

Severn Trent Water Limited

Report and financial statements

Year ended 31 March 2009

Registered number: 2366686

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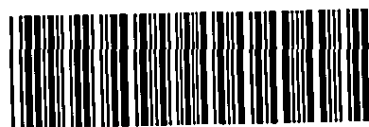
COMPANIES HOUSE

Delivering performance

through higher standards and continuous improvement

Annual Report
and Accounts
2009

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COMPANIES HOUSE

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Our turnover was

> £1,324.9m in 2008/09,
up 4.7% on 2007/08

Our profit before tax was

> £281.6m, up 17.2%

Turnover

+4.7%

2009 £1,324.9m

2008 £1,265.3m

Operating profit before
exceptional items

+3.8%

2009 £488.3m

2008 £470.4m

Profit before tax

+17.2%

2009 £281.6m

2008 £240.3m

Our business at a glance

For every £2 we make in profit we invest approximately

£3

back into water and sewerage assets.

Severn Trent Water Limited provides high quality water and sewerage services to over 3.7 million households and businesses across the Midlands and mid Wales.

We provide drinking water to 7.4 million people and sewerage services to 8.5 million people across the Midlands and mid Wales. We employ 5,624 people.

Our business is streamlined and organised around our three key processes:

- water
- waste water
- customer relations

Our key strengths:

- we have amongst the lowest bills for customers in the UK industry
- we provide drinking water and waste water quality above industry average
- we are a streamlined business delivering against 20 Key Performance Indicators (KPIs)
- we are committed to the long term responsible stewardship of the business, to the environment, customers and the communities in which we live and work

Our industry

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

The industry is monitored and controlled by government appointed regulators who report each year on standards and progress.

Our water quality and environmental standards

Drinking water quality is regulated by the Drinking Water Inspectorate (DWI). Compliance with EU and UK environmental standards is regulated by the Environment Agency.

The DWI publishes an annual report assessing the quality of water supplied by us. It also reviews our standards in the previous calendar year. The report includes the results of thousands of tests carried out across our region. According to these tests, we have consistently achieved 99.9% compliance with water quality standards since 1997. The DWI annual reports are published on their website: www.dwi.gov.uk

Our prices

The industry's economic regulator is the Water Services Regulation Authority (Ofwat). Ofwat sets our price limits to enable us to finance our activities.

Each water company has to submit an annual return (the June Return) to Ofwat covering its activities.

Ofwat measures each company's customer and operational service against a number of so called DG performance indicators.

The June Return and the DG indicators enable Ofwat to monitor and compare the performance and progress of the companies, and ensure that customers' service standards are protected. Ofwat produces an annual league table of performance against these indicators across the industry.

Every five years, Ofwat sets annual price limits for each water company. The current price limits were set in 2004 for the period 2005-10 (the AMP4 period). The present 2009 price review (PR09), will set price limits for the period 2010-15 (AMP5) and will be completed by the end of the year.

See page 3 for our final business plan.

Our region

Our region stretches from mid Wales to Rutland and from the Bristol Channel to the Humber. We deliver nearly 2 billion litres of water a day to homes and businesses through 46,000 km of pipes. We take away around 2.5 billion litres of waste water per day through 54,000 km of sewers, treating it at over 1,000 sewage works.

Our vision for the future

In 2007, each water company produced a 25 year Strategic Direction Statement for the years 2010-35. This forms the key foundation for the long term direction and development of the companies. The full document is available for download at www.stwater.co.uk/sds

Our vision for Severn Trent Water is to be the water and waste water company in the UK which achieves the highest quality and customer service standards while offering customers the lowest prices, with great people delivering the service.

Our strategic direction revolves around eight Key Strategic Intentions (KSIs), which we will deliver over the next 25 years, while ensuring we have a sustainable impact on the environment and playing a critical role in the communities we serve. We focus on delivering continuously improving performance against 20 KPIs. You can find more information on our KPIs on pages 4 and 5 of this report.

With our business aligned around driving up standards, driving down costs and developing great people, we have been focusing on improving our operational performance on all fronts. We report on our performance against our KSIs and KPIs in the following pages.

Delivering on our promises

In 2008/09, we continued to focus on water, to deliver improvements in our business and to improve our performance across the company.

Delivering continuous improvement

We said to our customers that we would make fewer mistakes, deal with their calls more effectively and reduce the number of causes of complaint in our business. We said to Ofwat, our economic regulator, that we would deliver reduced leakage, improve security of supply and reduce pollution incidents. We said to our investors that we would continue to deliver operating (opex) and capital (capex) efficiencies and maintain our progressive dividend. We said to our stakeholders that we would operate to the highest standards of governance. We said to our people that we would continue to improve what it's like to work for Severn Trent.

We said we would do these things and we have done them, in line with our ongoing commitment to be the best water and waste water company in the UK, with the highest standards, the lowest possible charges and great people.

