the directors, be disclosed by virtue of their size or nature if the financial statements are to give a true and fair view In this context, materiality is assessed at the segment level

e) Taxation
Current tax payable is based on taxable profit for the year Taxable profit differs from net profit as reported in the income statement because it excludes items of income and expenses that are taxable or deductible in other years and it further excludes items that are never taxable or deductible The group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date

Deferred taxation is provided in full, using the liability method, on taxable temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements A deferred tax asset is only recognised to the extent it is probable that sufficient taxable profits will be available in the future to utilise it Deferred taxation is measured on a non-discounted basis using the tax rates and laws that have then been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred tax liability is settled

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the group intends to settle its current tax assets and liabilities on a net basis

f) Goodwill
Goodwill represents the excess of the fair value of purchase consideration over the fair value of the net assets acquired Goodwill arising on acquisition of subsidiaries is included in intangible assets, whilst goodwill arising on acquisition of associates is included in investments in associates If an acquisition gives rise to negative goodwill this is credited directly to the income statement Fair value adjustments based on provisional estimates are amended within one year of the acquisition, if required, with a corresponding adjustment to goodwill

Notes to the group financial statements (continued)

For the year ended 31 March 2011

2 Accounting policies (continued)

f) Goodwill (continued)

Goodwill arising on all acquisitions prior to 1 April 1998 was written off to reserves under UK GAAP and remains eliminated against reserves Purchased goodwill arising on acquisitions after 31 March 1998 is treated as an intangible fixed asset

Goodwill is tested for impairment in accordance with the policy set out in note 2 m) below and carried at cost less accumulated impairment losses Goodwill is allocated to the cash-generating unit that derives benefit from the goodwill for impairment testing purposes

Where goodwill forms part of a cash-generating unit and all or part of that unit is disposed of, the associated goodwill is included in the carrying amount of that operation when determining the gain or loss on disposal of the operation

g) Intangible non-current assets

Intangible assets acquired separately are capitalised at cost and when acquired in a business combination are capitalised at fair value at the date of acquisition Following initial recognition, the historical cost model is applied to intangible assets Amortisation charged on assets with finite lives is taken to the income statement through operating expenses

Finite life intangible assets are amortised on a straight line basis over their estimated useful economic lives as follows

	Years
Software	3-10
Other assets	2-20

Intangible assets are reviewed for impairment where indicators of impairment exist

h) Research and development

Research expenditure is expensed when it is incurred Development expenditure is capitalised and written off over its expected useful economic life where the following criteria are met

- it is technically feasible to create and make the asset available for use or sale,
- there are adequate resources available to complete the development and to use or sell the asset,
- there is the intention and ability to use or sell the asset,
- it is probable that the asset created will generate future economic benefits, and
- the development cost can be measured reliably

Expenditure on property, plant and equipment relating to research and development projects is capitalised and written off over the expected useful life of those assets

i) Pre-contract costs

Pre-contract costs are expensed as incurred except where it is probable that the contract will be awarded, in which case they are recognised as a prepayment which is written off to the income statement over the life of the contract

j) Property, plant and equipment

Property, plant and equipment is held at cost (or at deemed costs for infrastructure assets on transition to IFRS) less accumulated depreciation The costs of like for like replacement of infrastructure components are recognised in the income statement as they arise Where it is probable that the expenditure will cause future economic benefits to flow to the group, then costs are capitalised

Where items of property, plant and equipment are transferred to the group from customers or developers, the fair value of the asset transferred is recognised in the balance sheet Fair value is determined based on estimated depreciated replacement cost Where the transfer is in exchange for connection to the network and there is no further obligation, the corresponding credit is recognised immediately in turnover Where the transfer is considered to be linked to the provision of ongoing services the corresponding credit is recorded in deferred income and released to operating costs over the expected useful lives of the related assets

Borrowing costs directly attributable to the acquisition, construction or production of assets, that necessarily take a substantial period of time to get ready for their intended use, are added to the cost of those assets until such time as the assets are ready for their intended use

Property, plant and equipment is depreciated to its estimated residual value over its estimated useful life, with the exception of freehold land which is not depreciated Assets in the course of construction are not depreciated until commissioned

The estimated useful lives are

	Years
Infrastructure assets	
Impounding reservoirs	250
Raw water aqueducts	250
Mains	80-150
Sewers	150-200
Other assets	
Buildings	30-80
Fixed plant and equipment	20-40
Vehicles and mobile plant	2-15

k) Leased assets

Where the group obtains assets under leasing arrangements which transfer substantially all the risks and rewards of ownership of an asset to the group as lessee (finance leases), the lower of the fair value of the leased asset or the present value of the minimum lease payments is capitalised as an asset with a corresponding liability representing the obligation to the lessor Lease payments are treated as consisting of a capital element and a finance charge, the capital element reducing the obligation to the lessor and the finance charge being written off to the income statement at a constant rate over the period of the lease in proportion to the capital amount outstanding Depreciation is charged over the shorter of the estimated useful life and the lease period

Leases where substantially all the risks and rewards of ownership remain with the lessor are classified as operating leases Rental costs arising under operating leases are expensed on a straight line basis over the term of the lease Leases of land are normally treated as operating leases, unless ownership is transferred to the group at the end of the lease

l) Grants and contributions

Grants and contributions received in respect of non-current assets, including certain charges made as a result of new connections to the water and sewerage networks, are treated as deferred income and released to the income statement over the useful economic life of those non-current assets

2 Accounting policies (continued)

l) Grants and contributions (continued)
Grants and contributions which are given in compensation for expenses incurred with no future related costs are recognised in operating costs in the income statement in the period that they become receivable

m) Impairment of non-current assets
If the recoverable amount of goodwill, an item of property, plant and equipment, or any other non-current asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount Where the asset does not generate cash flows that are independent from other assets, the group estimates the recoverable amount of the cash-generating unit to which the asset belongs Recoverable amount is the higher of fair value less costs to sell or estimated value in use at the date the impairment review is undertaken Fair value less costs to sell represents the amount obtainable from the sale of the asset in an arm's length transaction between knowledgeable and willing third parties, less costs of disposal Value in use represents the present value of future cash flows expected to be derived from a cash generating unit, discounted using a pre-tax discount rate that reflects current market assessments of the cost of capital of the cash-generating unit or asset

The discount rate used is based on the group's cost of capital adjusted for the risk profiles of individual businesses

Goodwill is tested for impairment annually Impairment reviews are also carried out if there is an indication that an impairment may have occurred, or, where otherwise required, to ensure that non-current assets are not carried above their estimated recoverable amounts

Impairments are recognised in the income statement

n) Inventory
Inventory and work in progress is stated at the lower of cost and net realisable value Cost includes labour, materials, transport and attributable overheads

o) Service concession agreements
Where the group has an unconditional right to receive cash from a government body in exchange for constructing or upgrading a public sector asset, the amounts receivable are recognised as a financial asset in prepayments and accrued income

Costs of constructing or upgrading the public sector asset are recognised on a straight line basis, before adjusting for expected inflation, over the life of the contract

p) Retirement benefits
The group operates both defined benefit and defined contribution pension schemes

The difference between the value of defined benefit pension scheme assets and defined benefit pension scheme liabilities is recorded on the balance sheet as a retirement benefit asset or obligation

Defined benefit pension scheme assets are measured using bid price Defined benefit pension scheme liabilities are measured at the balance sheet date by an independent actuary using the projected unit method and discounted at the current rate of return on high quality corporate bonds of equivalent term and currency to the liability Service cost, which is the increase in the present value of the liabilities of the group's defined benefit pension schemes expected to arise from employee service in the period, is included in operating costs The expected return on the scheme's assets and the increase during the period in the present value of the scheme's liabilities, arising from the passage of time, are included in other finance income or cost

Actuarial gains and losses arising from experience adjustments, changes in actuarial assumptions and amendments to pension plans are charged or credited to equity and recorded in the statement of comprehensive income

Contributions to defined contribution pension schemes are charged to the income statement in the period in which they fall due

q) Provisions
Provisions are recognised where

- there is a present obligation as a result of a past event,
- it is probable that there will be an outflow of economic benefits to settle this obligation, and
- a reliable estimate of this amount can be made

Insurance provisions are recognised for claims notified and for claims incurred but which have not yet been notified, based on advice from the group's independent insurance advisers

Provisions are discounted to present value using a pre-tax discount rate that reflects the risks specific to the liability where the effect is material

r) Purchase of own shares
The group balance sheet includes the shares held by the Severn Trent Employee Share Ownership Trust and which have not vested unconditionally by the balance sheet date These are shown as a deduction from shareholders' funds until such time as they vest

s) Financial instruments
(i) Financial assets
Financial assets are classified into the following specified categories

- At fair value through profit or loss,
- Held to maturity investments,
- Available for sale financial assets, and
- Loans and receivables

Financial assets at fair value through profit or loss
A financial asset is classified at fair value through profit or loss if it is so designated or if it is held for trading Derivative financial assets that are not designated and effective as hedging instruments are classified as held for trading Financial assets at fair value through profit or loss are stated at fair value, with any gains or losses arising on remeasurement recognised in gains/losses on financial instruments in the income statement Fair value is determined using the methodology described in note 32 Interest receivable in respect of derivative financial assets is included in finance income

Held to maturity investments
Where the group has the ability and intent to hold an investment to maturity the financial asset is classified as held to maturity Such financial assets are measured at amortised cost using the effective interest rate method, with any gains or losses being recognised in the income statement

Notes to the group financial statements (continued)

For the year ended 31 March 2011

2 Accounting policies (continued)

s) Financial instruments (continued)

(i) Financial assets (continued)

Available for sale financial assets

After initial recognition at cost (being the fair value of the consideration paid), investments which are classified as available for sale are measured at fair value, with gains or losses recognised in equity When an available for sale investment is disposed of or impaired, the gain or loss previously recognised in equity is taken to the income statement Where there is no active market in the investments and the fair value cannot be measured reliably, the investments are held at cost

Loans and receivables

Trade receivables, loans and other receivables that have fixed or determinable payments and that are not quoted in an active market are classified as loans and receivables Such assets are measured at fair value on initial recognition and are subsequently measured at amortised cost using the effective interest rate method unless there is objective evidence that the asset is impaired, where it is written down to its recoverable amount and the irrecoverable amount is recognised as an expense

Trade receivables that are assessed not to be impaired individually are assessed collectively for impairment by reference to the group's historical collection experience for receivables of similar age

(ii) Financial liabilities

Financial liabilities are classified as either

- financial liabilities at fair value through profit or loss, or
- other financial liabilities

Financial liabilities at fair value through profit or loss

A financial liability is classified at fair value through profit or loss if it is so designated or if it is held for trading Derivative financial liabilities that are not designated and effective as hedging instruments are classified as held for trading Financial liabilities at fair value through profit or loss are stated at fair value, with any gains or losses arising on remeasurement recognised in gains/losses on financial instruments in the income statement Fair value is determined using the methodology described in note 32 Interest payable in respect of derivative financial liabilities is included in finance costs

Other financial liabilities

Other financial liabilities, including borrowings, are initially recognised at fair value less transaction costs After initial recognition, other financial liabilities are subsequently measured at amortised cost using the effective interest rate method

(iii) Hedge accounting

The group uses derivative financial instruments such as cross currency swaps, forward currency contracts and interest rate swaps to hedge its risks associated with foreign currency and interest rate fluctuations Such derivative instruments are recognised and measured in accordance with the accounting policies described above

At the inception of the hedge relationship the group documents

- the relationship between the hedging instrument and the hedged item,
- its risk management objectives and strategy for undertaking hedge transactions, and
- whether the hedging instrument is highly effective in offsetting changes in fair values or cash flows (as appropriate) of the hedged item

The group continues to test and document the effectiveness of the hedge on an ongoing basis

Hedge accounting is discontinued when the hedging instrument expires, is sold, terminated or exercised, or no longer qualifies for hedge accounting

Fair value hedges

Where a loan or borrowing is in a fair value hedging relationship it is remeasured for changes in fair value of the hedged risk at the balance sheet date, with gains or losses being recognised in gains/losses on financial instruments in the income statement The gain or loss on the hedging instrument is taken to gains/losses on financial instruments in the income statement where the effective portion of the hedge will offset the gain or loss on the hedged item

When hedge accounting is discontinued the fair value adjustment to the carrying amount of the hedged item arising from the hedged risk is amortised to the income statement from that date

Cash flow hedges

The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in equity and the ineffective portion in gains/losses on financial instruments in the income statement The gains or losses deferred in equity in this way are recycled through gains/losses on financial instruments in the income statement in the same period in which the hedged underlying transaction or firm commitment is recognised in the income statement

When hedge accounting is discontinued any cumulative gain or loss on the hedging instrument recognised in equity is kept in equity until the forecast transaction occurs, or transferred to gains/losses on financial instruments in the income statement if the forecast transaction is no longer expected to occur

Hedges of net investments in foreign operations

Where forward currency contracts and foreign currency borrowings are used to hedge net investments in foreign currency denominated operations, to the extent that they are designated and effective as net investment hedges, they are matched in equity against changes in value of the related assets Any ineffectiveness is taken to gains/losses on financial instruments in the income statement

(iv) Embedded derivatives

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contract and the host contract is not carried at fair value, with gains and losses reported in gains/losses on financial instruments in the income statement

t) Share based payments

The group operates a number of equity settled share based compensation plans for employees The fair value of the employee services received in exchange for the grant is recognised as an expense over the vesting period of the grant

The fair value of employee services is determined by reference to the fair value of the awards granted calculated using an appropriate pricing model, excluding the impact of any non-market vesting conditions The number of awards that are expected to vest takes into account non-market vesting conditions including, where appropriate, continuing employment by the group The charge is adjusted to reflect shares that do not vest as a result of failing to meet a non-market condition

2 Accounting policies (continued)

u) Cash and cash equivalents
For the purpose of the cash flow statement, cash and cash equivalents include highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value Such investments are normally those with less than three months' maturity from the date of acquisition and include cash and bank balances and investments in liquid funds Cash and cash equivalents also include overdrafts repayable on demand

v) Foreign currency
The results of overseas subsidiary and associated undertakings are translated into sterling, the presentational currency of the group, using average rates of exchange ruling during the year

The net investments in overseas subsidiary and associated undertakings are translated into sterling at the rates of exchange ruling at the year end Exchange differences thus arising are treated as movements in equity On disposal of a foreign currency denominated subsidiary, the deferred cumulative amount recognised in equity since 1 April 2004 relating to that entity is recognised in the income statement under the transitional rule of IFRS 1

Exchange differences arising in respect of foreign exchange instruments taken out as hedges of overseas investments are also treated as movements in equity to the extent that the hedge is effective (see note 2 s)

All other foreign currency denominated assets and liabilities of the company and its subsidiary undertakings are translated into the relevant functional currency at the rates of exchange ruling at the year end Any exchange differences so arising are dealt with through the income statement

Foreign currency transactions arising during the year are translated into sterling at the rate of exchange ruling on the date of the transaction All profits and losses on exchange arising during the year are dealt with through the income statement

w) Discontinued operations and assets held for sale
Where an asset or group of assets (a disposal group) is available for immediate sale and the sale is highly probable and expected to occur within one year then the disposal group is deemed as held for sale The disposal group is measured at the lower of the carrying amount and fair value less costs to sell

Where a group of assets which comprises operations that can be clearly distinguished operationally and for financial reporting purposes from the rest of the group, (a component), has been disposed of or classified as held for sale, and it

- represents a separate major line of business or geographical area of operations, or
- is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations, or
- is a subsidiary acquired exclusively with a view to resale,

then the component is classified as a discontinued operation

Non-current assets classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell Depreciation is not charged on such assets

3 New accounting policies and future requirements

IAS 27 (revised) was required to be implemented by the group from 1 April 2010 The revised standard requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control The standard also specifies the accounting when control is lost The group has had no transactions in the current or prior year that would have been impacted by the revised standard

IFRS 3 (revised) was also required to be implemented by the group from 1 April 2010 The standard continues to apply the acquisition method to business combinations, with some significant changes The group has had no significant transactions in the current or prior year that would have been impacted by the revised standard

IFRIC 18 "Transfers of assets from customers" was issued in January 2009 and was required to be applied with effect from 1 April 2010 for assets transferred after 1 July 2009 Where property, plant and equipment is transferred, the fair value of the asset is recognised in the balance sheet Where the transfer is in exchange for connection to the network, the corresponding credit is recognised immediately in turnover However, in most cases the transfer is considered to be linked to the provision of ongoing services and in these cases the corresponding credit is recorded in deferred income and released to operating costs over the expected useful lives of the related assets The impact of the adoption of IFRIC 18 on the comparative figures presented in these financial statements is summarised below

At 31 March 2010	Property plant and equipment £m	Trade and other payables: Current liabilities £m	Trade and other payables: Non-current liabilities £m
As previously stated	6,260 5	(464 2)	(243 6)
Fair value of assets transferred	41 5	(0 2)	(41 3)
As restated	**6,302.0**	**(464 4)**	**(284 9)**

The following standards have been issued by the International Accounting Standards Board and are likely to affect future financial statements

IFRS 9 "Financial instruments" is likely to affect the measurement and disclosure of financial instruments The standard is required to be implemented by the group with effect from the year ending 31 March 2014, subject to EU endorsement

IFRS 10 "Consolidated Financial Statements" was issued in May 2011 and is required to be implemented by the group from 1 April 2013 The standard includes a new definition of control to be used to determine when entities are consolidated The standard is not expected to have a material impact on the current consolidation

IFRS 11 "Joint Agreements" was issued in May 2011 and is required to be implemented by the group from 1 April 2013 IFRS 11 replaces IAS 31 "Interests in Joint Ventures" and SIC-13 "Jointly-controlled Entities" IFRS 11 uses the definition of control given in IFRS 10 to define joint control and removes the option to account for joint ventures using proportionate consolidation This is not expected to have a material impact on the group

Notes to the group financial statements (continued)

For the year ended 31 March 2011

3 New accounting policies and future requirements (continued)

IFRS 12 "Disclosure of Interests in Other Entities" was issued in May 2011 and is required to be implemented by the group from 1 April 2013 The standard provides disclosure requirements for subsidiaries, associates and joint agreements and structured entities which were previously covered in IAS 27, IAS 28 and IAS 31 Additional disclosures will be required in the group financial statements to meet the requirements of the standard

IFRS 13 "Fair Value Measurement" was issued in May 2011 and is required to be implemented by the group from 1 April 2013 The standard provides additional guidance on how to measure fair value but does not change when fair value is permitted or required The standard may impact the methods of determining fair value which are currently employed by the group and will require enhanced disclosure of these methods

The directors assess that the other standards and interpretations issued but not yet effective are not likely to have a significant impact on future financial statements

4 Significant accounting judgements and key sources of estimation uncertainty

In the process of applying the group's accounting policies, the group is required to make certain judgements, estimates and assumptions that it believes are reasonable based on the information available

The more significant judgements were

a) Tax provisions
Assessing the outcome of uncertain tax positions requires judgements to be made regarding the result of negotiations with and enquiries from tax authorities in a number of jurisdictions The assessments made are based on advice from independent tax advisers and the status of ongoing discussions with the relevant tax authorities

b) Provisions for other liabilities and charges
Assessing the financial outcome of uncertain commercial and legal positions requires judgements to be made regarding the relative merits of each party's case and the extent to which any claim against the group is likely to be successful The assessments made are based on advice from the group's internal counsel and, where appropriate, independent legal advice