We believe in continuous improvement and we are giving our people the encouragement, the training, the tools and techniques to ensure it is a fundamental everyday part of the way we do things.

Continuous improvement is about finding ever safer, better, faster ways of doing things in line with the Key Strategic Intentions we are committed to delivering over the next 25 years and the 20 Key Performance Indicators we work towards and assess ourselves against day after day. It's about becoming ever more customer focused. It's about being ever more ambitious for efficiency improvements that help lower charges, for process improvements that help raise standards, and for workplace improvements that attract, retain, develop and reward our great people.

You have to keep on challenging the way that people think and behave, you have to ensure that people have the right skills and tools to solve problems, you have to ensure that you involve people in solving problems so that you get a diversity of ideas, you have to engender a dissatisfaction with the status quo, you have to engender a mindset of enquiry and constructive challenge. These things characterise the way we work.

Continuous improvement runs through our Final Business Plan for AMP5. Preparations for AMP5 have gone well. There is still a way to go in the regulatory process, but we have what we believe to be a high quality, holistic and balanced plan that has customers at its heart, is supported by all the key stakeholders and will enable a fair and appropriate return for our investors.

We talk more about our plan on page 3 of this report.

Looking ahead

Continuous improvement is central to the way we tackle the many challenges and opportunities that lie ahead. We are very aware of the challenging economic climate and what that means for our customers, for our supply chain, and for our funding. We are being very diligent in keeping our standards as high as they need to be and constantly seeking to make every efficiency in order to continue keeping prices as low as possible for our customers.

We are also very conscious of our corporate responsibilities, not least in playing our part to address the increasing challenges of climate change through our water resources, our waste processing, our energy use and our engagement with customers through education. We are one of the few companies that has committed to deliver the UK government's carbon reduction targets and we continue to lead the way in renewable energy generation in our sector.

In the future, the nature of our industry is bound to change. We can't be sure exactly how, but we can and will play our part in shaping developments, for example, around competition in the UK regulated industry. As a customer focused business committed to highest standards, lowest possible charges and great people, we have clear ideas about how it might best be developed in a way that both benefits customers and addresses regional water supply imbalances. We are actively discussing these ideas with Ofwat and other interested parties.

Whatever the future holds, we will continue focusing on water, on our core skills, on aligning ourselves around our key processes, and on having excellent relationships with our key stakeholders. Continuous improvement is the best possible preparation for us prospering now and in the days ahead.

Tony Wray
Chief Executive

Final Business Plan (2010-15)

“

Sir James Perowne,
Consumer Council
for Water

CCWater like the way Severn Trent's plan reflects customer priorities. We value the transparent and open consultations they have had with us and other stakeholders in developing the programme.

“

Roger Owen,
Natural England

Natural England is pleased to have been involved with Severn Trent throughout the business planning process and we very much value our relationship with the company. We have been encouraged by the commitment to maintaining and enhancing the environment, particularly for biodiversity and the development of more sustainable catchment management solutions.

We believe we have a high quality, holistic, balanced Final Business Plan which has customers at its heart and takes into account the interests of all our stakeholders.

We submitted our Final Business Plan for 2010-15 to Ofwat on 7 April 2009.

Our Plan is aligned to our eight Key Strategic Intentions set out in our 25 year Strategic Direction Statement. It has customers at the heart of it, in delivering the improvements they want for a price they consider to be good value for money with the help of our talented and committed workforce.

The Plan has been put together in a holistic and balanced way and has been produced directly from our business planning process. It reflects the views of the wider stakeholder groups we consulted during its preparation. We have engaged with the Consumer Council for Water, the Environment Agency, the Drinking Water Inspectorate and Natural England – sharing the results and outcomes of our plan and research. We undertook extensive research into customer expectations and their willingness to pay for improvements as our plan developed.

The next steps in the business plan process will be for Ofwat to publish its draft determination of prices for consultation in July 2009 and final determination in November 2009.

Key improvements outlined in the Plan include:

KSI	Examples of key outputs planned for 2010-15
Providing a continuous supply of quality water	<ul style="list-style-type: none"> Increased spending on our assets to <ul style="list-style-type: none"> – Increase network resilience – Ensure that the environmental and drinking water quality improvements achieved since privatisation are maintained Sustainable solutions through catchment management
Dealing effectively with waste water	<ul style="list-style-type: none"> Improving services by reducing sewer flooding Environmental improvements delivered through improving sewage treatment works Sustainable solutions for drainage
Responding to customers' needs	<ul style="list-style-type: none"> Lowest possible bills rising by just 4% in real terms by the end of the period 2010-15 Improving the quality and speed of response when customers contact us
Minimising our carbon footprint	<ul style="list-style-type: none"> Taking into account carbon impacts when assessing quality and environmental improvements
Having the lowest possible charges	<ul style="list-style-type: none"> Delivery of continued improvements in efficiency, for both operating costs and capital expenditure, to keep bills down
Having the right skills to deliver	<ul style="list-style-type: none"> Maximising the benefits of our process, technology, workplace and structural changes, whilst retaining and upskilling the talent of our workforce
Maintaining investor confidence	<ul style="list-style-type: none"> A plan financed to strike the right balance in keeping prices low for the long term and maintaining investor confidence, including delivering a sustainable and progressive dividend policy
Promoting an effective regulatory regime	<ul style="list-style-type: none"> Continuing to work constructively with our regulators and government on ways in which the regulatory regime could be improved for customers and the environment Having a business plan that is realistic and robust

Delivering against our KPIs

We measure our performance and progress against 20 Key Performance Indicators. Our aim is to achieve upper quartile performance across our 20 KPIs.

Our 20 KPIs are the result of a detailed and thorough examination of the key aspects of Severn Trent Water's performance. This includes benchmarking against comparable companies in the water and sewerage sector and other companies with similar characteristics in other sectors. We use a range of publicly available and internally generated data to identify the population that we should compare ourselves to. This process involves a number of judgments to ensure we used appropriately comparable data points for each measure.

Throughout 2008/09, we have been measuring ourselves against our KPIs and the updated benchmarks we established last year. The results are presented here.

We are committed to continually review and reset our KPI targets and expectations, in line with our Strategic Direction Statement.

We reward our people based on the 20 KPIs.

Reduction in pollution incidents

27%

Reduction in lost time incidents

30%

Reduction in unplanned interruptions to supply

67%

Reduction in written customer complaints

41%

Basis	Key performance indicator
MAT	Lost time incidents per 100,000 hrs worked ²
QR	Employee motivation % ³
MAT	Water quality (test failure rate) ppm ¹³
MAT	Customer written complaints per 1,000 properties ^{1,5}
MAT	First time call resolution for billing % ⁶
MAT	Unplanned interruptions > 6 hours per 1,000 properties ^{1,7}
NPR	Properties at risk of low pressure per 1,000 properties ^{8,9}
MAT	First time job resolution % ⁵
QR	Non performance against regulatory obligations % ^{6,12}
ATD	Capex (Gross) vs final determination % ¹⁰
MAT	Capital process quality (no defects per £100k) ⁶
	Debtor days ^{8,10}
MAT	Opex vs final determination (UK GAAP) £m ¹⁰
MAT	Cost to serve per property - £ ¹¹
MAT	Pollution incidents (cat 1, 2 and 3) per 1,000 properties ⁴
MAT	Sewer flooding incidents - other causes per 1,000 properties ¹
PPS	Sewage treatment works - breach of consents % ⁴
	Security of supply ⁸
MAT	Net energy use - kWh/MI ⁶
MLE	Leakage MI/d ¹

2007/08 Performance	2008/09 Performance	2008/09 Quartile	At a glance	Know more
0.61	0.43	Upper		
77%	83%	Upper		
240.1	200.4	Upper		
10.90	6.44	Upper		
85%	88%	Upper		
21.86	7.29	Lower		
0.46	1.21	Upper		
85%	96%	Upper		
15%	10%	Median		
1.7%	5.0%	Upper		
0.03	0.00	Upper		
37.4	33.1	Median		
480.9	500.9	Median		
236.82	236.53	Upper		
0.11	0.08	Upper		
0.21	0.17	Median		
0.0%	0.0%	Upper		
95	98	Median		
608	622	Upper		
491	492	Upper		

Sewage treatment works
compliance with consents

100%

Compliance with water
quality standards

99.98%

Key

- Improved
- Maintained high standards
- No change
- Page numbers to related articles

Notes:

All measures are for the period to 31 March 2009, except as stated.

MAT = Moving Annual Total

QR = Quarterly Review

NPR = Number of properties on register

ATD = AMP4 to date

PPS = Percentage of population served

MLE = Maximum Likelihood Estimate

1. As reported in June Return to Ofwat. Performance figures are provisional at this stage as the June Return will be submitted to Ofwat on 12 June 2009.
2. Actual performance across all employees and agency staff.
3. Performance based on quarterly survey of 10% of permanent employees.
4. Measure for calendar year to 31 December 2008.
5. Performance excludes properties billed by other water companies.
6. Actual performance based on internal data.
7. 2008 performance excludes impact of Summer 2007 flooding. 2008 performance is 184.5 if impact of Summer 2007 flooding included.
8. Measure as at 31 March 2009
9. 2009 and 2008 performance includes impact of new pressure loggers installed in 2007/08. Excluding pressure loggers, 2009 performance is 0.005 (2008: 0.06) as there has been a significant reduction in reactive identification.
10. Actual performance based on audited UK GAAP financial statements for the year ended 31 March 2009 and expressed in absolute terms.
11. Actual performance based on audited regulatory accounts for the year ended 31 March 2009.
12. Measure expressed as percentage non performance against regulatory obligations.
13. Measure now expressed as test failure rate (parts per million). 2008 performance restated accordingly.