The key accounting estimates were

a) Goodwill impairment
Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units (CGU) to which goodwill has been allocated The value in use calculation requires the group to estimate the future cash flows expected to arise from the CGU and a suitable discount rate to calculate present value Details of the assumptions used are set out in note 16 to the financial statements

b) Depreciation and carrying amounts of property, plant and equipment
Calculating the depreciation charge and hence the carrying value for property, plant and equipment requires estimates to be made of the useful lives of the assets The estimates are based on engineering data and the group's experience of similar assets Details are set out in note 2 j)

c) Retirement benefit obligations
Determining the amount of the group's retirement benefit obligations and the net costs of providing such benefits requires assumptions to be made concerning long term interest rates, inflation, salary and pension increases, investment returns and longevity of current and future pensioners Changes in these assumptions could significantly impact the amount of the obligations or the cost of providing such benefits The group makes assumptions concerning these matters with the assistance of advice from independent qualified actuaries Details of the assumptions made are set out in note 27 to the financial statements

d) Unbilled revenue
Severn Trent Water raises bills and recognises revenue in accordance with its right to receive revenue in line with the limits established by the periodic regulatory price review processes For water and waste water customers with water meters, the amount recognised is dependent upon the volume supplied including an estimate of the sales value of units supplied between the date of the last meter read and the year end Meters are read on a cyclical basis and the group recognises revenue for unbilled amounts based on estimated usage from the last billing to the end of the financial year The estimated usage is based on historical data, judgement and assumptions

e) Provision for impairment of trade receivables
Provisions are made against Severn Trent Water's trade receivables based on historical experience of levels of recovery from accounts in a particular ageing category The actual amounts collected could differ from the estimated level of recovery which could impact operating results

5 Segmental analysis

The group has two reportable segments Severn Trent Water and Severn Trent Services The key factor determining the identification of reportable segments is the regulatory environment in which the businesses operate Severn Trent Water is subject to economic regulation by Ofwat and operates under a licence to provide water and sewerage services within a defined geographical region in England and Wales Severn Trent Services is not subject to economic regulation and operates in markets in the USA, Europe and Asia

The Severn Trent Executive Committee (STEC) is considered to be the group's chief operating decision maker The reports provided to STEC include segmental information prepared on the basis described above Details of Severn Trent Water's operations are described on pages 10 to 15 of the Business Review and those of Severn Trent Services on pages 16 to 19

The group has a large and diverse customer base and there is no significant reliance on any single customer

5 Segmental analysis (continued)

The measure of profit or loss that is reported to STEC for the segments is profit before interest, tax and exceptional items (underlying PBIT) A segmental analysis of sales and underlying PBIT is presented below

2011	Severn Trent Water £m	Severn Trent Services £m
External sales	1,388 9	321 7
Inter-segment sales	0 9	14 4
Total sales	1,389 8	336 1
Profit before interest, tax and exceptional items	503 7	25 7
Exceptional items	(13 0)	(4 5)
Profit before interest and tax	490 7	21 2
Profit before interest, tax and exceptional items is stated after		
Amortisation of intangible assets	23 6	1 6
Depreciation of property plant and equipment	247 4	6 4
Profit on disposal of fixed assets	(2 1)	(0 5)

2010	Severn Trent Water £m	Severn Trent Services £m
External sales	1,383 6	320 3
Inter-segment sales	1 7	16 2
Total sales	1,385 3	336 5
Profit before interest, tax and exceptional items	541 3	28 7
Exceptional items	(42 1)	(7 6)
Profit before interest and tax	499 2	21 1
Profit before interest, tax and exceptional items is stated after charging		
Amortisation of intangible assets	23 4	1 6
Depreciation of property plant and equipment	232 5	6 1
Profit on disposal of fixed assets	(4 3)	(0 2)

The group's treasury and tax affairs are managed centrally by the Group Treasury and Tax Departments Finance costs are managed on a group basis and hence interest income and costs are not reported at the segmental level Tax is not reported to STEC on a segmental basis

Interests in joint ventures and associates are not material and are not included in the segmental reports reviewed by STEC

Separate segmental analyses of assets and liabilities are not reviewed by STEC The balance sheet measure reviewed by STEC on a segmental basis is capital employed which includes the following components

2011	Severn Trent Water £m	Severn Trent Services £m
Operating assets	6,864 8	203 8
Goodwill	–	68 3
Interests in joint ventures and associates	0 1	4 7
Segment assets	6,864 9	276 8
Segment operating liabilities	(959 7)	(87 8)
Capital employed	5,905 2	189 0

Notes to the group financial statements (continued)

For the year ended 31 March 2011

5 Segmental analysis (continued)

2010	Severn Trent Water (Restated see note 3) £m	Severn Trent Services £m
Operating assets	6,731 4	215 3
Goodwill	–	70 6
Interests in joint ventures and associates	0 2	4 7
Segment assets	6,731 6	290 6
Segment operating liabilities	(1,026 8)	(92 0)
Capital employed	5,704 8	198 6

Operating assets comprise other intangible assets, property plant and equipment, inventory and trade and other receivables

Operating liabilities comprise trade and other payables, retirement benefit obligations and provisions

The comparative figures for Severn Trent Water have been restated to reflect the impact of IFRIC 18, which is described in note 3

Additions to other intangible assets and property, plant and equipment were as follows

2011	**Severn Trent Water £m**	**Severn Trent Services £m**
Other intangible assets	18 3	2 6
Property, plant and equipment	370 7	4 9

2010	Severn Trent Water (Restated see note 3) £m	Severn Trent Services £m
Other intangible assets	44 4	3 2
Property, plant and equipment	538 9	13 0

The comparative figures for Severn Trent Water have been restated to reflect the impact of IFRIC 18, which is described in note 3

The reportable segments' revenue is reconciled to group turnover as follows

	2011 £m	2010 £m
Severn Trent Water	**1,389 8**	1,385 3
Severn Trent Services	**336 1**	336 5
Other	**8 1**	5 3
Inter-segment sales	**(22 7)**	(23 2)
Group turnover	**1,711 3**	1,703 9

5 Segmental analysis (continued)

Segmental underlying PBIT is reconciled to the group's profit before tax and discontinued operations as follows

	2011 £m	2010 £m
Underlying PBIT		
- Severn Trent Water	**503 7**	541 3
- Severn Trent Services	**25.7**	28 7
Corporate and other costs	**(12 5)**	(14 2)
Consolidation adjustments	**2 2**	1 3
Group underlying PBIT	**519.1**	557 1
Exceptional items		
- Severn Trent Water	**(13 0)**	(42 1)
- Severn Trent Services	**(4 5)**	(7 6)
Corporate	**(3 9)**	–
Share of results of associates and joint ventures	**0 1**	0 1
Net finance costs	**(230 6)**	(218 8)
(Losses)/gains on financial instruments	**(14 2)**	45 7
Profit before tax and discontinued operations	**253 0**	334 4

The reportable segments' assets are reconciled to the group's total assets as follows

	2011 £m	2010 (Restated see note 3) £m
Segment assets		
- Severn Trent Water	**6,864 9**	6,731 6
- Severn Trent Services	**276 8**	290 6
Corporate assets	**46 8**	21 7
Financial assets	**192 4**	206 7
Cash and cash equivalents	**315.2**	227 8
Available for sale financial assets	**0 1**	0 1
Consolidation adjustments	**(47 7)**	(28 6)
Total assets	**7,648 5**	7,449 9

The consolidation adjustments include intra-group debtors and unrealised profits on fixed assets

The comparative figures for Severn Trent Water have been restated to reflect the impact of IFRIC 18, which is described in note 3

Notes to the group financial statements (continued)

For the year ended 31 March 2011

5 Segmental analysis (continued)

The reportable segments' liabilities are reconciled to the group's total liabilities as follows

	2011 £m	2010 (Restated see note 3) £m
Segment liabilities		
- Severn Trent Water	**(959.7)**	(1,026 8)
- Severn Trent Services	**(87 8)**	(92 0)
Corporate and other	**(59.0)**	(49 7)
Borrowings	**(4,344 4)**	(4,176 5)
Derivative financial liabilities	**(122 5)**	(144 7)
Current tax	**(67.0)**	(67 2)
Deferred tax	**(919 4)**	(956 4)
Consolidation adjustments	**17 4**	10 4
Total liabilities	**(6,542 4)**	(6,502 9)

The consolidation adjustments include intra-group creditors

The comparative figures for Severn Trent Water have been restated to reflect the impact of IFRIC 18, which is described in note 3

Geographical areas

The group's sales were derived from the following countries

	2011 £m	2010 £m
UK	**1,465 4**	1,459 2
USA	**154 0**	145 1
Other	**91 9**	99 6
	1,711 3	1,703 9

The group's non-current assets (excluding financial instruments, deferred tax assets and post employment benefit assets) were located in the following countries

	2011 £m	2010 (Restated see note 3) £m
UK	**6,550.8**	6,428 2
USA	**58 3**	61 3
Other	**26.2**	26 6
	6,635.3	6,516 1

The comparative figures have been restated to reflect the impact of IFRIC 18, which is described in note 3

6 Revenue

	2011 £m	2010 (Restated) £m
Water and sewerage services	**1,380 0**	1,377 0
Other services	**192 3**	190 4
Sale of goods	**103 2**	100 5
Service concession arrangements (note 36)	**35 8**	36 0
Total turnover	**1,711 3**	1,703 9
Interest receivable (note 10)	**7 5**	9 8
Total revenue	**1,718.8**	1,713 7

The significant categories of revenue have been redefined to better reflect the nature of the activities performed The prior year figures have been restated accordingly Revenue from service concessions arrangements is now disclosed separately to other service income and revenue from long term contracts to supply goods is included in sale of goods

7 Operating costs

	2011 Before exceptional costs £m	2011 Exceptional costs £m	2011 Total £m	2010 Before exceptional costs £m	2010 Exceptional costs £m	2010 Total £m
Wages and salaries	**263 7**	**3.1**	**266 8**	276 8	14 6	291 4
Social security costs	**15 8**	**0.4**	**16.2**	18 5	0 5	19 0
Pension costs	**27 0**	**0.6**	**27 6**	19 1	7 5	26 6
Share based payments	**4 6**	**–**	**4 6**	5 1	–	5 1
Total employee costs	**311.1**	**4.1**	**315 2**	319 5	22 6	342 1
Power	**57.9**	**–**	**57 9**	56 0	–	56 0
Raw materials and consumables	**135.3**	**0 6**	**135 9**	116 9	0 4	117 3
Rates	**62.4**	**–**	**62.4**	61 0	0 8	61 8
Charge for bad and doubtful debts	**35 2**	**–**	**35.2**	35 1	0 1	35 2
Service charges	**32 6**	**–**	**32 6**	31 1	–	31 1
Depreciation of property, plant and equipment	**251 5**	**–**	**251.5**	236 1	0 8	236 9
Amortisation of intangible fixed assets	**25 4**	**–**	**25 4**	25 2	5 8	31 0
Hired and contracted services	**177 6**	**7.2**	**184 8**	145 9	4 9	150 8
Operating leases rentals						
- land and buildings	**4 3**	**0 4**	**4 7**	4 2	5 4	9 6
- other	**0 8**	**–**	**0.8**	1 1	0 1	1 2
Hire of plant and machinery	**7 8**	**–**	**7 8**	8 2	0 1	8 3
Research and development expenditure	**4 5**	**–**	**4.5**	5 6	–	5 6
Profit on disposal of property, plant and equipment	**(2.6)**	**–**	**(2 6)**	(4 5)	–	(4 5)
Foreign exchange gains	**(0.9)**	**–**	**(0 9)**	–	–	–
Water and sewerage infrastructure maintenance expenditure	**96 9**	**–**	**96 9**	104 5	–	104 5
Other operating costs	**60 8**	**9.1**	**69 9**	89 5	7 0	96 5
	1,260 6	**21.4**	**1,282 0**	1,235 4	48 0	1,283 4
Release from deferred income	**(8 4)**	**–**	**(8 4)**	(7 5)	–	(7 5)
Own work capitalised	**(60 0)**	**–**	**(60.0)**	(81 1)	–	(81 1)
Total operating costs	**1,192.2**	**21 4**	**1,213.6**	1,146 8	48 0	1,194 8

Further details of exceptional costs are given in note 8

During the year the following fees were charged by the auditors

	2011 £m	2010 £m
Fees payable to the company's auditors for		
- the audit of the company's annual accounts	**0.1**	0 1
- the audit of the company's subsidiaries pursuant to legislation	**0 4**	0 4
- audit fees payable to associates of the company's auditors	**0 1**	0 1
Total audit fees	**0 6**	0 6
Fees payable to the company's auditors and their associates for other services to the group		
- other services pursuant to legislation	**0.2**	0 2
- other services relating to taxation	**0.2**	–
- services relating to corporate finance	**–**	0 1
Total non-audit fees	**0.4**	0 3

Details of directors' remuneration are set out in the Directors' remuneration report on pages 51 to 55

Notes to the group financial statements (continued)

For the year ended 31 March 2011

8 Exceptional items

	2011 £m	2010 £m
Restructuring programmes		
- Severn Trent Water	**13 0**	42 1
- Severn Trent Services	**0.7**	5 9
Exceptional restructuring costs	**13.7**	48 0
Costs relating to regulatory matters (see note 35)		
- Severn Trent Services	**3 8**	–
- Corporate and other	**3 9**	–
Exceptional costs relating to regulatory matters	**7 7**	–
Total exceptional operating costs	**21.4**	48 0
Exceptional loss on disposal of business	**–**	1 7
Total exceptional items	**21 4**	49 7

9 Employee numbers

Average number of employees (including executive directors) during the year

	2011 Number	2010 Number
By type of business		
Severn Trent Water	**5,236 6**	5,685 8
Severn Trent Services	**3,031 7**	3,090 0
Corporate and Other	**13 2**	11 7
	8,281 5	8,787 5

10 Finance income

	2011 £m	2010 £m
Interest revenue earned on		
Bank deposits	**3 8**	7 0
Other financial income	**3 7**	2 8
Total interest revenue	**7 5**	9 8
Expected return on defined benefit scheme assets	**93.2**	71 1
Total finance income	**100.7**	80 9

11 Finance costs

	2011 £m	2010 £m
Interest on bank loans and overdrafts	**6 9**	7 6
Interest on other loans	**214.1**	195 0
Interest on finance leases	**11.1**	10 1
Total borrowing costs	**232.1**	212 7
Other financial expenses	**0 8**	0 9
Interest cost on defined benefit scheme obligations	**98 4**	86 1
Total finance costs	**331 3**	299 7

In accordance with IAS 23 borrowing costs of £11 4 million (2010 £2 6 million) incurred funding eligible capital projects have been capitalised at an interest rate of 5 99% (2010 5 65%)

12 (Losses)/gains on financial instruments

	2011 £m	2010 £m
Gain/(loss) on cross currency swaps used as hedging instruments in fair value hedges	**17 6**	(10 9)
(Loss)/gain arising on adjustment for foreign currency debt in fair value hedges	**(10 4)**	22 3
Exchange loss on other loans	**(1 2)**	–
Loss on cash flow hedges transferred from equity	**(4 5)**	(7 6)
(Loss)/gain arising on swaps where hedge accounting is not applied	**(15 7)**	41 9
	(14 2)	45 7

The group's hedge accounting arrangements are described in note 32 g)

13 Taxation

a) Analysis of tax (credit)/charge in the year

	2011 £m	2010 £m
Current tax		
Current year at 28% (2010 28%)	**66.5**	71 3
Prior year at 28% (2010 28%)	**(34 4)**	(30 6)
Total current tax	**32 1**	40 7
Deferred tax		
Origination and reversal of temporary differences - current year	**4 6**	25 9
Origination and reversal of temporary differences - prior year	**9.5**	16 3
Exceptional credit arising from rate change	**(67 7)**	–
Total deferred tax	**(53 6)**	42 2
Total tax (credit)/charge	**(21.5)**	82 9

The prior year credit for current tax arises from the settlement in the year of certain outstanding tax positions which arose principally in the years 2005 – 2009

The exceptional deferred tax credit arises from the reduction in the rate at which the temporary differences are expected to reverse from 28% to 26%

The standard rate of corporation tax in the UK changed from 28% to 26% with effect from 1 April 2011

Notes to the group financial statements (continued)

For the year ended 31 March 2011

13 Taxation (continued)

b) Factors affecting the tax (credit)/charge in the year

The tax expense for the current year is lower (2010 lower) than the standard rate of corporation tax in the UK The differences are explained below

	2011 £m	2010 £m
Profit on ordinary activities before tax	**253 0**	334 4
Tax at the standard rate of corporation tax in the UK 28% (2010 28%)	**70 8**	93 6
Tax effect of (income not taxable)/expenditure not deductible in determining taxable profits	**(0 2)**	2 7
Effect of different rates in overseas jurisdictions	**0 5**	0 9
Adjustments in respect of prior years	**(24 9)**	(14 3)
Exceptional deferred tax credit arising from rate change	**(67 7)**	–
Total tax (credit)/charge	**(21 5)**	82 9

c) Tax charged/(credited) directly to equity

In addition to the amount (credited)/charged to the income statement, the following amounts of tax have been charged/(credited) directly to equity

	2011 £m	2010 £m
Current tax		
Tax on share based payments	**(0 3)**	(0 3)
Tax on pension contributions in excess of profit and loss charge	**–**	(0 7)
Tax on exchange differences on foreign currency hedging	**0.4**	0 4
Total current tax credited directly to equity	**0 1**	(0 6)
Deferred tax		
Tax on actuarial gains/losses	**13 2**	(34 1)
Tax on cash flow hedges	**5 3**	(1 6)
Tax on share based payments	**(1 2)**	–
Effect of change in tax rate	**(0 7)**	–
Total deferred tax charged/(credited) directly to equity	**16 6**	(35 7)

14 Dividends

Amounts recognised as distributions to equity holders in the period

	2011		2010	
	Pence per share	£m	Pence per share	£m
Final dividend for the year ended 31 March 2010 (2009)	**45 6**	**107.8**	41 1	96 5
Interim dividend for the year ended 31 March 2011 (2010)	**26 0**	**61.6**	26 7	63 2
	71 7	**169 4**	67 8	159 7
Proposed final dividend for the year ended 31 March 2011	**39 1**			

The proposed final dividend is subject to approval by shareholders at the AGM and has not been included as a liability in these financial statements

15 Earnings per share

Basic earnings per share are calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the year, excluding those held in the Severn Trent Employee Share Ownership Trust, which are treated as cancelled

For diluted earnings per share, the weighted average number of ordinary shares in issue is adjusted to assume conversion of all potentially dilutive ordinary shares These represent share options granted to employees where the exercise price is less than the average market price of the company's shares during the year

Basic and diluted earnings per share from continuing operations are calculated on the basis of profit from continuing operations attributable to the equity holders of the company

The calculation of basic and diluted earnings per share is based on the following data

Earnings

	2011 £m	2010 £m
Earnings for the purpose of basic and diluted earnings per share from operations		
Profit for the period attributable to the equity holders of the company	**272 6**	249 2