Throughout 2008/09, we have been performing well against our KPIs in line with our commitment to highest standards, lowest possible charges and great people.

Focus on corporate responsibility

Corporate responsibility (CR) must be at the heart of the way we develop, manage and operate for long term sustainable benefit and the way we strive for highest standards, lowest possible charges and great people. In 2008/09, we focused on aligning our CR activities even more closely to the fundamental objectives of our business, our eight Key Strategic Intentions (KSIs). Because all areas of our business are linked closely to our CR agenda we have not included a separate section in this review. We do, however, recognise that a number of our stakeholders are particularly interested in understanding more about some of the key CR issues we are addressing. We have therefore produced a separate CR summary report which is available from our website, alongside additional online data and information.

Focus on highest standards

This first section looks at how we have been improving and performing in water, waste and customer service.

KSI: Providing a continuous supply of quality water

We have a number of projects and also KPIs that contribute to ensuring we have the highest standards in our water service.

Water quality

This year we continued to achieve one of the best records in the industry at 99.98% compliance with the regulatory standards set by the Drinking Water Inspectorate.

Our KPI now measures compliance with regulatory samples taken along the whole process from reservoir to tap. This is a more challenging measure which enables us to gain a broader and deeper understanding and allows us to drive water quality even higher through more effective long term solutions.

Unplanned interruptions

We significantly improved our KPI performance from last year by reducing the number of unplanned interruptions by 67% after excluding the effect of flooding at The Mythe Water Treatment Works in July 2007. Our KPI for unplanned interruptions to supply is based on Ofwat's DG3 level of service. In 2008/09, around 25,000 properties experienced unplanned interruptions to supply on this measure, compared to around 195,000 properties in 2007/08 (due to exceptional weather that year). This represents less than 1% of the properties connected to our network, compared to 5.7% in 2007/08.

By analysing the problems we had in 2007, we have been able to focus on improving our operational procedures and response times and aim to continue to look for ways to drive up our performance in this area.

Low pressure

We have installed 4,000 permanent pressure loggers throughout our distribution network to identify more points of low pressure and their root causes.

In the short term, as expected, this has resulted in us identifying more properties at risk, putting pressure on our KPI performance. This year we have identified and rectified over 9,000 properties at risk. We have 4,142 properties on the register and we intend to address these in the coming year. This compares to 1,546 properties in 2007/08 and represents around 0.12% of the properties we serve.

Maintaining security of supply

We have replaced our raw water storage measure with a new security of supply KPI. This is a more complete measure of our ability to supply treated water to customers as opposed to the amount of raw water storage we have and is based on the Ofwat security of supply index.

We remain on track to deliver in line with our written undertaking to Ofwat on security of supply index and recorded a performance this year of 98.

We are making good progress with our major scheme at Frankley Water Treatment Works commissioned in 2009, which will enable us to pump up to 120 megalitres per day (Ml/d) from the river Severn into the works.

Meeting our leakage target

Our leakage was 492 Ml/d in 2008/09. For the second year running and despite the coldest winter for eight years, we have met our leakage target of 500 Ml/d set by Ofwat. In 2008/09, we found and fixed 39,000 leaks, a similar number to 2007/08.

With increased focus on water efficiency, being able to reduce leakage becomes ever more important for our customers, for the environment and for our business. We have succeeded as a result of better network maintenance, better response times to finding and fixing leaks and a better understanding of where water is used.

Each year we invest in maintaining, repairing and modernising our extensive water network, some of which is over 100 years old. In AMP4 we set a target of 1,100 km of mains to be renewed over five years. We have already achieved this target and are planning to deliver 1,230 km at a cost of 3% more than the amount assumed in the Ofwat determination.

Improving flood protection at our sites

Following the floods in 2007, we provided additional flood protection at four water treatment sites. At The Mythe Water Treatment Works, the temporary flood barriers remain in place while we seek planning permission for permanent flood defences. We are also seeking planning permission for an additional pipeline to bring extra supply into the Gloucester area. We continue to liaise closely with the Gloucestershire scrutiny committee.

Investing in improving the resilience and capacity of our network Given the demands of climate change and population growth, investing in improving the resilience and capacity of our network will become increasingly important. Our draft Water Resources Management Plan, published on www.stwater.co.uk sets out our proposed strategy for maintaining the balance between supply

Putting fats, oils and grease to good use

At the heart of our vision for corporate responsibility are projects that benefit our communities, environment, customers and business. A great example is our project with the charity Community Service Volunteers (CSV), Grease Lightening. This trial project involves doorstep collections of fats, oils and grease (FOG) from homes that may usually put these

blockage causing substances down the drain. The FOG collected is used for biofuel and the money generated reinvested by CSV. Our goal is a reduction in the number of sewer blockages in this area. This will reduce community impact, our costs, and help us to keep our bills as low as possible for all customers.

and demand in our region over the next 25 years. Our strategy seeks to maximise the sustainable use of our existing water resources and includes:

- reducing leakage;
- accelerating domestic customer metering;
- improving the connectivity of our network; and
- increasing water efficiency by working with customers to install more water efficient equipment and promote water conservation.

We estimate that without future investment we face a potential shortfall of 32 Ml/d over the next five years. In our Final Business Plan, we have proposed investments that are designed to prevent a supply shortfall and ensure that we can meet customer demands for water in the future.

Promoting the responsible use of water

Water efficiency plays a key part in our water resources planning. In addition to saving water in our own business, we have worked on helping our customers reduce the water they use. For example, we have run workshops with our major use customers to help them identify ways to save water and reduce their bills. We also have a range of programmes to provide schools and households with water saving devices and water saving advice, such as our Be Smart education programme. Through this scheme, employees work as mentors with 50 schools each year using an education pack focused on water efficiency.

KSI: Dealing effectively with waste water

Through our community and education programme, we work with schools, community groups, charities and other organisations to promote both water efficiency and the responsible disposal of waste down sinks, drains and toilets. We run a programme of site visits, for example, where we show people first hand how the waste water treatment process works and the consequences of disposing of fats, oils, grease and other products which can block sewers and result in pollution.

We also work with charities who are focused on changing people's behaviour around water and waste water for the better. These include Community Service Volunteers (see case study above), Envision, The Small Piece Trust, The Farming and Wildlife Advisory Group and The Wildlife Trust.

Looking after the environment

We place great emphasis on our environmental responsibilities. How we abstract water, manage waste water discharges, operate over 1,000 sewage treatment sites, 54,000 km of sewers, almost 3,600 sewage pumping stations and how we manage resources all have a huge potential impact on the local environment. We have a responsibility to minimise our environmental impact and maximise our use of resources.

Underlining the seriousness with which we take our responsibilities, six of our 20 KPIs are linked to environmental performance, while also reflecting our broader operational performance. The six KPIs are: breach of consents at sewage treatment works; pollution incidents; sewer flooding; security of supply; net energy use; and leakage.

100% compliance at our sewage treatment works

In 2008, all our sewage treatment works again complied with the discharge consents issued to them by the Environment Agency. This consistently high level of compliance is amongst the best in the industry and demonstrates our continuously improving performance in line with compliance standards that get higher year after year.

Fewer pollution incidents

Building on last year's progress, we again reduced pollution incidents in 2008. Pollution incidents in the calendar year 2008 are significantly down 25% to 313, from 417 in 2007. Of the total recorded, eight were in the more serious categories 1 and 2, compared with 13 in 2007. In terms of our KPI for pollution incidents, we achieved 0.08 per 1,000 properties in 2008.

In line with the 13 point plan we agreed with the Environment Agency and Ofwat to improve our environmental performance in relation to pollutions, we have heightened awareness and improved our processes in order to be able to prevent, identify and tackle pollution incidents more quickly and effectively. Our performance is considerably better than the level envisaged in the 2007 joint plan.

Reduced sewer flooding

We performed better than last year against our KPI measure for sewer flooding – other causes per 1,000 properties. There is still more to do and we have a specific improvement plan for this area, including encouraging our customers not to put fats, oils and grease down the drain as well as carrying out targeted cleansing of our network. Sewer flooding can also be caused by overloaded sewers. Properties flooded in this way are put onto flooding registers and solutions are investigated. In agreement with Ofwat, we have now brought our methodology into line with the rest of the water industry and as a result the number of properties on the register in our region has come down significantly in 2008/09.

To tackle the many complexities surrounding flooding in the most effective way, we work closely with all concerned, including local authorities, the community and the Environment Agency.

Investing in waste water improvements

We invest heavily in every aspect of our waste water process and network. In 2008/09, we invested £300 million in this part of our business and currently have around 600 schemes underway. Minworth Sewage Treatment Works, which serves over two million people in Birmingham and the Black Country, is our biggest ongoing scheme and one of the largest in the industry. The work has progressed well and is nearing completion. It is intended to enable us to achieve higher standards more efficiently ahead of the new effluent standards which come into force in March 2010. Other big sewage projects underway include improvements at Leicester, Stoke-on-Trent and Derby Sewage Treatment Works.

This year, we completed our £18 million investment to build a 21st century sewer network for Kenilworth. In Albrighton, Shropshire, we have also invested a significant amount to improve the infrastructure and, in turn, prevent sewer flooding.

We are working closely with government and agencies on the requirement for us to take ownership of private sewers in our region. This will grow our sewer network by around 50%.