Number of shares

	2011 m	2010 m
Weighted average number of ordinary shares for the purpose of basic earnings per share	**236 7**	236 0
Effect of dilutive potential ordinary shares		
- share options and LTIPs	**1.1**	0 3
Weighted average number of ordinary shares for the purpose of diluted earnings per share	**237 8**	236 3

Adjusted earnings per share

	2011 pence	2010 pence
Adjusted basic earnings per share	**105 6**	122 8
Adjusted diluted earnings per share	**105.1**	122 6

Adjusted earnings per share figures are presented for continuing operations These exclude the effects of deferred tax, losses/gains on financial instruments and exceptional items in both 2011 and 2010 The directors consider that the adjusted figures provide a useful additional indicator of performance The denominators used in the calculations of adjusted basic and diluted earnings per share are the same as those used in the unadjusted figures set out above

The adjustments to earnings are as follows

Adjustments to earnings

	2011 £m	2010 £m
Earnings for the purpose of basic and diluted earnings per share from continuing operations	**272.6**	249 2
Adjustments for		
- exceptional items	**21 4**	49 7
- current tax related to exceptional items at 28% (2010 28%)	**(4 7)**	(5 6)
- losses/(gains) on financial instruments	**14 2**	(45 7)
- deferred tax	**(53 6)**	42 2
Earnings for the purpose of adjusted basic and diluted earnings per share	**249 9**	289 8

Notes to the group financial statements (continued)

For the year ended 31 March 2011

16 Goodwill

	2011 £m	2010 £m
Cost and net book value		
At 1 April	**70 6**	63 3
Additions	**–**	10 3
Amounts written off	**–**	(0 2)
Exchange adjustments	**(2 3)**	(2 8)
At 31 March	**68 3**	70 6

Goodwill impairment tests

Goodwill is allocated to the group's cash-generating units (CGUs) identified according to country of operation and business segment

A summary of the goodwill allocation by CGU is presented below

	2011 £m	2010 £m
Severn Trent Services		
Water Purification US	**26.2**	27 8
Contract Operations	**11.6**	12 5
UK Laboratories	**12 0**	12 0
Services Italy	**8.2**	8 0
Apliclor	**10 3**	10 3
	68 3	70 6

The recoverable amount of a CGU is determined using value in use calculations These calculations use cash flow projections based on financial budgets approved by management covering a five year period The key assumption underlying these budgets is revenue growth Assumptions are determined by management of each CGU based on past experience, current market trends and expectations of future developments

Cash flows beyond the five year period are extrapolated using an estimated nominal growth rate stated below The growth rate does not exceed the long term average growth rate for the economy in which the CGU operates The assumptions used in relation to growth rates beyond the five year period and discount rates were

	Nominal growth rate		Discount rate	
	2011 %	2010 %	2011 %	2010 %
Water Purification US	**3 0**	3 0	**7 3**	7 8
Contract Operations	**3 0**	3 0	**7 7**	8 9
UK Laboratories	**3 0**	3 0	**7 3**	8 9
Services Italy	**3 0**	3 0	**11 0**	10 1
Apliclor	**3 0**	3 0	**11 6**	10 0

The weighted average growth rates used are consistent with the forecasts included in industry reports The discount rates used are pre-tax and reflect specific risks relating to the CGU

16 Goodwill (continued)

Changes in the growth rate outside the five year period or in the discount rate applied to the cash flows may cause a CGU's carrying value to exceed its recoverable amount Where such a change is considered reasonably possible, the amount by which the recoverable amount exceeded its carrying value, and the amount by which the growth rate and discount rate would have to change, is set out below for each CGU

	Surplus of recoverable amount over carrying amount £m	Change required for recoverable amount to equal carrying amount: Growth rate percentage points	Discount rate percentage points
Severn Trent Services			
UK Laboratories	22 0	(4 7)	3 5
Services Italy	1 0	(0 3)	0 1
Apliclor	–	(0 4)	0 2

In the opinion of the directors, the changes in growth rate or discount rate that would be required to reduce the recoverable amounts of Water Purification US and Contract Operations below their carrying value are not reasonably possible

17 Intangible assets

	Computer software		Other	
	Internally generated £m	Purchased £m	Internally generated £m	Total £m
Cost				
At 1 April 2009	104 3	154 9	18 7	277 9
Additions	13 1	31 5	3 1	47 7
Acquisition of businesses	–	0 3	–	0 3
Disposals	–	(1 2)	–	(1 2)
Disposal of businesses	–	(0 1)	(0 1)	(0 2)
Reclassifications	–	0 1	0 4	0 5
Exchange adjustments	–	(0 2)	(0 3)	(0 5)
At 1 April 2010	117 4	185 3	21 8	324 5
Additions	4 1	14 6	2 2	20 9
Disposals	–	(29 8)	–	(29 8)
Reclassifications	–	0 2	1 2	1 4
Exchange adjustments	–	(0 2)	(0 4)	(0 6)
At 31 March 2011	**121.5**	**170 1**	**24 8**	**316 4**
Amortisation				
At 1 April 2009	(62 0)	(84 1)	(10 5)	(156 6)
Amortisation for year	(9 1)	(14 7)	(1 4)	(25 2)
Exceptional impairment	(2 3)	(3 5)	–	(5 8)
Disposals	–	1 1	–	1 1
Disposal of businesses	–	0 1	0 1	0 2
Exchange adjustments	–	0 2	0 1	0 3
At 1 April 2010	(73 4)	(100 9)	(11 7)	(186 0)
Amortisation for year	(9 4)	(15 1)	(0 9)	(25 4)
Disposals	–	29 7	–	29 7
Exchange adjustments	–	0 1	0 1	0 2
At 31 March 2011	**(82.8)**	**(86.2)**	**(12 5)**	**(181 5)**
Net book value				
At 31 March 2011	**38 7**	**83.9**	**12.3**	**134 9**
At 31 March 2010	44 0	84 4	10 1	138 5

Other assets primarily comprise capitalised development costs and patents

Notes to the group financial statements (continued)

For the year ended 31 March 2011

18 Property, plant and equipment

	Land and buildings £m	Infrastructure assets £m	Fixed plant and equipment £m	Movable plant £m	Total £m
Cost					
At 1 April 2009	2,330 0	3,942 2	2,902 1	60 4	9,234 7
Additions (restated see note 3)	162 2	119 8	270 0	10 4	562 4
Acquisition of businesses	0 3	–	0 9	–	1 2
Disposals	(7 4)	–	(22 0)	(10 0)	(39 4)
Disposal of businesses	–	–	(0 3)	–	(0 3)
Reclassifications	(1 4)	–	1 0	(0 1)	(0 5)
Exchange adjustments	(0 4)	–	(1 7)	(0 7)	(2 8)
At 1 April 2010	2,483 3	4,062 0	3,150 0	60 0	9,755 3
Additions	94 7	130 2	153 5	3 8	382 2
Disposals	(7 5)	(0 5)	(32 0)	(6 4)	(46 4)
Reclassifications	(0 3)	–	(3 9)	–	(4 2)
Exchange adjustments	(0 3)	–	(1 4)	(0 7)	(2 4)
At 31 March 2011	**2,569 9**	**4,191.7**	**3,266 2**	**56 7**	**10,084.5**
Depreciation					
At 1 April 2009	(725 8)	(1,040 2)	(1,457 5)	(31 1)	(3,254 6)
Charge for the year	(51 7)	(25 7)	(150 3)	(8 4)	(236 1)
Exceptional impairment	–	–	(0 8)	–	(0 8)
Acquisition of businesses	–	–	(0 7)	–	(0 7)
Disposals	7 3	–	21 7	8 0	37 0
Reclassifications	0 9	–	(1 0)	0 1	–
Exchange adjustments	0 2	–	1 2	0 5	1 9
At 1 April 2010	(769 1)	(1,065 9)	(1,587 4)	(30 9)	(3,453 3)
Charge for the year	(56 3)	(27 6)	(160 5)	(7 1)	(251 5)
Disposals	7 3	–	31 5	5 0	43 8
Reclassifications	1 9	–	–	–	1 9
Exchange adjustments	0 1	–	1 0	0 5	1 6
At 31 March 2011	**(816 1)**	**(1,093 5)**	**(1,715.4)**	**(32 5)**	**(3,657 5)**
Net book value					
At 31 March 2011	**1,753 8**	**3,098.2**	**1,550.8**	**24 2**	**6,427 0**
At 31 March 2010	1,714 2	2,996 1	1,562 6	29 1	6,302 0

The comparative figures have been restated to reflect the impact of IFRIC 18 as set out in note 3 The amounts included for additions to infrastructure assets and fixed plant and equipment increased by £41 1 million and £0 4 million respectively

The carrying amount of property, plant and equipment includes the following amounts in respect of assets held under finance leases

	Land and buildings £m	Infrastructure assets £m	Fixed plant and equipment £m	Movable plant £m	Total £m
Net book value					
At 31 March 2011	**–**	**120 1**	**96 4**	**–**	**216 5**
At 31 March 2010	–	121 1	116 4	–	237 5

Property, plant and equipment includes £433 8 million (2010 £459 6 million) in respect of assets in the course of construction for which no depreciation is charged

19 Interests in joint ventures

	2011 £m	2010 £m
Group's share of		
Long term assets	**0 2**	–
Current assets	**0 6**	1 8
Current liabilities	**(0 6)**	(1 5)
	0 2	0 3
Group's share of		
Turnover	**3 3**	4 7
Operating costs	**(3 3)**	(4 7)
Profit before tax	–	–
Tax	–	–
Profit after tax	–	–

As at 31 March 2011 and 2010 the joint ventures had no significant contingent liabilities to which the group was exposed and the group did not have any significant contingent liabilities in relation to its interests in the joint ventures The group had no capital commitments in relation to its interests in the joint ventures

Particulars of the group's principal joint venture undertakings at 31 March 2011 were

Name	Country of incorporation	Proportion of ownership	Proportion of voting power
Cognica Limited	Great Britain	50%	50%
Jackson Water Partnership	USA	70%	See below

The partnership agreement for the Jackson Water Partnership requires that certain key decisions require the unanimous consent of the partners and consequently the partnership has been accounted for as a joint venture

20 Interests in associates

	2011 £m	2010 £m
At 1 April 2009	**4 6**	4 8
Share of profits	**0 1**	0 1
Other movements	**0 1**	(0 3)
At 31 March 2010	**4 8**	4 6
Group's share of		
Total assets	**26.1**	25 6
Total liabilities	**(21.3)**	(21 0)
	4 8	4 6
Turnover	**0.1**	8 0
Profit before tax	**0 1**	0 1

At 31 March 2011 and 2010 the associate company had no significant contingent liabilities to which the group was exposed The group had no capital commitments in relation to its interests in the associate at 31 March 2011 and 2010

The principal associate at 31 March 2011 was

Name	Country of operation and incorporation	Equity interest	Percentage of share capital held	Nature of business
Servizio Idrico Integrato S c p a	Italy	16,279,127 of €1	30%	Water and sewerage

The group has given certain guarantees in respect of the associate's borrowings The guarantees are limited to €11 2m (2010 €11 2m) The group does not expect any liabilities to arise from these arrangements

Notes to the group financial statements (continued)

For the year ended 31 March 2011

21 Inventory

	2011 £m	2010 £m
Inventory and work in progress	**27 1**	26 5

22 Trade and other receivables

	2011 £m	2010 £m
Trade receivables	**286 6**	288 4
Less provisions for impairment of receivables	**(98.5)**	(91 8)
Trade receivables net	**188 1**	196 6
Receivables from related parties	**0 2**	0 2
Other amounts receivable	**40 1**	42 4
Prepayments and accrued income	**250 1**	233 6
	478 5	472 8

The carrying values of trade and other receivables are reasonable approximations of their fair values

Prepayments and accrued income include £27 1 million (2010 £26 2 million) in respect of amounts due from customers for contract work and £49 7 million (2010 £43 0 million) which is recoverable after more than one year

Credit control policies and procedures are determined at the individual business unit level By far the most significant business unit of the group is Severn Trent Water Limited, which represents 81% of group turnover and 68% of net trade receivables Severn Trent Water has a statutory obligation to provide water and sewerage services to customers within its region Therefore there is no concentration of credit risk with respect to its trade receivables and the credit quality of its customer base reflects the wealth and prosperity of all of the commercial businesses and domestic households within its region None of the other business units are individually significant to the group

Movements on the doubtful debts provision were as follows

	2011 £m	2010 £m
At 1 April	**91.8**	93 0
Amounts written off during the year	**(28 5)**	(36 3)
Charge for bad and doubtful debts	**35.2**	35 2
Exchange adjustments	**–**	(0 1)
At 31 March	**98.5**	91 8

22 Trade and other receivables (continued)

Included in trade receivables are balances with a carrying amount of £146 0 million (2010 £139 2 million) which were past due at the reporting date but for which no specific provision has been made as the collective impairment recorded against such assets is considered to be sufficient allowance for the risk of non-collection of such balances

The aged analysis of past due receivables that were not individually impaired is as follows

	2011 £m	2010 £m
Up to 90 days	**47 7**	52 6
91-365 days	**60 6**	60 4
1-2 years	**25 0**	19 4
2-3 years	**8 4**	5 9
More than 3 years	**4 3**	0 9
Total	**146 0**	139 2

Included in the allowance for doubtful debts are provisions amounting to £24 million (2010 £13 1 million) against specific trade receivables The age of the impaired receivables was as follows

	2011 £m	2010 £m
Up to 90 days	**2 5**	1 6
91-365 days	**18 1**	15 4
1-2 years	**4.1**	1 2
2-3 years	**3 7**	0 4
More than 3 years	**4 7**	3 1
Total	**33.1**	21 7

23 Cash and cash equivalents

	2011 £m	2010 £m
Cash at bank and in hand	**66 6**	44 1
Short term deposits	**248 6**	183 7
	315.2	227 8

Of the £248 6 million (2010 £183 7 million) of short term bank deposits, £28 4 million (2010 £27 4 million) is held as security deposits for insurance obligations and is not available for use by the group

24 Finance leases

Obligations under finance lease are as follows

	2011 £m	2010 £m
Gross obligations under finance leases	**316 6**	385 5
Less future finance charges	**(49 9)**	(84 7)
Present value of lease obligations	**266 7**	300 8

Notes to the group financial statements (continued)

For the year ended 31 March 2011

24 Finance leases (continued)

A maturity analysis of gross obligations under finance leases is presented in note 32 Net obligations under finance leases fall due as follows

	2011 £m	2010 £m
Within one year	**13.5**	47 3
In the second year	**16 4**	12 9
In the third to fifth year inclusive	**84 1**	57 3
After more than five years	**152 7**	183 3
Included in non-current liabilities	**253 2**	253 5
	266 7	300 8

The remaining terms of finance leases ranged from 4 to 21 years at 31 March 2011 Interest terms are set at the inception of the leases Leases with capital outstanding of £266 7 million (2010 £159 0 million) bear fixed interest at a weighted average rate of 5 4% (2010 5 4%) The lease obligations are secured against the related assets

There were no contingent rents, escalation clauses or material renewal or purchase options The terms of the finance leases do not impose restriction on dividend payments, additional debt or further leasing

25 Trade and other payables

	2011 £m	2010 (Restated see note 3) £m
Current liabilities		
Trade payables	**31 8**	28 4
Social security and other taxes	**6 8**	6 0
Other payables	**32 1**	34 9
Accruals and deferred income	**320 5**	395 1
	391 2	464 4
Non-current liabilities		
Trade payables	**0 5**	–
Other payables	**2 1**	0 3
Deferred income	**345 9**	280 6
Accrued expenses	**19 3**	4 0
	367 8	284 9

The directors consider that the carrying value of trade payables is not materially different from their fair values

Accruals and deferred income includes nil (2010 nil) in respect of amounts due to customers for contract work

The comparative figures for accruals and deferred income have been restated by £0 2 million and £41 3 million respectively (see note 3)

26 Deferred tax

An analysis of the movements in the major deferred tax liabilities and assets recognised by the group is set out below

	Accelerated tax depreciation £m	Retirement benefit obligation £m	Tax losses £m	Fair value of financial instruments £m	Other £m	Total £m
At 1 April 2009	1,066 0	(65 3)	(10 5)	(44 2)	2 4	948 4
Charge to income	44 2	–	2 7	12 3	(17 0)	42 2
Charge to equity	–	(34 1)	–	(1 6)	–	(35 7)
Transfers	51 0	–	–	–	(51 0)	–
Acquisitions/disposals	0 4	–	–	–	–	0 4
Exchange differences	0 2	–	0 7	–	0 2	1 1
At 1 April 2010	1,161 8	(99 4)	(7 1)	(33 5)	(65 4)	956 4
Charge to income	13 6	3 2	0 3	1 0	(4 0)	14 1
Credit to income arising from rate change	(77 5)	3 1	–	1 2	5 5	(67 7)
Charge to equity	–	13 2	–	5 3	(1 2)	17 3
Credit to equity arising from rate change	(5 5)	4 0	–	1 2	(0 4)	(0 7)
Exchange differences	(0 5)	–	0 4	–	0 1	–
At 31 March 2011	**1,091 9**	**(75.9)**	**(6 4)**	**(24 8)**	**(65.4)**	**919.4**

Certain deferred tax assets and liabilities have been offset The offset amounts are as follows

	2011 £m	2010 £m
Deferred tax asset to be recovered after more than 12 months	**(14 4)**	(13 6)
Deferred tax asset to be recovered within 12 months	–	(4 0)
	(14.4)	(17 6)
Deferred tax liability to be settled after more than 12 months	**933.8**	974 0
Deferred tax liability to be settled within 12 months	–	–
	933.8	974 0
	919 4	956 4

27 Retirement benefit schemes

a) Defined benefit schemes

(i) Amount included in the balance sheet arising from the group's obligations under defined benefit schemes

	2011 £m	2010 £m
Fair value of scheme assets		
Equities	**798.8**	745 7
Gilts	**41.3**	270 8
Corporate bonds	**530 6**	307 0
Property	**95.0**	61 1
Cash	**7 7**	8 4
Total fair value of assets	**1,473 4**	1,393 0
Present value of the defined benefit obligations – funded schemes	**(1,757.4)**	(1,740 3)
	(284 0)	(347 3)
Present value of the defined benefit obligations – unfunded schemes	**(8.1)**	(7 6)
Liability recognised in the balance sheet	**(292.1)**	(354 9)

Notes to the group financial statements (continued)

For the year ended 31 March 2011

27 Retirement benefit schemes (continued)

Movements in the fair value of the scheme assets were as follows

	2011 £m	2010 £m
Fair value at 1 April	**1,393 0**	1,075 0
Expected return on scheme assets	**93 2**	71 1
Contributions from the sponsoring companies	**40 0**	39 6
Contributions from scheme members	**6 1**	6 8
Actuarial gains recognised in the statement of comprehensive income	**12 2**	270 4
Benefits paid	**(71 1)**	(69 9)
Fair value at 31 March	**1,473 4**	1,393 0

Movements in the present value of the defined benefit obligations were as follows

	2011 £m	2010 £m
Present value at 1 April	**1,747 9**	1,308 0
Service cost	**22 7**	14 7
Interest cost	**98 4**	86 1
Curtailment/settlement costs	**–**	7 4
Contributions from scheme members	**6 1**	6 8
Actuarial (gains)/losses recognised in the statement of comprehensive income	**(38 5)**	394 8
Benefits paid	**(71 1)**	(69 9)
Present value at 31 March	**1,765 5**	1,747 9