Renewable energy

We have ambitious plans to expand our approach to renewable energy and have a target to generate 30% of our energy from renewable sources by 2013. The measures to achieve this include increasing use of our two established methods: hydro power and combined heat and power (CHP) using biogas from our sewage treatment works. We are also developing

new methods: wind energy and biomass energy crops. We have invested substantial time and resource into both these methods and are confident of their potential to help us significantly increase our generation of renewable energy. We intend to have our first energy crop digester operational by April 2010.

KSI: Minimising our carbon footprint

We are committed to reducing greenhouse gas emissions by being more efficient in our operations and also by increasing renewable energy generation. We have a target of generating 30% of our net electricity demand from renewable sources by 2013. This involves a wide range of solutions, from wind turbines, to generating energy from biomass crops, with by far the largest proportion of our energy generation coming from biogas generation at sewage treatment works.

In 2008/09, we undertook a major piece of work to calculate our carbon emissions for the AMP4 period and on into AMP5. Despite the continued upward pressures of providing water to more people and meeting higher water quality standards which require more energy, when we take into account both our investment in renewable technologies and energy efficiency, we have been successful in avoiding significant growth in energy consumption over the last five years.

For the next AMP, net greenhouse gas emissions are forecast to remain virtually unchanged between 2009/10 and 2014/15. Reductions come from:

- energy efficiency measures such as pump efficiency and real time pump optimisation and control;
- reduced water supply as a result of reduced leakage and water demand;
- employees relocated to new energy efficient offices such as the new Severn Trent Centre in Coventry; and
- increased renewable energy generation.

The UK Government has a number of targets for reducing UK greenhouse gas emissions. Whilst these targets are not requirements on us, they are a good way of putting our progress into context. For example, whilst the UK Kyoto target is to reduce greenhouse gas emissions by 12.5% by 2012 (against a 1990 baseline), our plans show a 23% reduction over the period since 1990.

Responsible use of energy

Our net energy use KPI measures how much energy (net of renewable energy generated by us) we consume per megalitre of water supplied or waste water treated. In 2008/09, although we succeeded in continuing to decrease our energy use, our generation of renewable energy was held back, notably at Minworth Sewerage Treatment Works, where our investment in improving effluent quality at the site has reduced the amount of biogas we have been able to produce there this year. As a result, our net energy use remained broadly in line with last year, at 622 kWh/MI during this year.

We continue to improve our energy efficiency, from increasing awareness of our processes on site and managing them more effectively, to acting on data to target high cost processes and investing in more efficient plants.

We have ambitious plans to expand our approach to renewable energy. The measures to achieve this include increasing our use of our two established methods: hydro power and combined heat and power using biogas from our sewage treatment works. We are also looking at new methods: wind energy and biomass energy crops. We are at relatively early planning stages with both of these methods but are confident of their potential to help us significantly increase our use of renewable energy.

We have engaged a consultant and are reviewing a number of potential sites for wind energy with the intention of partnering in a joint venture. We are also working with a partner on biomass energy crops. This is a particularly interesting potential source of renewable energy for us as it would make good use of land to grow crops for energy.

Biodiversity

Our biodiversity activities range from site maintenance and integration of biodiversity within capital scheme projects to management of our public access sites and the Sites of Special Scientific Interest (SSSI) that lie within our landholdings. Because of the diverse nature of these activities we have produced a strategy which sets out how we will fulfil the commitment in Severn Trent Plc's Environmental Policy to 'ensure the effective stewardship of the biodiversity of our landholdings'. In line with this, we continue to work towards reversing the declining condition of our Charnwood Reservoir (SSSI) by working in partnership with Environment Agency (EA), Natural England (NE), Farming and Wildlife Advisory (FWAG), Department for Environment, Food and Rural Affairs (DEFRA) and the local Wildlife Trust.

KSI: Responding to customers' needs

Customer service standards have also seen very positive improvements in the last 12 months.

Resolving jobs first time

Our aim is to resolve jobs on the customer's first call to us. In 2008/09 we achieved 96% first time job resolution, compared with 85% in 2007/08.

This performance improvement was delivered through our 24/7 Customer Operations Service Centre at Coventry and was based upon improved customer service and operational processes.

Building on last year's progress, we continued to improve our performance in customer service and refine our processes to find and fix operational problems as quickly and effectively as possible and we are now achieving upper quartile performance.

Reducing customer complaints

We succeeded in reducing written complaints by 41%, from 45,710 in 2007/08 to 27,066 in 2008/09. This is based on written customer complaints per 1,000 properties and improves on last year's reduction of 34%.

Better call handling

Having invested in our call handling service this year we have seen further improvements in the service received by our customers. We are developing the capability of all our teams through a comprehensive upskilling programme, and coupled with our continuous improvement programme, have improved the number of times we will resolve a customer query at the first point of contact. In 2008/09 we have achieved 88% for our first time call resolution improving on last year's result of 85%.

We handle a huge number of calls each year, including around 800,000 from people moving home. Resolving these calls first time is good both for our customers and for us. In 2008/09, we achieved 87% for our first time call resolution for billing KPI, improving on last year's result, of 85%.

Improving all customer service standards

Alongside our KPI performance measures and in line with what we said we would do, we have again improved our performance across Ofwat's DG service standards.

We achieved 99.79% for DG6 (response to written billing queries), compared to 90.72% in 2007/08. We achieved 99.95% for DG7 (response to written complaints), compared to 99.90% in 2007/08. We achieved 99.85% for DG8 (meter readings). For DG9 (customer satisfaction with telephone calls), we are running at 3.05% abandon rate and an engaged tone of less than 0.5% of calls. Again, these are upper quartile results.

This year we fitted 44,331 meters through our free meter option scheme, which we continue to promote to our customers.

In addition, we have invested in our website to improve it further to become a genuine customer service centre. The facility to manage your account online is now live, enabling customers to quickly and easily view and pay bills, update details and submit a meter reading online anytime they want to. This is part of our ambition to enable our customers to interact with us in whichever way best suits them – email, website, phone, letter or text message.

Contributing to our good performance for DG8, we have made substantial improvements to our meter reading process to ensure we get accurate and timely meter reads. The meter read is the start of the measured billing process, so if we get that right the rest should follow. Following very successful trials, we will be rolling out remote reading technology for difficult to access meters, typically in inner city areas and high rise buildings.

Looking ahead, our focus will be to carry on improving. We want to continue getting more out of our systems and we want our people to continue getting better and better at what they do.

Addressing the needs of vulnerable customers

While we actively pursue those who are able but unwilling to pay their bills, we offer flexibility for those who genuinely struggle to pay. As a result of the downturn in the economy, we are finding more people need help.

This year for the first time we have set ourselves targets to increase the number of customers on our registers for vulnerable customers. We have created a dedicated team to actively seek out customers who might need help, together with organisations such as the Citizens Advice Bureau and Age Concern. Through a combination of increasing need and increasing awareness, the number of customers on our registers has grown this year.

The amount of money in the Severn Trent Trust Fund has increased this year by £1 million to £5.5 million. We also continue to promote our WaterSure tariff to cap charges for vulnerable customers who have a water meter.

Along with the rest of the water industry we have teamed up with the Home Office and local police constabularies in supporting their distraction burglary initiative. Our password scheme is available to all our customers to reassure them that they can check the genuine identity of doorstep callers at anytime.

In recognising the differing needs of our customers we continue to provide literature in alternative formats such as braille, large print and audio throughout the year.

New connections

Our new connections team manages, from application to delivery, the connections of customers to water and waste water services.

In 2008/09 the economic climate has resulted in a decline in the level of activity undertaken. This has been most significant in the provision of services to developers. In response to these external pressures we have rationalised our department to a single operating base at our offices in Leicester Water Centre. These changes continue to build upon improvements in our performance, with connections completed within 21 working days increasing from 86% in 2007/08 to 90% in 2008/09.

Customer research

In 2008, as part of the ongoing consultation process into the business plan, further work was undertaken with the main objectives of determining stakeholders support for the proposed business plan, both in terms of planned increases and the planned programme of improvements. Overall, there was strong support for our proposals and these results have been incorporated into the Final Business Plan for PR09.

Developing a sustainable service for customers

Serving customers also means looking after their long term interests as well as their immediate concerns. We continue to maintain the serviceability of our assets. This means carrying out the work necessary to make sure our water and sewerage systems deliver reliable service in the future for customers and the environment. It takes into consideration above ground and below ground water and sewerage assets. Our most recent assessment shows that we have made progress, and we aim to continue to do so.

Business customers

The Cave Review explored the ability for business customers to choose their water supplier. We are currently considering its findings and will be continuing to work with relevant industry participants in developing our services.

Focus on lowest charges

We are committed to keep bills as low as possible for our customers. Managing our operational and capital costs is a key contributor to this.

KSI: Having the lowest possible charges

Financial performance

The past year has seen an unprecedented period of disruption to financial markets, leading to the so called 'credit crunch' and wider economic recession. The first half of the year saw increased RPI inflation, peaking at 5% in September, with a rapid fall in the second half. Annual RPI inflation at March 2009 was negative 0.4%.

This volatility has presented a number of challenges. The economics of the Ofwat regulatory framework are explicitly linked to RPI, with Ofwat's final determination for both total opex and capex set in 2002/03 prices and adjusted by the relevant inflation index each year (RPI for opex, COPI, a construction price index, for capex).