Of which

	2011 £m	2010 £m
Amounts relating to funded schemes	**1,757.4**	1,747 9
Amounts relating to unfunded schemes	**8.1**	–
Present value at 31 March	**1,765.5**	1,747 9

(ii) Amounts recognised in the income statement in respect of these defined benefit schemes

	2011 £m	2010 £m
Amounts charged to operating costs		
Current service cost	**(22 7)**	(14 7)
Exceptional curtailment charge	**–**	(7 4)
	(22.7)	(22 1)
Amounts charged to finance costs		
Interest cost	**(98.4)**	(86 1)
Amounts credited to finance income		
Expected return on scheme assets	**93 2**	71 1
Total amount charged to the income statement	**(27 9)**	(37 1)

The actual return on scheme assets was a gain of £105 4 million (2010 gain of £341 5 million)

Actuarial gains and losses have been reported in the statement of comprehensive income The cumulative amount of actuarial gains and losses recognised in the statement of comprehensive income since the adoption of IFRSs is a net loss of £169 4 million (2010 net loss of £220 1 million)

27 Retirement benefit schemes (continued)

(iii) Background

The group operates a number of defined benefit pension schemes in the UK, covering the majority of UK employees The defined benefit schemes are funded to cover future salary and pension increases and their assets are held in separate funds administered by trustees The trustees are required to act in the best interests of the schemes' beneficiaries A formal actuarial valuation of each scheme is carried out on behalf of the trustees at triennial intervals by an independent professionally qualified actuary Under the defined benefit schemes, members are entitled to retirement benefits calculated as a proportion (varying between $1/_{30}$ and $1/_{80}$ for each year of service) of their salary for the final year of employment with the group or, if higher, the average of the highest three consecutive years' salary in the last ten years of employment

The final salary sections of all of the pension schemes listed below are closed to new entrants and the age profile of scheme participants is expected to rise and hence service costs are also expected to rise in the future

On 11 May 2011, Severn Trent announced it is consulting with its 6,000 plus UK employees on proposed changes to its pension arrangements, which would see all existing pensions replaced by one new defined contribution scheme Under the new proposals, the group would close its defined benefit scheme to future accrual, whilst protecting the benefits already built up by members

The UK defined benefit schemes and the date of their last formal actuarial valuation are as follows

	Date of last formal actuarial valuation
Severn Trent Pension scheme (STPS)*	31 March 2007
Severn Trent Mirror Image Pension Scheme	31 March 2009

* The STPS is by far the largest of the group's UK defined benefit schemes

The group has an obligation to pay pensions to a number of former employees, whose benefits would otherwise have been restricted by the Finance Act 1989 earnings cap Provision for such benefits amounting to £8 1 million (2010 £7 6 million) is included as an unfunded scheme within the retirement benefit obligation

(iv) Actuarial assumptions

The major assumptions used in the valuation of the STPS (also the approximate weighted average of assumptions used for the valuations of all group schemes) were as follows

	2011 %	2010 %
Price inflation	**3 50**	3 60
Salary increases	**4 00**	4 10
Pension increases in payment	**3 50**	3 60
Pension increases in deferment	**3 50**	3 60
Discount rate	**5 60**	5 70
Long term rate of return on		
Equities	**7 85**	8 00
Gilts	**4 35**	4 50
Corporate bonds	**5 60**	5 70
Property	**6 85**	7 00
Cash	**4 25**	4 50

The assumption for price inflation is derived from the difference between the yields on longer term fixed rate gilts and on index-linked gilts The discount rate is set by reference to AA rated sterling corporate 17 year bonds

The expected rate of return on scheme assets is based on market expectations at the beginning of the period for returns over the life of the benefit obligation For gilts and corporate bonds the expected rates of return are based on market yields For equities, an equity risk premium has been added to the gilt rate

The mortality assumptions adopted are based on mortality tables applicable to the sex and year of birth of individual members, with allowance for the CMI 2010 future improvements and a 0 5% trend For men the assumptions are based on 110% of the "SAPS" S1NMA_L tables and for women on 78% of the S1NFA_L tables These have been based on a mortality investigation carried out in conjunction with the valuation of the STPS as at 31 March 2010 on behalf of the Trustees

The life expectancies implied by the mortality assumptions adopted at each year end are as follows

	Years	Years
Age to which current pensioners aged 65 are expected to live		
- men	**87 4**	85 3
- women	**91 0**	88 6
Age to which future pensioners aged 45 at the balance sheet date are expected to live		
- men	**88.0**	86 5
- women	**91.8**	89 6

Notes to the group financial statements (continued)

For the year ended 31 March 2011

27 Retirement benefit schemes (continued)

(iv) Actuarial assumptions (continued)
The calculation of the scheme liabilities is sensitive to the actuarial assumptions and in particular to the assumptions relating to discount rate, price inflation and mortality The following table summarises the estimated impact on scheme liabilities and service cost resulting from changes to key actuarial assumptions whilst holding all other assumptions constant

Assumption	Change in assumption	Impact on scheme liabilities
Discount rate	Increase/decrease by 0 1%	Decrease/increase by £30 million
Price inflation	Increase/decrease by 0 1%	Increase/decrease by £25 million
Mortality	Increase in life expectancy by 1 year	Increase by £45 million

(v) Contributions to the schemes
Contribution rates are set in consultation with the trustees for each scheme and each participating employer The triennial actuarial valuation of the STPS is currently under discussion with the trustees It is therefore not possible to determine the level of contributions that will be payable in the year ending 31 March 2012

(vi) History of actual and expected performance of pension scheme assets and liabilities

	2011 £m	2010 £m	2009 £m	2008 £m	2007 £m
Present value of defined benefit obligations	**(1,765 5)**	(1,747 9)	(1,308 0)	(1,458 3)	(1,499 7)
Fair value of scheme assets	**1,473 4**	1,393 0	1,075 0	1,332 3	1,364 6
Deficit in schemes	**(292 1)**	(354 9)	(233 0)	(126 0)	(135 1)
Difference between actual and expected return on scheme assets	**12 2**	270 4	(329 8)	(125 7)	(10 6)
Experience adjustments on scheme liabilities	**105 1**	19 8	(7 9)	(64 3)	(3 7)

b) Defined contribution schemes
The group also operates defined contribution arrangements for certain of its UK and overseas employees In September 2001, the Severn Trent Group Pension Scheme (an occupational defined contribution scheme) was established to ensure compliance with stakeholder legislation and to provide the group with an alternative pension arrangement This was closed to new entrants on 1 April 2005 and replaced by the Severn Trent Stakeholder Pension Scheme

The total cost charged to operating costs of £4 9 million (2010 £4 5 million) represents contributions payable to these schemes by the group at rates specified in the rules of the schemes As at 31 March 2011, all contributions (2010 100%) due in respect of the current reporting period had been paid over to the schemes

28 Provisions

	Restructuring £m	Insurance £m	Onerous contracts £m	Terminated operations and disposals £m	Other £m	Total £m
At 1 April 2010	10 9	22 1	12 4	5 6	2 9	53 9
Charged to income statement	2 0	9 0	(2 3)	(1 8)	(0 1)	6 8
Utilisation of provision	(9 5)	(8 0)	(0 8)	–	(0 7)	(19 0)
Other movements	(0 1)	–	(2 4)	–	(1 0)	(3 5)
Exchange differences	–	–	–	(0 1)	(0 1)	(0 2)
At 31 March 2011	**3 3**	**23 1**	**6 9**	**3 7**	**1 0**	**38.0**

	2011 £m	2010 £m
Included in		
Current liabilities	**12 6**	25 5
Non-current liabilities	**25 4**	28 4
	38 0	53 9

28 Provisions (continued)

The restructuring provision reflects costs to be incurred in respect of committed restructuring programmes

Derwent Insurance Limited, a captive insurance company, is a wholly owned subsidiary of the group Provisions for claims are made as set out in note 2 The associated outflows are estimated to arise over a period of up to five years from the balance sheet date

The onerous or loss making contract provision relates to specific contractual liabilities either assumed with businesses acquired or arising in existing group businesses, where estimated future costs are not expected to be recovered in revenues The associated outflows are estimated to occur over a period of ten years from the balance sheet date

Provisions relating to terminated operations and disposals include amounts that it is probable will be paid in respect of claims arising from services performed by these businesses and the indemnities described in note 35 b)

29 Share capital

	2011 £m	2010 £m
Total issued and fully paid share capital		
237,142,534 ordinary shares of $97^{17}/_{19}$p (2010 236,585,205)	**232 2**	231 6

Changes in share capital were as follows

	Number	£m
Ordinary shares of $97^{17}/_{19}$p		
At 1 April 2010	236,585,205	231 6
Shares issued under the Employee Sharesave Scheme	550,525	0 6
Shares issued under the group's Share Option Scheme	6,804	–
At 31 March 2011	**237,142,534**	**232 2**

30 Share premium

	2011 £m	2010 £m
At 1 April	**75 9**	71 9
Share premium arising on issue of shares for Employee Sharesave Scheme	**4 1**	4 0
At 31 March	**80 0**	75 9

31 Other reserves

	Capital redemption reserve £m	Infrastructure reserve £m	Translation exchange reserve £m	Hedging reserve £m	Total other reserves £m
At 1 April 2009	156 1	314 2	40 8	(42 4)	468 7
Total comprehensive loss for the period	–	–	(9 1)	(4 0)	(13 1)
At 1 April 2010	156 1	314 2	31 7	(46 4)	455 6
Total comprehensive (loss)/income for the period	–	–	(6 3)	15 2	8 9
At 31 March 2011	**156 1**	**314 2**	**25 4**	**(31.2)**	**464.5**

The capital redemption reserve arose on the redemption of B shares

The infrastructure reserve arose on restating infrastructure assets to fair value as deemed cost on transition to IFRS

The translation reserve arises from exchange differences on translation of the results and financial position of foreign subsidiaries as well as foreign exchange differences arising from hedges of net investment

The hedging reserve arises from gains or losses on interest rate swaps taken directly to equity under the hedge accounting provisions of IAS 39 and the transition rules of IFRS 1

Notes to the group financial statements (continued)

For the year ended 31 March 2011

32 Financial instruments

a) Capital management

It is the group's policy to access a broad range of sources of finance to obtain both the quantum required and the lowest cost compatible with the need for continued availability The group is funded using a mixture of equity and debt (including fixed rate, index linked and floating rate)

At 31 March the group's equity and debt capital comprised the following

	2011 £m	2010 £m
Cash and short term deposits	**315 2**	227 8
Bank loans	**(846 8)**	(689 8)
Other loans	**(3,230.9)**	(3,185 9)
Obligations under finance leases	**(266 7)**	(300 8)
Cross currency swaps	**160.4**	187 3
Net debt	**(3,868 8)**	(3,761 4)
Equity attributable to the company's equity shareholders	**(1,099.8)**	(940 7)
Total capital	**(4,968 6)**	(4,702 1)

b) Categories of financial assets

	2011 £m	2010 £m
Fair value through profit and loss		
Derivatives that do not qualify for hedge accounting		
- cross currency swaps	**62 3**	–
- interest rate swaps	**17.3**	19 4
Derivatives that are designated and effective as hedging instruments carried at fair value		
- cross currency swaps	**98 1**	187 3
- energy swaps	**14.7**	–
	192 4	206 7
Available for sale investments carried at fair value		
Unquoted shares	**0 1**	0 1
Loans and receivables (including cash and cash equivalents)		
Trade receivables	**188 1**	196 6
Short term deposits	**248 6**	183 7
Cash at bank in hand	**66 6**	44 1
	503 3	424 4
Total financial assets	**695 8**	631 2
Disclosed in the balance sheet as		
Non-current assets		
Derivative financial instruments	**188 1**	203 8
Available for sale financial assets	**0 1**	0 1
	188 2	203 9
Current assets		
Derivative financial instruments	**4 3**	2 9
Cash and cash equivalents	**315 2**	227 8
Trade receivables (note 22)	**188 1**	196 6
	507 6	427 3
	695 8	631 2

32 Financial instruments (continued)

c) Categories of financial liabilities

	2011 £m	2010 £m
Fair value through profit and loss		
Derivatives that do not qualify for hedge accounting		
- interest rate swaps	**(104.6)**	(125 4)
- foreign exchange forward contracts	**(0.1)**	–
Derivatives that are designated and effective as hedging instruments carried at fair value		
- interest rate swaps	**(17.8)**	(9 5)
- energy swaps	**–**	(9 8)
	(122 5)	(144 7)
Other financial liabilities		
Bank loans	**(846 8)**	(689 8)
Other loans	**(3,230 9)**	(3,185 9)
Obligations under finance leases	**(266.7)**	(300 8)
Trade payables	**(32 3)**	(28 4)
	(4,376 7)	(4,204 9)
Total financial liabilities	**(4,499 2)**	(4,349 6)
Disclosed in the balance sheet as		
Non-current liabilities		
Derivative financial instruments	**(122 4)**	(140 3)
Borrowings	**(4,320 5)**	(3,915 6)
	(4,442 9)	(4,055 9)
Current liabilities		
Derivative financial instruments	**(0 1)**	(4 4)
Borrowings	**(23.9)**	(260 9)
Trade payables (note 25)	**(32 3)**	(28 4)
	(56 3)	(293 7)
	(4,499 2)	(4,349 6)

Notes to the group financial statements (continued)

For the year ended 31 March 2011

32 Financial instruments (continued)

d) Derivative contracts

	2011		2010	
	Asset £m	Liability £m	Asset £m	Liability £m
Cross currency swaps - fair value hedges	98 1	–	187 3	–
Interest rate swaps - cash flow hedges	–	(17 8)	–	(9 5)
Energy swaps - cash flow hedges	14 7	–	–	(9 8)
Interest rate swaps - derivatives not in a formal hedging relationship	17 3	(104 6)	19 4	(125 4)
Cross currency swaps - derivatives not in a formal hedging relationship	62 3	–	–	–
Foreign exchange forward contracts - derivatives not in a formal hedging relationship	–	(0.1)	–	–
Total	192 4	(122 5)	206 7	(144 7)
Less non-current portion				
Cross currency swaps - fair value hedges	95 6	–	184 5	–
Interest rate swaps - cash flow hedges	–	(17 8)	–	(9 5)
Energy swaps - cash flow hedges	12 9	–	–	(9 7)
Interest rate swaps - derivatives not in a formal hedging relationship	17 3	(104 5)	19 3	(121 1)
Cross currency swaps - derivatives not in a formal hedging relationship	62 3	–	–	–
Foreign exchange forward contracts - derivatives not in a formal hedging relationship	–	(0.1)	–	–
Total non-current	188 1	(122 4)	203 8	(140 3)
Current portion	4 3	(0 1)	2 9	(4 4)

e) Fair values of financial instruments

Except as disclosed below, the directors consider that the carrying amount of financial assets and liabilities recorded in the financial statements approximate their fair values

	31 March 2011		31 March 2010	
	Book value £m	Fair value £m	Book value £m	Fair value £m
Bank loans - amortised cost	(846 8)	(836 8)	(689 8)	(679 1)
Other loans	(3,230 9)	(3,597.6)	(3,185 9)	(3,328 5)
Obligations under finance leases - amortised cost	(266 7)	(237 4)	(300 8)	(260 3)
	(4,344 4)	(4,671 8)	(4,176 5)	(4,267 9)

Discounted future cash flows are used to determine fair values for debt Discount rates are derived from yield curves based on quoted interest rates and are adjusted for the group's credit risk

Fair value measurements recognised in the balance sheet

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable

Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets and liabilities,

Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, and

Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data

The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows estimated and discounted based on the application of yield curves derived from quoted interest rates

Cross currency swaps and forward exchange contracts are valued by reference to quoted forward exchange rates at the balance sheet date and yield curves derived from quoted interest rates matching the maturities of the contracts

32 Financial instruments (continued)

e) Fair values of financial instruments (continued)

2011	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Derivative financial assets				
Cross currency swaps - fair value hedges	–	98 1	–	98 1
Cross currency swaps - derivatives not in designated hedging relationships	–	62 3	–	62 3
Interest rate swaps - derivatives not in designated hedging relationships	–	17 3	–	17 3
Energy swaps - cash flow hedges	–	14 7	–	14 7
	–	**192.4**	**–**	**192 4**
Derivative financial liabilities				
Interest rate swaps - cash flow hedges	–	(17 8)	–	(17 8)
Interest rate swaps - derivatives not in designated hedging relationships	–	(104 6)	–	(104 6)
Foreign exchange forward contracts	–	(0 1)	–	(0 1)
	–	**(122.5)**	**–**	**(122 5)**
	–	**69 9**	**–**	**69.9**

2010	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Derivative financial assets				
Cross currency swaps - fair value hedges	–	187 3	–	187 3
Interest rate swaps - derivatives not in designated hedging relationships	–	19 4	–	19 4
	–	206 7	–	206 7
Derivative financial liabilities				
Interest rate swaps - cash flow hedges	–	(9 5)	–	(9 5)
Interest rate swaps - derivatives not in designated hedging relationships	–	(125 4)	–	(125 4)
Energy swaps - cash flow hedges	–	(9 8)	–	(9 8)
	–	(144 7)	–	(144 7)
	–	62 0	–	62 0

f) Financial risk factors

The group's activities expose it to a variety of financial risks market risk (including currency and interest rate risk) credit risk, liquidity risk and inflation risk The group's overall risk management programme addresses the unpredictability of financial markets and seeks to reduce potential adverse effects on the group's financial performance or position

Financial risks are managed by a central treasury department (Group Treasury) under policies approved by the board of directors Group Treasury identifies, evaluates and hedges financial risks in close co-operation with the group's operating units The board provides written principles for overall risk management, as well as written policies covering specific areas such as exchange rate risk, interest rate risk, credit risk, the use of derivative and non-derivative financial instruments Derivative financial instruments are used to hedge exposure to changes in exchange rates and interest rates The group's policy is that derivative financial instruments are not held for trading

Notes to the group financial statements (continued)

For the year ended 31 March 2011

32 Financial instruments (continued)

f) Financial risk factors (continued)

(i) Market risk

The principal market risk that the group is exposed to is fluctuations in interest rates Since substantially all of the group's profits and net assets arise from Severn Trent Water, which has very limited and indirect exposure to changes in exchange rates, the sensitivity of the group's results to changes in exchange rates is not material

Interest rate risk

The group's income and operating cash flows are substantially independent of changes in market interest rates

The group's interest rate risk arises from long term borrowings Borrowings issued at variable rates expose the group to cash flow interest rate risk Borrowings issued at fixed rates expose the group to fair value interest rate risk Group policy is to maintain 45-90% of its net debt in fixed rate instruments At 31 March 2011 75 9% of the group's net debt was fixed (2010 82 4%)

The group manages its cash flow interest rate risk by using floating to fixed interest rate swaps Such interest rate swaps have the economic effect of converting borrowings from floating rates to fixed rates Under the terms of the interest rate swaps, the group agrees with other parties to exchange, mainly semi-annually, the difference between fixed contract and floating rate interest rates calculated by reference to the agreed notional principal amounts The group has entered into a series of long dated interest rate swaps to hedge future debt Economically these act to fix debt within the group which is denominated as floating rate, but do not achieve hedge accounting under the strict criteria of IAS 39 This has led to a £15 7 million charge (2010 credit of £41 9 million) in the income statement

Some of the group's debt is index-linked, that is its cost is linked to changes in the Retail Price Index (RPI) This debt provides an economic hedge for Severn Trent Water's revenues and Regulatory Capital Value that are also RPI linked under its regulatory regime

Financial liabilities analysed by interest rate after taking account of various interest rate swaps entered into by the group

2011	Non-interest bearing liabilities £m	Floating rate £m	Fixed rate £m	Index-linked £m	Total £m
Bank loans and overdrafts	–	(544 1)	(150 0)	(152 7)	(846 8)
Other loans	(1 2)	(263 5)	(2,014 7)	(951 5)	(3,230 9)
Finance leases	–	–	(266 7)	–	(266 7)
Other financial liabilities	(32 3)	–	–	–	(32 3)
	(33 5)	(807 6)	(2,431 4)	(1,104 2)	(4,376 7)
Impact of interest rate swaps not matched against specific debt instruments	–	462 3	(462 3)	–	–
	(33 5)	(345 3)	(2,893 7)	(1,104 2)	(4,376 7)
Weighted average interest rate			5 96%		
Weighted average period for which interest is fixed (years)			11 7		

2010	Non-interest bearing liabilities £m	Floating rate £m	Fixed rate £m	Index-linked £m	Total £m
Bank loans and overdrafts	–	(544 2)	–	(145 6)	(689 8)
Other loans	–	(247 5)	(2,029 9)	(908 5)	(3,185 9)
Finance leases	–	(141 8)	(159 0)	–	(300 8)
Other financial liabilities	(28 5)	–	–	–	(28 5)
	(28 5)	(933 5)	(2,188 9)	(1,054 1)	(4,205 0)
Impact of interest rate swaps not matched against specific debt instruments	–	835 0	(835 0)	–	–
	(28 5)	(98 5)	(3,023 9)	(1,054 1)	(4,205 0)
Weighted average interest rate			5 88%		
Weighted average period for which interest is fixed (years)			10 9		

32 Financial instruments (continued)

f) Financial risk factors (continued)

Financial assets analysed by interest rates

2011	Non-interest bearing liabilities £m	Floating rate £m	Fixed rate £m	Index-linked £m	Total £m
Available for sale financial assets	0 1	–	–	–	0 1
Loans and receivables	188 1	–	–	–	188 1
Cash and cash equivalents	–	315 2	–	–	315 2
	188 2	315 2	–	–	503 4

2010	Non-interest bearing liabilities £m	Floating rate £m	Fixed rate £m	Index-linked £m	Total £m
Available for sale financial assets	0 1	–	–	–	0 1
Loans and receivables	196 6	–	–	–	196 6
Cash and cash equivalents	–	227 8	–	–	227 8
	196 7	227 8	–	–	424 5

Interest rate sensitivity analysis

The sensitivity after tax of the group's profits, cash flow and equity, including the impact on derivative financial instruments, to changes in interest rates at 31 March is as follows

	2011		2010	
	+1 0% £m	-1 0% £m	+1 0% £m	-1 0% £m
Profit or loss	**46.1**	**(55 3)**	(38 7)	47 9
Cash flow	**0 1**	**(0 1)**	19 4	(15 4)
Equity	**83 3**	**(98 6)**	(33 7)	43 5

Inflation rate sensitivity analysis

The sensitivity of the group's profit and equity to changes in inflation at 31 March is set out in the following table This analysis excludes any impact on Severn Trent Water's revenues and Regulated Capital Value

	2011		2010	
	+1 0% £m	-1 0% £m	+1 0% £m	-1 0% £m
Profit or loss	**(8 0)**	**8.0**	(7 6)	7 6
Equity	**(8.0)**	**8.0**	(7 6)	7 6

Exchange rate risk

The group operates internationally and is exposed to foreign exchange risk arising from net investments in foreign operations, primarily with respect to the US dollar and the euro However, since substantially all of the group's profits and net assets arise from Severn Trent Water which has very limited and indirect exposure to changes in exchange rates, the sensitivity of the group's results to changes in exchange rates is not material

The group has a significant value of foreign currency debt, primarily in yen and euros The group's policy is to manage the foreign exchange risk arising from foreign currency debt by entering into cross currency swaps, or forward contracts with external parties

At 31 March 2011 the group had cross currency swaps or forward contracts in place for all foreign currency denominated debt (2010 100%)

Notes to the group financial statements (continued)

For the year ended 31 March 2011

32 Financial instruments (continued)

f) Financial risk factors (continued)

Monetary assets and liabilities by currency, excluding functional currency

Certain of the group's subsidiaries operate in markets where the local currency is different from the functional currency of the operation Exchange risks relating to such operations are managed centrally by Group Treasury through forward exchange contracts to buy or sell currency External foreign exchange contracts are designated at group level as hedges of foreign exchange risk on specific assets, liabilities or future transactions on a gross basis The net amount of foreign currency assets and liabilities and the forward contracts that have been taken out to hedge the exchange risks on these assets and liabilities and on future committed transactions are summarised below

2011	US Dollar £m	Euro £m	Other £m	Total £m
Functional currency of operation				
Sterling	–	0 1	0 1	0 2
Total	–	0 1	0 1	0 2

2010	US Dollar £m	Euro £m	Other £m	Total £m
Functional currency of operation				
Sterling	0 6	0 1	0 1	0 8
Total	0 6	0 1	0 1	0 8

The group's borrowings are denominated in the following currencies after taking account of cross currency swaps

	2011 £m	2010 £m
Sterling	**(4,343 1)**	(4,175 3)
Euro	**(1.3)**	(1 2)
	(4,344 4)	(4,176 5)

The euro denominated borrowings relate to operations in which the euro is the functional currency

(ii) Credit risk

Operationally the group has no significant concentrations of credit risk It has policies in place to ensure that sales of products are made to customers with an appropriate credit history, other than in Severn Trent Water Limited, whose operating licence obliges it to supply domestic customers even in cases where bills are not paid Amounts provided against accounts receivable and movements on the provision during the year are disclosed in note 22

For financing purpose, derivative counterparties and cash transactions are limited to high credit quality financial institutions The group has policies that limit the amount of credit exposure to any one financial institution

Credit risk analysis

At 31 March the credit limits and the amounts held on short term deposits were as follows

	Credit limit		Amount deposited	
	2011 £m	2010 £m	2011 £m	2010 £m
AAA	**300 0**	300 0	**54 8**	35 5
Double A range	**450 0**	450 0	**81.2**	89 6
Single A range	**525 0**	525 0	**112.6**	58 6
	1,275 0	1,275 0	**248.6**	183 7

The amounts of derivative assets analysed by credit ratings of counterparties were as follows

	Financial assets	
Rating	2011 £m	2010 £m
Double A range	**100.9**	90 8
Single A range	**91 5**	115 9
	192.4	206 7

32 Fınancıal ınstruments (contınued)

f) Fınancıal rısk factors (contınued)

(ııı) Lıquıdıty rısk

Prudent lıquıdıty management ımplıes maıntaınıng suffıcıent cash balances and the avaılabılıty of fundıng through an adequate amount of commıtted facılıtıes and the abılıty to close out market posıtıons Group Treasury manages lıquıdıty and flexıbılıty ın fundıng by monıtorıng forecast and actual cash flows and the maturıty profıle of fınancıal assets and lıabılıtıes and by keepıng commıtted credıt lınes avaılable

At the balance sheet date the group had commıtted undrawn borrowıng facılıtıes expırıng as follows

	2011 £m	2010 £m
Wıthın one year	**41 7**	–
Between one and two years	**458.3**	191 7
Between two and fıve years	**–**	458 3
	500 0	650 0

Non-derıvatıve fınancıal ınstruments analysed by maturıty date

The followıng tables detaıl the group's remaınıng contractual maturıty for ıts non-derıvatıve net fınancıal lıabılıtıes The ınformatıon presented ıs based on the earlıest date on whıch the group can be requıred to pay and represents the undıscounted cash flows ıncludıng prıncıpal and ınterest

2011	wıthın one year £m	between one and two years £m	between two and fıve years £m	between fıve and ten years £m	between ten and twenty years £m	after more than twenty years £m	Total £m
Fınancıal lıabılıtıes							
Bank loans	(19 7)	(26 8)	(431 5)	(507 7)	(39 4)	–	(1,025 1)
Other loans	(135 8)	(201 3)	(1,264 3)	(808 8)	(1,650 1)	(5,770 3)	(9,830 6)
Fınance leases	(19 7)	(25 7)	(109 5)	(47 4)	(114 3)	–	(316 6)
Other fınancıal lıabılıtıes	(32 3)	–	–	–	–	–	(32 3)
	(207 5)	(253 8)	(1,805 3)	(1,363 9)	(1,803 8)	(5,770 3)	(11,204 6)
Fınancıal assets							
Trade receıvables	188 1	–	–	–	–	–	188 1
Cash and short term deposıts	315 2	–	–	–	–	–	315 2
	295 8	(253 8)	(1,805 3)	(1,363 9)	(1,803 8)	(5,770 3)	(10,701 3)

2010	wıthın one year £m	between one and two years £m	between two and fıve years £m	between fıve and ten years £m	between ten and twenty years £m	after more than twenty years £m	Total £m
Fınancıal lıabılıtıes							
Bank loans	(206 0)	(10 4)	(212 7)	(341 9)	(43 1)	–	(814 1)
Other loans	(142 4)	(142 2)	(743 7)	(1,444 8)	(1,680 0)	(5,320 7)	(9,473 8)
Fınance leases	(56 2)	(21 2)	(78 8)	(101 5)	(95 8)	(32 0)	(385 5)
Other fınancıal lıabılıtıes	(28 4)	–	–	–	–	–	(28 4)
	(433 0)	(173 8)	(1,035 2)	(1,888 2)	(1,818 9)	(5,352 7)	(10,701 8)
Fınancıal assets							
Trade receıvables	196 6	–	–	–	–	–	196 6
Cash and short term deposıts	227 8	–	–	–	–	–	227 8
	(8 6)	(173 8)	(1,035 2)	(1,888 2)	(1,818 9)	(5,352 7)	(10,277 4)

Notes to the group financial statements (continued)

For the year ended 31 March 2011

32 Financial instruments (continued)

f) Financial risk factors (continued)

Other loans include index-linked debt with maturities up to 56 years The principal is revalued at fixed intervals and is linked to movements in the retail price index Interest payments are made biannually based on the revalued principal The principal repayment equals the revalued amount at maturity The calculations above are based on forward inflation rates at the balance sheet date

Derivative financial instruments analysed by maturity date

The following table details the group's liquidity analysis for its derivative financial instruments The tables are based on the undiscounted net cash inflows/(outflows) on the derivative financial instruments that settle on a net basis and the undiscounted gross inflows and (outflows) on those derivatives that require gross settlement When the amount payable or receivable is not fixed, the amount disclosed has been determined by reference to the projected interest and foreign currency rates derived from the forward curves existing at the balance sheet date Actual amounts may be significantly different from those indicated below

2011	Within one year £m	Between one and two years £m	Between two and five years £m	Between five and ten years £m	Between ten and twenty years £m	Greater than twenty years £m	Financial assets falling due Assets total £m
Instruments settled net							
Interest rate swaps	71	51	62	–	–	–	184
Energy swaps	19	91	48	–	–	–	158
Instruments settled gross							
Cross currency swaps							
- cash receipts	483	1314	8919	24	275	–	1,1015
- cash payments	(316)	(992)	(7598)	(22)	(122)	–	(9050)
Net cash flow	167	322	1321	02	153	–	1965
Total	257	464	1431	02	153	–	2307

2011	Within one year £m	Between one and two years £m	Between two and five years £m	Between five and ten years £m	Between ten and twenty years £m	Greater than twenty years £m	Financial liabilities falling due Liabilities total £m
Instruments settled net							
Interest rate swaps	(302)	(234)	(428)	(152)	(69)	08	(1177)
Total	(302)	(234)	(428)	(152)	(69)	08	(1177)

32 Financial instruments (continued)

f) Financial risk factors (continued)

2010	Within one year £m	Between one and two years £m	Between two and five years £m	Between five and ten years £m	Between ten and twenty years £m	Greater than twenty years £m	Financial assets falling due Assets total £m
Instruments settled net							
Interest rate swaps	8 0	6 0	5 5	0 3	–	–	19 8
Instruments settled gross							
Cross currency swaps							
- cash receipts	51 9	48 2	303 7	753 7	56 7	128 9	1,343 1
- cash payments	(33 0)	(43 3)	(244 2)	(630 9)	(38 7)	(60 7)	(1,050 8)
Net cash flow	18 9	4 9	59 5	122 8	18 0	68 2	292 3
Total	26 9	10 9	65 0	123 1	18 0	68 2	312 1

2010	Within one year £m	Between one and two years £m	Between two and five years £m	Between five and ten years £m	Between ten and twenty years £m	Greater than twenty years £m	Financial liabilities falling due Liabilities total £m
Instruments settled net							
Interest rate swaps	(44 5)	(30 4)	(45 4)	(26 1)	(33 4)	(15 8)	(195 6)
Energy swaps	(0 1)	(0 6)	(8 7)	(1 0)	–	–	(10 4)
Total	(44 6)	(31 0)	(54 1)	(27 1)	(33 4)	(15 8)	(206 0)

g) Hedge accounting

The group uses derivative financial instruments to hedge exposures to changes in exchange rates and interest rates Hedge accounting is adopted for such instruments where the criteria set out in IAS 39 are met

(i) Fair value hedges

The group raises debt denominated in currencies other than sterling – principally Japanese Yen and Euro Cross currency swaps are entered into at the time that the debt is drawn down to swap the proceeds into sterling debt bearing interest based on LIBOR in order to mitigate the group's exposure to exchange rate fluctuations The terms of the receivable leg of the swap closely match the terms of the underlying debt hence the swaps are expected to be effective hedges At the year end the amounts of cross currency swaps designated as fair value hedges were as follows

	Notional principal amount		Fair value	
	2011 £m	2010 £m	**2011 £m**	2010 £m
US dollar	**27.0**	27 0	**6 6**	7 7
Euro	**11 4**	548 0	**6.0**	90 2
Yen	**103.3**	161 0	**60 8**	66 9
Czech krona	**47 2**	47 2	**24.7**	22 5
	188.9	783 2	**98.1**	187 3

Notes to the group financial statements (continued)

For the year ended 31 March 2011

32 Financial instruments (continued)

g) Hedge accounting (continued)

(ii) Cash flow hedges

The group has entered into interest rate swaps under which it has agreed to exchange the difference between fixed and floating interest rate amounts calculated on agreed notional principal amounts Such contracts enable the group to mitigate the risk of changing interest rates on future cash flow exposures arising from issued variable rate debt The group also entered into a number of interest rate contracts with future start dates during the AMP5 regulatory period Such contracts enable the group to mitigate the risk of changing interest rates on debt which is highly probable to be issued over the AMP5 period to fund Severn Trent Water's capital programme and have been accounted for as cash flow hedges The fair value of interest rate swaps at the balance sheet date is determined by discounting the future cash flows using the yield curve prevailing at the balance sheet date and the credit risk inherent in the contract

The interest rate swaps primarily settle net on a biannual basis The floating rate on the interest rate swaps is six months LIBOR

Details of interest rate swaps that have been accounted for as cash flow hedges are summarised below

	Average contract fixed interest rate		Notional principal amount		Fair value	
Period to maturity	**2011 %**	2010 %	**2011 £m**	2010 £m	**2011 £m**	2010 £m
Less than 1 year	–	–	–	–	–	–
1-2 years	–	–	–	–	–	–
2-5 years	–	–	–	–	–	–
5-10 years	–	–	–	–	–	–
10-20 years	**5 07%**	5 07%	**493 0**	493 0	**(17 8)**	(9 5)
More than 20 years	–	–	–	–	–	–
	5 07%	5 07%	**493 0**	493 0	**(17 8)**	(9 5)

The group has entered into a series of energy swaps under which it has agreed to exchange the difference between fixed and market prices of electricity at six-monthly intervals up to March 2015

Details of energy swaps that have been accounted for as cash flow hedges are summarised below

	Average contract price		Notional contracted amount		Fair value	
Period to maturity	**2011 £/MWh**	2010 £/MWh	**2011 MWh**	2010 MWh	**2011 £m**	2010 £m
Less than 1 year	**42 0**	35 6	**131,040**	65,520	**1.8**	(0 1)
1-2 years	**45 1**	43 9	**428,064**	196,560	**6.2**	(1 0)
2-5 years	**54 7**	52 4	**1,087,632**	1,275,456	**6 7**	(8 7)
	47 3	44 0	**1,646,736**	1,537,536	**14 7**	(9 8)

Changes in the amounts deferred in equity during the period relating to cash flow hedges were as follows

	2011 £m	2010 £m
Fair value (losses)/gains deferred in equity at the start of the period	**(2 1)**	3 5
Fair value gains/(losses) recognised in equity in the period	**16 0**	(13 2)
Fair value gains transferred to finance costs in the period	**4 5**	7 6
Fair value gains/(losses) deferred in equity at the end of the period	**18 4**	(2 1)

32 Financial instruments (continued)

g) Hedge accounting (continued)

Details of interest rate swaps that have not been accounted for as cash flow hedges are summarised below

Period to maturity	Average contract fixed interest rate 2011 %	2010 %	Notional principal amount 2011 £m	2010 £m	Fair value 2011 £m	2010 £m
Less than 1 year	–	5 11	–	355 0	–	(4 2)
1-2 years	–	–	–	–	–	–
2-5 years	**6 32**	–	**225.0**	–	**(33 0)**	–
5-10 years	–	6 32	–	225 0	–	(38 6)
10-20 years	**5 41**	–	**237 3**	–	**(41.2)**	–
20-30 years	**5 22**	5 32	**200.0**	455 0	**(30 4)**	(82 6)
	5 60	5 60	**662 3**	1,035 0	**(104 6)**	(125 4)

Contracts where the group receives fixed interest are summarised below

Period to maturity	Average contract fixed interest rate 2011 %	2010 %	Notional principal amount 2011 £m	2010 £m	Fair value 2011 £m	2010 £m
Less than 1 year	–	–	–	–	–	–
1-2 years	–	–	–	–	–	–
2-5 years	**5 18**	–	**200 0**	–	**17 3**	–
5-10 years	–	5 18	–	200 0	–	19 4
10-20 years	–	–	–	–	–	–
20-30 years	–	–	–	–	–	–
	5 18	5 18	**200 0**	200 0	**17 3**	19 4

33 Share based payments

The group operates a number of share based remuneration schemes for employees During the period, the group recognised total expenses of £4 6 million (2010 £5 1 million) related to equity settled share based payment transactions

The weighted average share price during the period was £13 40 (2010 £10 50)

At 31 March 2011 the number of shares that were exercisable under each of the share based remuneration schemes was as follows

	2011 Number of exercisable options/awards	2011 Weighted average exercise price	2010 Number of exercisable options/awards	2010 Weighted average exercise price
Long Term Incentive Plan	–	–	–	–
Employee Sharesave Scheme	**369,304**	**937p**	525,098	870p
Share Incentive Plan	–	–	–	–
Approved Share Option Scheme	–	–	3,125	720p
Unapproved Share Option Scheme	**22,984**	**729p**	35,259	728p
Share Matching Plan	–	–	–	–
	392,288		563,482	

a) Long Term Incentive Plans (LTIPs)

Under the LTIPs conditional awards of shares may be made to executive directors and senior staff Awards are subject to performance conditions and continued employment throughout the vesting period Awards have been made on different bases to Severn Trent Plc and Severn Trent Water employees (the LTIP) and to Severn Trent Services employees (the Services LTIP)

During the year awards over 141,111 shares (2010 163,421 shares) with a fair value of £7 91 (2010 £5 41) were made to 20 employees (2010 21 employees) under the LTIP The LTIP awards are subject to total shareholder return over three years relative to the companies ranked 51 – 150 by market capitalisation in the FTSE index (excluding investment trusts)

The Services LTIP awards vest in three equal tranches which are subject to achievement of turnover and profit targets in the years ending 31 March 2011, 2012 and 2013 No awards have been made to employees under the Services LTIP during the year (2010 nil)

Notes to the group financial statements (continued)

For the year ended 31 March 2011

33 Share based payments (continued)

a) Long term incentive plans (continued)

Details of changes in the number of awards outstanding during the year are set out below

	Number of awards	
	LTIP	Services LTIP
Outstanding at 1 April 2009	582,182	118,489
Granted during the year	163,421	–
Cancelled during the year	(17,131)	(8,049)
Lapsed during the year	(334,989)	–
Outstanding at 1 April 2010	393,483	110,440
Granted during the year	141,111	–
Vested during the year	(71,849)	–
Cancelled during the year	(10,671)	(9,053)
Lapsed during the year	(49,373)	–
Outstanding at 31 March 2011	**402,701**	**101,387**

Details of LTIP awards outstanding at 31 March were as follows

		Number of shares	
Date of grant	Normal date of vesting	2011	2010
July 2007	2010	–	121,223
July 2008	2011	**151,322**	153,528
July 2008	2012	**33,671**	36,813
July 2008	2013	**33,109**	36,813
July 2009	2012	**151,786**	155,546
July 2010	2013	**134,200**	–
		504,088	503,923

The fair value of the LTIP awards made during the year was calculated using the Monte Carlo method using the principal assumptions set out below

Assumptions	2011	2010
Expected volatility		
Severn Trent group	**27%**	25%
Comparator group	**47%**	45%
Correlation between Severn Trent Plc and comparator group	**32%**	30%
Proportion of employees expected to cease employment before vesting	**0%**	0%

Severn Trent share price volatility is based on observations of historical weekly volatility over a period prior to grant commensurate with the remaining term of the performance period for each award

For the July 2010 LTIP award and the July 2009 award the comparator group is the group of companies ranked 51 – 150 in the FTSE index excluding investment trusts

The volatility of the comparator companies, the correlation between Severn Trent and the comparator companies, and performance over the portion of the performance period that had elapsed at the date of grant was taken into account when modelling the TSR performance condition

The share price at the grant date was £12 28 (2010 £11 34) The vesting period commences before the grant date Performance in the vesting period prior to the grant date is taken into account in determining the fair value of the award

Dividends 'paid' on shares during the vesting period are accumulated during the vesting period and released subject to achievement of the performance condition in the same manner as the underlying shares As a result a dividend yield assumption is not required

The 2009 Services LTIP is based entirely on non-market conditions and hence market assumptions are not required to determine the fair value of the award For 2011 it has been assumed that performance against the Services LTIP non-market conditions will be 0 3%

Details of the basis of the LTIP schemes are set out in the remuneration report on page 48

33 Share based payments (continued)

b) Employee Sharesave Scheme

Under the terms of the Sharesave Scheme, the board may grant the right to purchase ordinary shares in the company to those employees who have entered into an HMRC approved Save As You Earn contract for a period of three or five years

Details of changes in the number of options outstanding during the year are set out below

	Number of share options	Weighted average exercise price
Outstanding at 1 April 2009	3,724,812	877p
Granted during the year	992,888	808p
Forfeited during the year	(95,659)	1,007p
Cancelled during the year	(320,240)	981p
Exercised during the year	(639,121)	715p
Expired during the year	(25,612)	953p
Outstanding at 1 April 2010	3,637,068	899p
Granted during the year	366,272	1,137p
Forfeited during the year	(146,468)	895p
Cancelled during the year	(92,030)	875p
Exercised during the year	(550,525)	841p
Expired during the year	(86,132)	1,062p
Outstanding at 31 March 2011	**3,128,185**	**904p**

Sharesave options outstanding at 31 March were as follows

Date of grant	Normal date of exercise	Option price	Number of share options 2011	2010
January 2003	2010	536p	–	73,017
January 2004	2011	592p	**45,820**	53,862
January 2005	2010 or 2012	759p	**54,324**	332,581
January 2006	2011 or 2013	823p	**212,941**	239,385
January 2007	2010, 2012 or 2014	1,172p	**93,243**	286,787
January 2008	2011 or 2013	1,221p	**218,048**	252,683
January 2009	2012 or 2014	862p	**1,247,781**	1,411,657
January 2010	2013 or 2015	806p	**890,670**	987,096
January 2011	2014 or 2016	1,137p	**365,358**	–
			3,128,185	3,637,068

The fair value of the Sharesave options granted during the year was calculated using the Black Scholes model The principal assumptions were as follows

	2011		2010	
Assumptions	3 year scheme	5 year scheme	3 year scheme	5 year scheme
Expected volatility	**27%**	**27%**	25%	25%
Risk free rate	**1 63%**	**2.24%**	1 80%	2 78%
Expected dividend yield	**4 4%**	**4 4%**	4 0%	4 0%
Proportion of employees expected to cease employment before vesting	**15%**	**17%**	15%	17%
Fair value per share - Sharesave	**348p**	**359p**	264p	280p

Expected volatility is based on historical weekly volatility over a three year period Weekly volatility in the observed data was between 25-31%

The risk free rate is derived from yields at the grant date of gilts of similar duration to the Sharesave contracts

The proportion of employees expected to cease employment before vesting is based on historically observed data

Notes to the group financial statements (continued)

For the year ended 31 March 2011

33 Share based payments (continued)

b) Employee Sharesave Scheme (continued)

The following data was used in calculating the fair value of the Sharesave options

	2011		2010	
	3 year scheme	5 year scheme	3 year scheme	5 year scheme
Share price at grant date	**1,486p**	**1,486p**	1,080p	1,080p
Vesting period (years)	**3**	**5**	3	5
Option life (years)	**3.5**	**5 5**	3 5	5 5

The number of employees entering into Sharesave contracts and the number of options granted during the year were as follows

	2011		2010	
	3 year scheme	5 year scheme	3 year scheme	5 year scheme
Number of employees	**1,073**	**448**	1,602	563
Number of options granted	**223,291**	**142,981**	586,381	406,507

c) Share Incentive Plan (SIP)

Under the SIP the board may grant share awards to employees of group companies During the year the board has announced that it will make awards under the SIP based on performance against Severn Trent Water's targets for its Key Performance Indicators Eligible employees will be entitled to shares to a maximum value of £750 It is expected that these awards will be made in August 2011 SIP shares vest with the employee on the date of grant

d) Approved Share Option Scheme

Under the terms of the Share Option Scheme (formerly Executive Share Option Scheme), the board has granted directors and other executives options to purchase ordinary shares in the company No awards have been made under this scheme since July 2003

	Number of share options	Weighted average exercise price
Outstanding 1 April 2009	4,759	724p
Exercised during the year	(1,634)	731p
Outstanding 1 April 2010	3,125	720p
Exercised during the year	(3,125)	720p
Outstanding 31 March 2011	**–**	**–**

Options outstanding under this scheme at 31 March were as follows

			Number of shares	
Date of grant	Normal date of exercise	Option price	2011	2010
July 2002	2005-2012	720p	**–**	3,125

e) Unapproved Share Option Scheme

The board has granted a number of executives options to purchase ordinary shares in the company under an unapproved share option scheme No awards have been made under this scheme since July 2003

Details of movements in the share awards outstanding during the year are as follows

	Number of share options	Weighted average exercise price
Outstanding at 1 April 2009	40,763	728p
Exercised during the year	(5,504)	728p
Outstanding at 1 April 2010	35,259	728p
Lapsed during the year	(8,596)	729p
Exercised during the year	(3,679)	720p
Outstanding at 31 March 2011	**22,984**	**729p**

33 Share based payments (continued)

e) Unapproved Share Option Scheme (continued)

Options outstanding under this scheme at 31 March were as follows

Date of grant	Normal date of exercise	Option price	Number of shares 2011	Number of shares 2010
June 2001	2004-2011	738p	**11,844**	16,274
June 2002	2005-2012	720p	**11,140**	18,985
			22,984	35,259

f) Share Matching Plan (SMP)

Under the Share Matching Plan members of the Executive Committee receive matching share awards over those shares which have been acquired under the deferred share component of the annual bonus scheme Matching shares may be awarded at a maximum ratio of one matching share for every one deferred share and are subject to a three year vesting period During the year matching shares were awarded at a ratio of 0 5 to 1

Matching shares are subject to total shareholder return over three years measured relative to the companies ranked 51-150 by market capitalisation in the FTSE Index (excluding investment trusts) This replicates the LTIP performance condition for the July 2010 award

The number of shares subject to an award will increase to reflect dividends paid through the performance period on the basis of such notional dividends being reinvested at the then prevailing share price Awards will normally vest as soon as the Remuneration Committee determines that the performance conditions have been met provided that the participant remains in employment at the end of the performance period

During the year 25,187 matching shares with a fair value of £6 79 were awarded to 11 employees (2010 nil)

	Number of share options
Outstanding at 1 April 2010	–
Granted during the year	25,187
Exercised during the year	–
Outstanding at 31 March 2011	**25,187**

Details of share matching awards outstanding at 31 March 2011 were as follows

Date of grant	Normal date of vesting	Number of shares 2011	Number of shares 2010
May 2010	June 2013	**25,187**	–

The fair value of the share matching awards made during the year was calculated using the Monte Carlo method using the principal assumptions set out below

Assumptions	2011
Expected volatility	
Severn Trent group	**27%**
Comparator group	**46%**
Correlation between Severn Trent Plc and comparator group	**33%**
Proportion of employees expected to cease employment before vesting	**0%**

Share price volatility is based on observations over a historical period prior to the date of grant, commensurate to the expected term of the performance period

The comparator group is the companies ranked 51-150 in the FTSE Index

The share price at the grant date was £11 26

Dividends paid on the shares during the vesting period are accumulated during the vesting period and released subject to the achievement of the performance condition, in the same manner as the underlying shares As a result a dividend yield assumption is not required

Notes to the group financial statements (continued)

For the year ended 31 March 2011

34 Cash flow statement

a) Reconciliation of operating profit to operating cash flows

	2011 £m	2010 £m
Profit before interest and tax	**497 7**	507 4
Depreciation of property, plant and equipment	**251 5**	236 1
Amortisation of intangible assets	**25 4**	25 2
Exceptional impairment and depreciation	**–**	6 6
Pension service cost	**22 7**	14 7
Curtailment cost	**–**	7 4
Pension contributions	**(40 0)**	(39 6)
Share based payments charge	**4 6**	5 1
Profit on sale of property, plant and equipment	**(2 6)**	(4 5)
Loss on disposal of businesses	**–**	1 7
Deferred income movement	**(8 4)**	(7 4)
Provisions charged to the income statement	**6 8**	24 2
Utilisation of provisions for liabilities and charges	**(19.0)**	(10 5)
(Increase)/decrease in stocks	**(0 5)**	3 9
Increase in debtors	**(7.5)**	(26 4)
Increase/(decrease) in creditors	**22.3**	(35 9)
Cash generated from operations	**753 0**	708 0
Tax paid	**(32.4)**	(53 8)
Net cash generated from operating activities	**720 6**	654 2

b) Non-cash transactions

No additions to property, plant and equipment during the year were financed by new finance leases (2010 nil)

c) Exceptional cash flows

The following cash flows arose from items classified as exceptional in the income statement

	2011 £m	2010 £m
Restructuring costs	**(27 6)**	(15 9)
Regulatory matters	**(3 8)**	–
Fines and penalties	**–**	(2 0)
Loss on disposal of businesses	**–**	(0 9)
	(31.4)	(18 8)

d) Reconciliation of movement in cash and cash equivalents to movement in net debt

	As at 1 April 2010 £m	Cash flow £m	Fair value adjustments £m	RPI uplift on index-linked debt £m	Foreign exchange £m	Other non-cash movements £m	**As at 31 March 2011 £m**
Cash and cash equivalents	227 8	88 3	–	–	(0 9)	–	**315 2**
Net cash and cash equivalents	227 8	88 3	–	–	(0 9)	–	**315 2**
Bank loans	(689 8)	(150 0)	–	(7 0)	–	–	**(846 8)**
Other loans	(3,185 9)	7 5	(10 4)	(42 9)	(1 2)	2 0	**(3,230 9)**
Finance leases	(300 8)	47 3	–	–	–	(13 2)	**(266 7)**
Cross currency swaps	187 3	(20 5)	(4 1)	–	–	(2 3)	**160 4**
Net debt	(3,761 4)	(27 4)	(14 5)	(49 9)	(2 1)	(13 5)	**(3,868 8)**

35 Contingent liabilities

a) Bonds and guarantees

Group undertakings have entered into bonds and guarantees in the normal course of business No liability is expected to arise in respect of either bonds or guarantees

b) Disposal of subsidiaries

The group has given certain guarantees and indemnities in relation to disposals of businesses

On 5 March 2007 the group received notice of a claim for €23 4 million from Veolia Proprete S A ('Veolia') alleging breach of warranty in relation to the disposal of Biffa Belgium The group subsequently received notice from Veolia of a further claim for €5 million relating to the same matter The group considered that there was no basis for this claim and hence no provision was recorded in the financial statements in relation to this matter Following a hearing in the Commercial Court in Belgium in February 2010, the Court rendered judgment in favour of the group on 1 April 2010 and declared all of Veolia's claims to be unfounded The group has received notice that Veolia has filed an appeal against this decision

The group is not aware of any other liability that is likely to result from these guarantees and indemnities that has not been provided for in these financial statements

c) Regulatory matters

Following an audit in September 2010 by the Drinking Water Inspectorate (DWI) of aspects of the services provided by Severn Trent Laboratories Ltd from its Bridgend laboratory, inorganic testing services provided by that laboratory were temporarily suspended, and transferred to another of the group's laboratories, pending completion of an investigation commissioned by Severn Trent Plc The results of this investigation have been discussed with the DWI Inorganics testing resumed at Bridgend in January 2011 following accreditation by UKAS of revised testing processes

At this stage it is not possible to determine what, if any, liability will arise as a result of this incident

On 17 December 2010 Severn Trent Plc, Severn Trent Water Ltd and Severn Trent Laboratories Ltd received a request from Ofwat to provide certain information under the Competition Act in connection with Severn Trent Laboratories Ltd's contracts with Severn Trent Water Ltd and certain other water companies The information requested has subsequently been provided to Ofwat

At this stage it is not possible to determine what, if any, liability will arise as a result of this request

36 Service concession arrangements

The group's contract to provide water and waste water services to the Ministry of Defence (MoD) is a service concession arrangement under the definition set out in IFRIC 12 The group acts as the service provider under the MoD Project Aquatrine Package C – a 25 year contract spanning some 1,523 sites across England covering the Eastern sea border and from Lancashire in the North West to West Sussex on the South Coast

Under the contract the group maintains and upgrades the MoD infrastructure assets and provides operating services for water and waste water The maintenance and upgrade services are charged at an agreed rate, adjusted for inflation, that is agreed in the contract The operating services are charged under an agreed volumetric tariff

Since the group has an unconditional right to receive cash in exchange for the maintenance and upgrade services, the amounts receivable are recognised as a financial asset within prepayments and accrued income At 31 March 2011 the amount receivable was £27 1 million (2010 £26 2 million)

There have been no significant changes to the arrangement during the year

Notes to the group financial statements (continued)

For the year ended 31 March 2011

37 Financial and other commitments

a) Investment expenditure commitments

	2011* £m	2010 £m
Contracted for but not provided in the financial statements	91.7	321 0

In addition to these contractual commitments, Severn Trent Water Limited has longer term expenditure plans which include investments to achieve improvements in performance mandated by the Director General of Water Services (Ofwat) and to provide for growth in demand for water and sewerage services

b) Leasing commitments

At the balance sheet date the group had outstanding commitments for future minimum operating lease payments under non-cancellable operating leases, which fall due as follows

	2011 £m	2010 £m
Within one year	4 4	4 9
In the second year to fifth years inclusive	11.2	9 0
After more than five years	7 3	4 9
	22 9	18 8

Operating lease payments represent rentals payable by the group for certain of its office properties, plant and equipment

38 Post balance sheet events

Following the year end the board of directors has proposed a final dividend of 39 05 pence per share Further details of this are shown in note 14

39 Related party transactions

Transactions between the company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not included in this note Transactions between the group and its associates and joint ventures are disclosed below

Trading transactions

	Sale of goods		Purchase of goods		Amounts due from related parties		Amounts due to related parties	
	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m	2011 £m	2010 £m
Cognica	–	–	–	0 1	–	–	–	–
SII	6.9	10 5	–	–	18.5	15 5	–	–
Jackson Water Partnership	2 9	5 0	–	–	–	1 5	–	–
	9 8	15 5	–	0 1	18 5	17 0	–	–

The related parties are associates and joint ventures in which the group has a participating interest

Remuneration of key management personnel

Key management personnel comprise the members of STEC during the year

The remuneration of the directors is included within the amounts disclosed below Further information about the remuneration of individual directors is provided in the audited part of the Directors' remuneration report on pages 51 to 55

	2011 £m	2010 £m
Short term employee benefits	4 8	5 5
Post employment benefits	0.5	0 6
Termination benefits	0 3	0 3
Share based payments	0.6	0 5
	6 2	6 9

Independent auditor's report to the members of Severn Trent Plc

We have audited the parent company financial statements of Severn Trent Plc for the year ended 31 March 2011 which comprise the company balance sheet, the company statement of total recognised gains and losses, and the related notes 1 to 19 The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom 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' responsibility statement, the directors are responsible for the preparation of the parent company 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 parent company 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 Ethical Standards for Auditors

Scope of the audit of the financial statements
An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error This includes an assessment of whether the accounting policies are appropriate to the parent 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 financial statements

Opinion on financial statements
In our opinion the parent company financial statements

- give a true and fair view of the state of the parent company's affairs as at 31 March 2011,
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matters prescribed by the Companies Act 2006
In our opinion

- the part of the Directors' remuneration report to be audited has been properly prepared in accordance with Companies Act 2006, and
- the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the parent company 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 by the parent company, or returns adequate for our audit have not been received from branches not visited by us, or
- the parent company financial statements and the part of the Directors' remuneration report to be audited 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

Other matter
We have reported separately on the group financial statements of Severn Trent Plc for the year ended 31 March 2011

Carl D Hughes (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
London, UK
26 May 2011

40 Principal subsidiary undertakings and their directors

Details of the principal operating subsidiaries as at 26 May 2011 are given below A complete list of subsidiary undertakings is available on request to the company and will be filed with the next Annual Return

Severn Trent Water
Severn Trent Water Limited
2 St John's Street, Coventry CV1 2LZ
Telephone 02477 715 000

Directors

A J Duff	M J Kane
A J Ballance	M J E McKeon
B Bulkin	Baroness Noakes
R H Davey	A P Smith
G Fryett	A P Wray
M J Lamb	

Severn Trent Services
Severn Trent Services Inc
Suite 300, 580 Virginia Drive,
Ft Washington, Pennsylvania 19034, USA
Telephone 001 215 646 9201
(Incorporated and operational in the United States of America)

Directors

D L Chester	L F Graziano

Severn Trent Environmental Services Inc
Park 10, 16337 Park Row
Houston, Texas 77084, USA
Telephone 001 281 578 4200
(Incorporated and operational in the United States of America)

Directors

D L Chester	K J Kelly
L F Graziano	

Severn Trent Services Limited
Arley Drive, Birch Coppice Business Park
Dordon, Tamworth B78 1SA
Telephone 01827 266 000

Directors

L F Graziano	K A A Porritt
R C McPheely	P M Senior

Severn Trent Water Purification Inc
3000 Advance Lane,
Colmar, Pennsylvania 18915, USA
Telephone 001 215 997 4000
(Incorporated and operational in the United States of America)

Directors

D L Chester	K J Kelly
L F Graziano	

Severn Trent Services International Limited
2308 Coventry Road, Birmingham B26 3JZ
Telephone 0121 722 6000

Directors

L F Graziano	K A A Porritt
R C McPheely	P M Senior

C2C Services Limited
(80% owned)
2308 Coventry Road, Birmingham B26 3JZ
Telephone 0121 722 6000

Directors

D Godfrey	R J Phillips
A J Handford	W G Weatherdon
R G Piper	E A Wilson

Severn Trent Laboratories Limited
STL Business Centre, Torrington Avenue
Coventry CV4 9GU
Telephone 024 764 21213

Directors

L F Graziano	K A A Porritt
R C McPheely	P M Senior

Other Businesses
Derwent Insurance Limited
6A Queensway, PO Box 64, Gibraltar
Telephone 00 350 47529
(Insurance company – incorporated and operational in Gibraltar)

Directors

J Davies	F B Smith
N Feetham	F White

Severn Trent Luxembourg Overseas Holdings S a r l
1A rue Thomas Edison L-1445 Strassen, Luxembourg
(Finance company – registered and operational in Luxembourg)

Directors

D L Chester	X Pauwels
L F Graziano	D Robyns
M J E McKeon	F B Smith

Country of incorporation and main operation is Great Britain and registration is in England and Wales unless otherwise stated All subsidiary undertakings are wholly owned unless otherwise indicated All shareholdings are in ordinary shares

All subsidiary undertakings have been included in the consolidation

Company balance sheet

At 31 March 2011

	Note	2011 £m	2010 £m
Non-current assets			
Tangible fixed assets	2	**0 2**	0 4
Investments in subsidiaries	3	**3,550 1**	3,609 3
Derivative financial instruments		**27.5**	21 0
		3,577 8	3,630 7
Current assets			
Debtors	4	**16 2**	56 3
Derivative financial instruments		**–**	2 8
Cash at bank and in hand		**223 2**	239 0
		239 4	298 1
Creditors amounts falling due within one year	5	**(827 2)**	(746 1)
Net current liabilities		**(587.8)**	(448 0)
Total assets less current liabilities		**2,990 0**	3,182 7
Creditors amounts falling due after more than one year	6	**(167 7)**	(466 6)
Net assets		**2,822 3**	2,716 1
Capital and reserves attributable to the company's equity shareholders			
Called up share capital	8	**232 2**	231 6
Share premium account	9	**80 0**	75 9
Other reserves	10	**150 6**	148 6
Retained earnings	11	**2,359 5**	2,260 0
Equity attributable to the company's equity shareholders	11	**2,822.3**	2,716 1

Signed on behalf of the board who approved the accounts on 26 May 2011

Andrew Duff
Chairman

Michael McKeon
Finance Director

Company Number 2366619

Company statement of total recognised gains and losses

For the year ended 31 March 2011

	2011 £m	2010 £m
Transfers		
Transfers to the profit and loss account on cash flow hedges	**2.7**	3 2
Deferred tax on transfers to the profit and loss account	**(0 7)**	(0 9)
	2 0	2 3
Profit for the period	**264.5**	140 0
Total recognised gains and losses for the period	**266 5**	142 3

Notes to the company financial statements

For the year ended 31 March 2011

1 Accounting policies

a) Basis of accounting
The financial statements have been prepared under the historical cost convention as modified by the revaluation of financial assets and liabilities (including derivative instruments) at fair value through profit or loss and in accordance with applicable United Kingdom Accounting Standards and comply with the requirements of the United Kingdom Companies Act 2006 ('the Act')

b) Tangible fixed assets and depreciation
Tangible fixed assets are included at cost less accumulated depreciation Freehold land is not depreciated Other assets are depreciated on a straight line basis over their estimated economic lives, which are principally as follows

	Years
Buildings	30-60
Computers and software	2-15

c) Leased assets
Where assets are financed by leasing arrangements which transfer substantially all the risks and rewards of ownership of an asset to the lessee (finance leases), the assets are accounted for as if they had been purchased and the fair values of the minimum lease payments are shown as an obligation to the lessor Lease payments are treated as consisting of a capital element and a finance charge, the capital element reducing the obligation to the lessor and the finance charge being written off to the profit and loss account over the period of the lease in proportion to the capital amount outstanding Depreciation is charged over the shorter of the estimated useful life and the lease period All other leases are accounted for as operating leases Rental costs arising under operating leases are charged to the profit and loss account on a straight line basis over the life of the lease

d) Impairment of fixed assets and investments
Impairments of fixed assets and investments are calculated as the difference between the carrying values of net assets of income generating units, including where appropriate investments and goodwill, and their recoverable amounts Recoverable amount is defined as the higher of net realisable value or estimated value in use at the date the impairment review is undertaken Net realisable value represents the net amount that can be generated through sale of assets Value in use represents the present value of expected future cash flows discounted on a pre-tax basis, using the estimated cost of capital of the income generating unit Impairment reviews are carried out if there is some indication that an impairment may have occurred, or, where otherwise required, to ensure that goodwill and fixed assets are not carried above their estimated recoverable amounts Impairments are recognised in the profit and loss account and, where material, are disclosed as exceptional

e) Financial instruments
(i) Financial assets
Financial assets are classified into the following specified categories

- At fair value through profit or loss,
- Held to maturity investments,
- Available for sale financial assets, and
- Loans and receivables

Financial assets at fair value through profit or loss
A financial asset is classified at fair value through profit or loss if it is so designated or if it is held for trading Derivative financial assets that are not designated and effective as hedging instruments are classified as held for trading Financial assets at fair value through profit or loss are stated at fair value, with any gains or losses arising on remeasurement recognised in gains/losses on financial instruments in the income statement Fair value is determined using the methodology described in note 32 to the group's financial statements Interest receivable in respect of derivative financial assets is included in finance income

Held to maturity investments
Where the company has the ability and intent to hold an investment to maturity the financial asset is classified as held to maturity Such financial assets are measured at amortised cost using the effective interest rate method, with any gains or losses being recognised in the income statement

Available for sale financial assets
After initial recognition at cost (being the fair value of the consideration paid), investments which are classified as available for sale are measured at fair value, with gains or losses recognised in equity When an available for sale investment is disposed of, or impaired, the gain or loss previously recognised in equity is taken to the income statement Where there is no active market in the investments and the fair value cannot be measured reliably, the investments are held at cost

Loans and receivables
Trade receivables, loans and other receivables that have fixed or determinable payments and that are not quoted in an active market are classified as loans and receivables Such assets are measured at fair value on initial recognition and are subsequently measured at amortised cost using the effective interest rate method unless there is objective evidence that the asset is impaired, where it is written down to its recoverable amount and the irrecoverable amount is recognised as an expense

(ii) Financial liabilities
Financial liabilities are classified as either

- financial liabilities at fair value through profit or loss, or
- other financial liabilities

Financial liabilities at fair value through profit or loss
A financial liability is classified at fair value through profit or loss if it is so designated or if it is held for trading Derivative financial liabilities that are not designated and effective as hedging instruments are classified as held for trading Financial liabilities at fair value through profit or loss are stated at fair value, with any gains or losses arising on remeasurement recognised in gains/losses on financial instruments in the income statement Fair value is determined using the methodology described in note 32 in the group financial statements Interest payable in respect of derivative financial liabilities is included in finance costs

Other financial liabilities
Other financial liabilities, including borrowings, are initially recognised at fair value less transaction costs After initial recognition, other financial liabilities are subsequently measured at amortised cost using the effective interest rate method

1 Accounting policies (continued)

e) Financial instruments (continued)

(iii) Hedge accounting

The company uses derivative financial instruments such as cross currency swaps, forward currency contracts and interest rate swaps to hedge its risks associated with foreign currency and interest rate fluctuations Such derivative instruments are recognised and measured in accordance with the accounting policies described above

At the inception of the hedge relationship the company documents

- the relationship between the hedging instrument and the hedged item,
- its risk management objectives and strategy for undertaking hedge transactions, and
- whether the hedging instrument is highly effective in offsetting changes in fair values or cash flows (as appropriate) of the hedged item

The company continues to test and document the effectiveness of the hedge on an ongoing basis

Hedge accounting is discontinued when the hedging instrument expires, is sold, terminated or exercised, or no longer qualifies for hedge accounting

Fair value hedges

Where a loan or borrowing is in a fair value hedging relationship it is remeasured for changes in fair value of the hedged risk at the balance sheet date, with gains or losses being recognised in gains/losses on financial instruments in the income statement The gain or loss on the hedging instrument is taken to gains/losses on financial instruments in the income statement where the effective portion of the hedge will offset the gain or loss on the hedged item

When hedge accounting is discontinued the fair value adjustment to the carrying amount of the hedged item arising from the hedged risk is amortised to the income statement from that date

Cash flow hedges

The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in equity and the ineffective portion in gains/losses on financial instruments in the income statement The gains or losses deferred in equity in this way are recycled through gains/losses on financial instruments in the income statement in the same period in which the hedged underlying transaction or firm commitment is recognised in the income statement

When hedge accounting is discontinued any cumulative gain or loss on the hedging instrument recognised in equity is kept in equity until the forecast transaction occurs, or transferred to gains/losses on financial instruments in the income statement if the forecast transaction is no longer expected to occur

Hedges of net investments in foreign operations

Where forward currency contracts and foreign currency borrowings are used to hedge net investments in foreign currency denominated operations, to the extent that they are designated and effective as net investment hedges, they are matched in equity against changes in value of the related assets Any ineffectiveness is taken to gains/losses on financial instruments in the income statement

(iv) Embedded derivatives

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contract and the host contract is not carried at fair value, with gains and losses reported in gains/losses on financial instruments in the income statement

f) Investments

Investments in subsidiary undertakings are held at historical cost

After initial recognition at cost (being the fair value of the consideration paid), investments which are classified as held for trading or available for sale are measured at fair value, with gains or losses recognised in income or equity respectively When an available for sale investment is disposed of, or impaired, the gain or loss previously recognised in reserves is taken to the profit and loss account

g) Share based payments

The company operates a number of equity settled, share based compensation plans for employees The fair value of the employee services received in exchange for the grant is recognised as an expense over the vesting period of the grant

The fair value of employee services is determined by reference to the fair value of the awards granted calculated using a pricing model, excluding the impact of any non-market conditions The number of awards expected to vest takes into account non-market vesting conditions including, where appropriate, continuing employment by the group The charge is adjusted to reflect shares that do not vest as a result of failing to meet a non-market based condition

h) Cash flow statement

The company has taken advantage of the exemption under Financial Reporting Statement 1 'Cash flow statements' and not produced a cash flow statement

i) Deferred taxation

Deferred taxation is fully provided for in respect of timing differences between the treatment of certain items for taxation and accounting purposes only to the extent that the company has an obligation to pay more tax in the future or a right to pay less tax in the future Deferred tax assets are only recognised to the extent that taxable profits are expected to arise in the future Material deferred taxation balances arising are discounted by applying an appropriate risk free discount rate

j) Pensions

The company participates in the group's defined benefit and defined contribution pension schemes, details of which are set out in note 27 to the group financial statements However, the company is currently unable to identify its share of assets and liabilities relating to the defined benefit schemes The pension costs charged against the operating profit are the contributions payable to the scheme in respect of the accounting period in respect of the defined benefit and defined contribution schemes

Notes to the company financial statements (continued)

2 Tangible fixed assets

	Land and buildings £m	Plant and equipment £m	Total £m
Cost			
As at 1 April 2010	0 7	0 6	1 3
As at 31 March 2011	**0 7**	**0.6**	**1 3**
Depreciation			
As at 1 April 2010	(0 7)	(0 2)	(0 9)
Charge for the year	–	(0 2)	(0 2)
As at 31 March 2011	**(0.7)**	**(0.4)**	**(1.1)**
Net book value			
At 31 March 2011	**–**	**0.2**	**0 2**
At 31 March 2010	–	0 4	0 4

3 Investments

	Subsidiary undertakings		
	Shares £m	Loans £m	Total £m
As at 1 April 2010	3,288 1	321 2	3,609 3
Additions/loans advanced	4 4	–	4 4
Disposals/loans repaid	–	(63 6)	(63 6)
As at 31 March 2011	**3,292.5**	**257 6**	**3,550.1**

Details of principal subsidiaries of the company are given in note 40 of the group financial statements

4 Debtors

	2011 £m	2010 £m
Amounts owed by group undertakings	**5.4**	3 5
Deferred tax	**9.2**	10 1
Corporation tax recoverable	**–**	38 3
Other debtors	**0.2**	0 1
Prepayments and accrued income	**1 4**	4 3
	16 2	56 3

5 Creditors amounts falling due within one year

	2011 £m	2010 £m
Bank overdrafts	**(4.9)**	(91 4)
Other loans	**–**	(10 6)
Borrowings	**(4 9)**	(102 0)
Derivative financial instruments	**–**	(2 0)
Trade creditors	**(0 2)**	(0 2)
Amounts due to group undertakings	**(808 3)**	(635 5)
Other creditors	**(8 6)**	(5 6)
Taxation and social security	**(0.7)**	–
Accrued expenses	**(4.5)**	(0 8)
	(827.2)	(746 1)

6 Creditors amounts falling due after more than one year

	2011 £m	2010 £m
Borrowings - other loans (note 7)	**(81 8)**	(77 8)
Amounts due to group undertakings	**(52 8)**	(350 2)
Derivative financial instruments	**(33 1)**	(38 6)
	(167 7)	(466 6)

7 Borrowings

	2011 £m	2010 £m
Borrowings due within one year	**4 9**	102 0
Borrowings due after more than one year		
Between one and two years	**22 9**	–
Between two and five years	**58 9**	55 8
After more than five years	**–**	22 0
Total borrowings due after one year	**81.8**	77 8
	86 7	179 8

Borrowings analysed by interest rate after taking account of interest rate swaps entered into by the company were

2011	Non-interest bearing liabilities £m	Floating rate £m	Fixed rate £m	Total £m
Bank loans and overdrafts	–	4 9	–	4 9
Other loans	–	81 8	–	81 8
	–	86 7	–	86 7
Impact of interest rate swaps not matched against specific debt instruments	–	(225 0)	225 0	–
	–	(138 3)	225 0	86 7
Weighted average interest rate			6 32%	
Weighted average period for which interest is fixed (years)			4 5	

2010	Non-interest bearing liabilities £m	Floating rate £m	Fixed rate £m	Total £m
Bank loans and overdrafts	–	91 4	–	91 4
Other loans	–	88 4	–	88 4
	–	179 8	–	179 8
Impact of interest rate swaps not matched against specific debt instruments	–	(300 0)	300 0	–
	–	(120 2)	300 0	179 8
Weighted average interest rate			6 32%	
Weighted average period for which interest is fixed (years)			4 2	

Notes to the company financial statements (continued)

7 Borrowings (continued)

The company's borrowings are denominated in sterling, after taking account of cross currency swaps the company has entered into There is no difference between the book value and the fair value of the company's borrowings Fair values are based on the expected future cash flows discounted using zero coupon forward interest rates related to the expected timing of payments

At the balance sheet date the company had committed undrawn borrowing facilities expiring as follows

	2011 £m	2010 £m
Within one year	**41.7**	–
1-2 years	**458.3**	191 7
2-5 years	**–**	458 3
After more than five years	**–**	–
	500 0	650 0

8 Share capital

	2011 £m	2010 £m
Total issued and fully paid share capital		
237,142,534 ordinary shares of $97\,^{17}/_{19}$p (2010 236,585,205)	**232.2**	231 6

Changes in share capital were as follows

	Number	£m
Ordinary shares of $97\,^{17}/_{19}$p		
At 1 April 2010	236,585,205	231 6
Shares issued under the group's Employee Sharesave Scheme	550,525	0 5
Shares issued under the group's Share Option Scheme	6,804	0 1
At 31 March 2011	**237,142,534**	**232 2**

9 Share premium

	2011 £m	2010 £m
At 1 April	**75 9**	71 9
Share premium arising on issue of shares for Employee Sharesave Scheme	**4 1**	4 0
At 31 March	**80 0**	75 9

10 Other reserves

	Capital redemption reserve £m	Hedging reserve £m	Total other reserves £m
At 1 April 2009	156 1	(9 8)	146 3
Transfers to the profit and loss account on cash flow hedges	–	2 3	2 3
At 1 April 2010	156 1	(7 5)	148 6
Transfers to the profit and loss account on cash flow hedges	–	2 0	2 0
At 31 March 2011	**156 1**	**(5 5)**	**150.6**

The capital redemption reserve arose on the repurchase of B shares This is not distributable

11 Reconciliation of movements in shareholders' equity

	Share capital £m	Share premium £m	Other reserves £m	Retained earnings £m	Equity attributable to the equity holders of Severn Trent Plc £m
At 1 April 2009	231 0	71 9	146 3	2,274 5	2,723 7
Cash flow hedges					
- transfers to net profit	–	–	2 3	–	2 3
Share options and LTIPs					
- proceeds from shares issued	0 6	4 0	–	–	4 6
- awards granted by subsidiaries	–	–	–	5 2	5 2
Net profit for the year	–	–	–	140 0	140 0
Dividends	–	–	–	(159 7)	(159 7)
At 1 April 2010	231 6	75 9	148 6	2,260 0	2,716 1
Cash flow hedges					
- Transfers to net profit	–	–	2 0	–	2 0
Share options and LTIPs					
- proceeds from shares issued	0 6	4 1	–	–	4 7
- awards granted by subsidiaries	–	–	–	4 4	4 4
Net profit for the year	–	–	–	264 5	264 5
Dividends	–	–	–	(169 4)	(169 4)
At 31 March 2011	**232 2**	**80.0**	**150.6**	**2,359.5**	**2,822 3**

In previous years £1,221 2 million of the company's retained profit arose as a result of group restructuring exercises, and is not considered likely to be distributable As permitted by Section 408 of the Companies Act 2006, no profit or loss account is presented for the company

12 Employee costs and auditors' remuneration

	2011 £m	2010 £m
Wages and salaries	**1.3**	1 2
Social security costs	**0 2**	0 1
Pension costs	**0 6**	0 8
Total employee costs	**2 1**	2 1

For details of directors' remuneration see the Directors' remuneration report on pages 51 to 55

Fees payable to Deloitte LLP and their associates for non-audit services to the company are not required to be disclosed because the consolidated financial statements are required to disclose such fees on a consolidated basis

13 Employee numbers

Average number of employees of the company (including executive directors) during this year was 12 (2010 11)

All were based in the United Kingdom

Notes to the company financial statements (continued)

14 Employee share schemes

For details of employee share schemes and options granted over the shares of the company, see note 33 of the group financial statements Details of the LTIP conditional awards and share options granted by the company to its employees are set out below

The company has charged £0 1 million (2010 £0 1 million) to the profit and loss account in respect of share based payments

At 31 March 2011 the number of options that were exercisable under each of the share based remuneration schemes was as follows

	2011		2010	
	Number of exercisable options/awards	**Weighted average exercise price**	Number of exercisable options	Weighted average exercise price
Employee Sharesave Plan	–	–	161	1,172
Long Term Incentive Plan	–	–	–	–
Share Matching Plan	–	–	–	–

(i) Long Term Incentive Plan

Changes in the number of awards outstanding during the year

	Number of awards
Outstanding at 1 April 2009	80,140
Granted during the year	4,813
Lapsed during the year	(76,574)
Outstanding at 1 April 2010	8,379
Granted during the year	4,422
Outstanding at 31 March 2011	**12,801**

Awards outstanding at 31 March were

		Number of shares	
Date of grant	Normal date of vesting	**2011**	2010
2008	2011	**3,566**	3,566
2009	2012	**4,813**	4,813
2010	2013	**4,422**	–
		12,801	8,379

(ii) Employee Sharesave Scheme

Changes in the number of options outstanding during the year

	Number of shares	Weighted average exercise price
Outstanding at 1 April 2009	1,237	598p
Granted during the year	449	806p
Exercised during the year	(1,237)	598p
Transferred from other group companies	4,107	874p
Outstanding at 1 April 2010	4,556	867p
Lapsed during the year	(161)	1,172p
Outstanding at 31 March 2011	**4,395**	**856p**

Options outstanding at 31 March were

			Number of shares	
Date of grant	Normal date of vesting	Option price	**2011**	2010
January 2007	2010, 2012 or 2014	1,172p	–	161
January 2009	2012 or 2014	862p	**3,946**	3,946
January 2010	2013 or 2015	806p	**449**	449
			4,395	4,556

14 Employee share schemes (continued)

(iii)Share Matching Plan (SMP)
Changes in the number of options outstanding during the year

	Number of share options
Outstanding at 1 April 2010	–
Granted during the year	457
Exercised during the year	–
Outstanding at 31 March 2011	457

Options outstanding at 31 March were

		Number of shares	
Date of grant	Normal date of vesting	2011	2010
May 2011	June 2011	**457**	–
		457	–

15 Pensions

The company operates two defined benefit schemes (being the Severn Trent Pension Scheme and the Severn Trent Water Mirror Image Pension Scheme) In addition, the group operates an unfunded arrangement for certain employees whose earnings are above the pension cap

Further details regarding the operation of these schemes are given in note 27 of the group financial statements

The company is currently unable to identify its share of the underlying assets and liabilities from the group's defined benefit schemes, and hence it continues to account for the cost of contributions as if the scheme was a defined contribution scheme

The pension charge for the year was £0 2 million (2010 £0 8 million)

16 Related party transactions

The company has taken advantage of the exemption under FRS 8 "Related Party Disclosures" and not disclosed details of transactions with other undertakings within the Severn Trent group of companies

17 Contingent liabilities

a) Bonds and guarantees
The company has entered into bonds and guarantees in the normal course of business No liabilities are expected to arise in respect of either the bonds or guarantees

b) Bank offset arrangements
The banking arrangements of the company operate on a pooled basis with certain of its subsidiary undertakings Under these arrangements participating companies guarantee each others' overdrawn balances to the extent of their credit balances, which can be offset against balances of participating companies

18 Post balance sheet events

On 26 May 2011 the board of directors proposed a final dividend of 39 05 pence per share

19 Dividends

For details of the dividends paid in the years ended 31 March 2011 and 31 March 2010 see note 14 in the group financial statements

Five year summary

Continuing operations	2011 £m	2010 (restated) £m	2009 £m	2008 £m	2007 £m
Turnover	**1,711 3**	1,703 9	1,642 2	1,552 4	1,480 2
Profit before interest, tax and exceptional items	**519 1**	557 1	469 9	469 5	405 3
Net exceptional items	**(21 4)**	(49 7)	(18 9)	(68 8)	24 7
Net interest payable before (losses)/gains on financial instruments	**(230 6)**	(218 8)	(196 4)	(177 4)	(153 8)
(Losses)/gains on financial instruments	**(14 2)**	45 7	(87 0)	(31 0)	48 8
Results of associates and joint ventures	**0.1**	0 1	–	0 1	0 5
Profit on ordinary activities before taxation	**253 0**	334 4	167 6	192 4	325 5
Current taxation on profit on ordinary activities	**(32.1)**	(40 7)	(52 1)	(56 2)	(58 5)
Deferred taxation	**53 6**	(42 2)	(171 5)	74 4	(18 4)
Profit on ordinary activities after taxation	**274 5**	251 5	(56 0)	210 6	248 6
Discontinued	–	1 0	–	0 8	20 0
Profit for the period	**274 5**	252 5	(56 0)	211 4	268 6
Net assets employed					
Fixed assets	**6,635 3**	6,516 1	6,169 9	5,892 9	5,675 5
Other net liabilities excluding net debt, retirement benefit obligation and provisions	**(320 4)**	(317 2)	(287 2)	(217 3)	(242 9)
Derivative financial instruments[1]	**(90 5)**	(125 3)	(153 9)	(26 1)	(41 6)
Retirement benefit obligation	**(292 1)**	(354 9)	(233 0)	(165 6)	(135 1)
Provisions for liabilities and charges and deferred tax	**(957 4)**	(1,010 3)	(988 0)	(885 5)	(930 0)
Net assets held for sale	–	–	4 2	–	–
	4,974 9	4,708 4	4,512 0	4,598 4	4,325 9
Financed by					
Called up share capital	**232 2**	231 6	231 0	229 7	228 3
Reserves	**867 6**	709 1	715 1	971 3	905 9
Total shareholders' funds	**1,099.8**	940 7	946 1	1,201 0	1,134 2
Non-controlling interests	**6 3**	6 3	6 0	4 2	3 1
Net debt[2]	**3,868 8**	3,761 4	3,559 9	3,393 2	3,188 6
	4,974 9	4,708 4	4,512 0	4,598 4	4,325 9
Statistics					
Earnings per share (continuing) - pence	**115 2**	105 6	(24 6)	89 3	106 1
Adjusted earnings per share - pence	**105.6**	122 8	92 7	97 8	82 4
Dividends per share (excluding special dividend) - pence	**65.1**	72 3	67 3	65 6	61 5
Dividend cover (before exceptional items and deferred tax)	**1 6**	1 7	1 4	1 5	1 3
Gearing	**77 8%**	79 9%	78 9%	74 0%	73 3%
Ordinary share price at 31 March - pence	**1,446.0**	1,195 0	990 0	1,419 0	1,434 0
Average number of employees					
- Severn Trent Water	**5,236.6**	5,685 8	5,624 0	5,569 0	5,289 0
- Other	**3,044 9**	3,101 7	3,144 0	2,814 0	7,172 0

[1] Excludes hedging instruments

[2] Includes hedging instruments

The prior year figures have been restated to reflect the impact of IFRIC 18, which is described in note 3

Gearing has been calculated as net debt divided by the sum of equity and net debt

Severn Trent Water – Delivering against our KPIs

Basis	KPI	2009/10 Performance	2010/11 performance	2010/11 quartile	At a glance
MAT	Lost time incidents per 100,000 hrs worked[1]	0.36	0.37	Upper	⊖
QR	Employee motivation %[2]	74%	74%	Lower	◒
MAT	Water quality (test failure rate) ppm	131	210	Upper	⊖
MAT	Customer written complaints per 1,000 properties[3,4]	4.95	5.73	Upper	⊖
MAT	First time call resolution for billing %[5]	89%	90%	Median	⊖
MAT	Unplanned interruptions > 6 hrs per 1,000 properties[3]	10.09	23.85	Lower	⊖
NPR	Properties at risk of low pressure per 1,000 properties[3]	0.12	0.07	Upper	●
MAT	First time job resolution %[5]	96.5%	97.5%	Upper	⊖
QR	Non-performance against Regulatory Obligations %[5]	5%	4%	Upper	⊖
AMP	Capex (Gross) vs Final Determination %[6,14]	6.1%	7.4%	N/A	N/A
ACT	Debtor days[7]	32.6	33.8	Median	⊖
ACT	Opex - £m[6,7]	492.4	519.0	N/A	N/A
MAT	Pollution incidents (cat 1, 2 & 3)[8,9]	322	378	Median	⊖
MAT	Sewer flooding incidents – other causes per 1,000 properties[3,13]	0.131	0.103	Upper	⊖
ACT	Sewage Treatment Works – failing consent limit %[9,10]	1.80%	1.69%	Lower	⊖
ACT	Supply availability %[11]	91.9%	94.4%	Lower	⊖
MAT	Net Energy Use – GWh[5,12]	714	706	Upper	⊖
MLE	Leakage Ml/d[3,6]	497	497	N/A	N/A

Key

● **Improved quartile** ⊖ **Maintained quartile** ◒ **Declined quartile**

Notes

Benchmarks updated in September

MAT = Moving Annual Total
QR = Quarterly Review
NPR = Number of Properties on Register
AMP = Asset Management Plan 5 to date
PPS = Percentage of Population Served
MLE = Maximum Likelihood Estimate
ACT = Year end Actual

1. Actual performance across all employees and agency staff
2. Performance based on annual survey of all employees (2009/10 based on a sample of 10% of STW's employees)
3. As reported in June Return to Ofwat. Performance figures are provisional at this stage as the June Return will be submitted to Ofwat on 10 June 2011
4. Performance excludes properties billed by other water companies
5. Actual performance based partially or wholly on internal data
6. As this is the first year of AMP5, benchmark data is unavailable until September 2011
7. Actual performance based on audited UK GAAP financial statements for the year ended 31 March 2011
8. Metrics of this KPI changed from pollution incidents per 1,000 properties to number of pollution incidents. Prior year performance has been restated accordingly
9. Measure for calendar year to 31 December 2010
10. Metrics of this KPI changed to align with Environment Agency approach. Prior year performance has been restated accordingly
11. Metrics of this KPI changed from security of supply to supply availability. Prior year performance has been restated accordingly. The KPI measures how much of our designed capacity is available taking into account known restrictions and works outages. There were no supply failures resulting from works restrictions during the year
12. Metrics of this KPI changed from KWh/Ml to GWh. Prior year performance has been restated accordingly
13. Excludes minor escape of sewage
14. Percentage outperformance against the Final Determination

Information for shareholders

Electronic communications and our website

Under the Articles of Association, the company is authorised to communicate with shareholders either via the Severn Trent Plc website or by post The company last wrote to shareholders in April 2008 asking that they choose to either

- provide an email address to receive notifications when shareholder documentation is made available on the website, or
- continue to receive shareholder documentation in hard copy by returning the personalised reply card

If the completed card was not returned then, in accordance with the Companies Act 2006, shareholders were deemed to have agreed to receive shareholder documentation via the website These shareholders, and those who have positively elected for website communication, will receive, immediately prior to the publication date, notification whenever shareholder documents are available to view on the website at www severntrent com

Shareholders may receive electronic communications either

- via email – this option is available though Shareview Shareholders will receive an email notification when a new document is made available, or
- via our website – shareholders will receive a notification by post when a new document is made available

The electronic arrangements enable shareholders to access information immediately as it becomes available By using electronic communications the company is also able to both reduce its impact on the environment from reducing the use of paper and the energy required for publication and distribution, and benefit from savings associated with reduced printing and mailing costs

Shareholders who register to receive shareholder documentation from Severn Trent Plc electronically can

- view the Annual Report and Accounts on the day it is published,
- receive an email alert when shareholder documents are available,
- cast their AGM vote electronically, and
- manage their shareholding quickly and securely online, through Shareview

Shareholders who receive such a notification are entitled to request a hard copy of the document and may also change the way they receive communications, at any time, by contacting Equiniti Visit www shareview co uk for more information and to register for electronic shareholder communications

We will periodically consult with shareholders to check how they wish to receive information from us and a shareholder is taken to have agreed to website communications if a response has not been received

Notwithstanding any election, the company may, at its sole and absolute discretion, send any notification or information to shareholders in hard copy form

Corporate website

Our website provides company news and information, together with links to our operational businesses' websites The Investor Centre on the website contains up to date information for shareholders including

- comprehensive share price information,
- financial results,
- a history of dividend payment dates and amounts, and
- access to current and historical shareholder documents such as the Annual Report and Accounts

Severn Trent shareholder helpline

The company's registrar is Equiniti Limited Equiniti's main responsibilities include maintaining the shareholder register and making dividend payments

If you have any queries on the following matters you should contact Equiniti

- transfer of shares,
- change of name or address,
- lost share certificate,
- lost or out of date dividend cheques and other dividend queries,
- death of the registered holder of shares, or
- any other query relating to your Severn Trent shareholding

Registrar contact details

Telephone 0871 384 2967*
Overseas enquiries +44 121 415 7044
Text phone 0871 384 2255*
By post Equiniti, Aspect House, Spencer Road, Lancing, West Sussex, BN99 6DA
Email severntrent@equiniti com

Dividend payments directly into bank accounts

Dividends can be paid automatically into your bank or building society account This service has a number of benefits

- no risk of the dividend cheque being lost in the post,
- the dividend payment is cleared more quickly as the cash is paid directly into the account on the payment date without the need to pay in the cheque and wait for it to clear, and
- since the 2009/10 financial year, a single consolidated tax voucher is issued annually in February in time for your self assessment tax return

To take advantage of this service or for further details contact Equiniti or visit www shareview co uk

Dividend reinvestment plan

A dividend reinvestment plan was introduced in July 2009

The plan gives shareholders the option of using their dividend payments to buy more Severn Trent Plc shares instead of receiving cash If you would like to participate in the plan, please request a dividend reinvestment plan mandate from Equiniti Financial Services Limited

Telephone 0871 384 2268*

Lines are open from 8 30am to 5 30pm Monday to Friday

Telephone number from outside the UK +44 121 415 7058

Overseas dividend payments

Shareholders in over 30 countries have the opportunity to receive Severn Trent dividends in their local currency For a small administration fee, shareholders can have their dividends automatically converted from sterling and paid into their bank account, normally within five working days of the dividend payment date Please call +44 121 415 7044 for further details

Amalgamating different share accounts

Shareholders with more than one account, arising from inconsistencies in name or address details, may avoid receipt of duplicate mailings by asking the registrar to amalgamate their holdings

* Calls to these numbers are charged at 8 pence per minute from a BT landline Other providers costs may vary

Lost investors
During 2009/10 we appointed ProSearch to look for investors who had failed to keep their details up to date We have unclaimed funds waiting to be claimed Shareholders are reminded that if they move house they need to contact Equiniti and advise them of their new address

Buying and selling shares in the UK
If you wish to buy or sell certificated Severn Trent shares, you will need to use a stockbroker or high street bank which trades on the London Stock Exchange There are also many telephone and online services available to you If you are selling, you will need to present your share certificate at the time of sale Details of low cost dealing services may be obtained from www shareview co uk or 0845 603 7037

Share price information
Shareholders can find share price information on our website and in most national newspapers Ceefax, where available, also displays share prices that are updated regularly throughout the trading day For a real-time buying or selling price, you should contact a stockbroker

Gifting your shares
To transfer your shares to another member of your family as a gift, please request a gift transfer form from Equiniti The completed transfer form together with the relevant share certificate(s) should be returned to Equiniti to record the change in ownership

If you have a small number of shares and would like to donate them to charity, please ask Equiniti for a ShareGift (charity donation scheme) transfer form ShareGift (registered charity No 1052686) is an independent charity which provides a free service for shareholders wishing to dispose charitably of small numbers of shares, which would cost more to sell than they are worth Further information is also available on the ShareGift website at www sharegift org or by telephoning 020 7337 0501

Shareholder security
Many companies have become aware that their shareholders have received unsolicited phone calls or correspondence concerning investment matters These are typically from overseas based 'brokers' who target UK shareholders, offering to sell them what often turn out to be worthless or high risk shares in US or UK investments These operations are commonly known as 'boiler rooms' These 'brokers' can be very persistent and extremely persuasive and the number of instances of this type of fraud has increased dramatically in recent years A 2006 survey by the Financial Services Authority (FSA) has reported that the average amount lost by investors is around £20,000 It is not just the novice investor that has been duped in this way many of the victims had been successfully investing for several years

In addition, in the current economic climate, boiler rooms are now targeting victims who have redundancy money or those who are not experienced investors, and are asking for smaller sums of money to be invested

If you receive any unsolicited investment advice

- ensure you get the full name of the person and organisation,
- check that they are properly authorised by the FSA before getting involved by visiting www fsa gov uk/register
- report the matter to the FSA either by calling 0300 500 5000 or visiting www moneymadeclear fsa gov uk, and
- if the calls persist, hang up

Please be aware that if you deal with an unauthorised firm, you will not be eligible to receive payment under the Financial Services Compensation Scheme The FSA can be contacted by completing an online form at www fsa gov uk/pages/doing/regulated/law alerts/overseas shtml

Shareholders are advised to be very wary of any unsolicited advice, offers to buy shares at a discount or offers of free company reports Details of any share dealing facilities that the company endorses will be included in company mailings or on our website For more detailed information from the FSA go to www moneymadeclear fsa gov uk

Shareholder fraud – tips on protecting your shareholding
To reduce the risk of fraud happening to you please consider the following

- ensure all your share certificates and dividend tax vouchers are kept in a safe place, or consider holding your shares electronically in CREST via a nominee,
- keep all correspondence from the registrar in a safe place Destroy all correspondence showing your personal details (e g shareholder reference number) by shredding,
- if you change your address inform the registrar If you receive a letter from the registrar regarding a change of address and have not recently moved house, please contact them immediately You may be a victim of identity theft, and
- know when dividends are paid Consider having your dividend paid directly into your bank or building society account, reducing the risk of cheques being intercepted or lost in the post If you change your bank or building society account, inform the registrar of the details of your new account immediately Respond to any letters the registrar sends you about this

If you have any reason to believe that you may have been the target of a fraud, or attempted fraud, please contact the registrar immediately

Unsolicited mail
The company is legally obliged to make its share register available to the general public Consequently some shareholders may receive unsolicited mail If you wish to limit the amount of unsolicited mail you receive please contact

The Mailing Preference Service (MPS),
Freepost 29 LON20771, London W1E 0ZT

Alternatively, register online at www mpsonline org uk or call the MPS Registration line on 0845 703 4599

Share capital history
Information on the company's share capital history, including the share capital reorganisation in August 1997 and the demerger of Biffa Plc, return of capital by payment of a special dividend and share consolidation in October 2006, is available from the Investor Centre pages on our website

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