As we move into the final year of AMP4, we maintain our objective to invest efficiencies in options to enhance long term value for our customers, support our improvement plans and deliver greater efficiency into AMP5. The three key areas we are focused on are:

- accelerating our renewable energy programme to deliver greater operational efficiency, enhance our natural hedge to energy costs and reduce our carbon footprint,
- to engage with our supply chain to further our early start contracting strategy, delivering benefits in the AMP5 investment programme, and
- investments in economically enhancing technology and locations, principally the construction of the new Severn Trent Centre.

Investing in our network

Year after year, we invest in improving the quality, resilience and maintenance of our network. During 2008/09, we invested £130 million (net of grants and contributions received) in maintaining our infrastructure network. Capital expenditure, excluding spending on infrastructure maintenance (and net of grants and contributions received), was £476 million. Gross capital expenditure (including infrastructure maintenance expenditure) increased to £635 million.

We are meeting our obligations on investments and making them more efficiently.

Our capex (gross) vs final determination KPI measures our performance on managing the financial aspects of the delivery of our investment programme. This measures the percentage variance between our capital expenditure to meet our obligations for AMP4 and Ofwat's final determination.

This is a continuation of our work in 2007/08 to smooth the so called investment rollercoaster, where investment rises steeply in years two, three and four of the AMP cycle before falling off sharply in year five. Smoothing this out so that there is a steady amount of investment throughout the five years is beneficial for our contractors, because it allows them to plan their resources more easily and cost effectively, and for us, because we can gain from efficiencies.

Whilst we continue to be on track to meet our regulatory obligations and capital expenditure targets in monetary terms, the recent rapid reduction in COPI is likely to lead to a lower than anticipated regulatory capital value cap as we proceed into the final year of AMP4. We remain focused on the successful delivery of the absolute levels of expenditure previously announced, although this may result in an overall efficiency of less than the previously announced 6%.

As we move into the final year of AMP4, we continue to carefully progress a number of return enhancing investments that will provide value over the longer term. These include further renewable energy generation, the early development of capital plans for AMP5 and the new Severn Trent Centre in Coventry. In all cases, our focus is on delivering sustainable efficiencies, lowering the cost of our operations and therefore providing value for our customers.

Managing our operating costs

Despite the economic pressures, we remain on track with our opex vs final determination KPI, which measures the variance between our latest formal forecast of operating costs and Ofwat's final determination for AMP4. The recent rapid reduction in RPI has led to a lower than anticipated baseline final determination for 2008/09, but we have delivered an outcome this year that is in line with the absolute levels of expenditure previously targeted.

As we proceed into the final year of AMP4, the recent rapid reduction in RPI is likely to have a significant negative impact on the anticipated baseline final determination. We have, however, accelerated some of our improvement plans and expect to incur around £20 million of restructuring costs in 2009/10 which will deliver around £5 million of additional operating cost savings in 2009/10 beyond our previous plans and further cost efficiencies in AMP5. We remain focused on the successful delivery of our plans and we continue our efforts to identify and pursue additional opportunities in this lower inflation environment.

Capital process quality

Our capital process quality KPI is now in place and is working well. We achieved zero defects on handover per £100,000 spend, a reduction on last year's 0.03.

The capital process quality measure assesses our delivery of high quality services.

Cost to serve a property

Our KPI cost to serve per property measures the total cost (including operating costs, depreciation, infrastructure renewals and third party costs) associated with serving a single property. During 2008/09, we continued to maintain a cost base that supports our position of having some of the lowest bills in the industry.

Managing trade debt

We continue to manage our trade debt as efficiently as possible. Despite the downturn in the economy, our debtor days performance improved from 37.4 days in 2007/08 to 33.1 days. This improvement is a result of enhancements made to our debt management process, including more customers signing up to our water direct scheme to make payments directly from their benefits and an increase in the range and volume of outbound message campaigns encouraging customers in debt to contact us and agree payment plans.

Despite our improved debtor days performance overall, the challenging economic conditions have seen an increase in customer insolvencies and greater difficulty in collecting debt over one year old. As a result, we increased our bad debt charge and it now represents around 2.3% of turnover, up from around 1.9% last year.

KSI: Promoting an effective regulatory regime

Performance against our regulatory obligations

In 2008/09, we improved our performance against our regulatory obligations KPI, reducing the number of areas with significant issues to 10%. This was a significant improvement on the 15% we achieved in 2007/08.

Promoting an effective regulatory regime

We have played an active part in developments in the regulatory framework and been active in supporting and exploring the development of competition in the industry. We have engaged with the Cave Review on Competition and Innovation and the Walker Review of Charges. In particular, we believe a competition model based on water trading could work and we are currently looking at how this might be developed in order to help address the balance of water supply and demand on a national basis. This may help to reduce the need for additional infrastructure in some parts of the country where water supplies are low and therefore keep costs as low as possible for all customers.

This was one of the recommendations of the Cave Review. Cave also recommends the separation of retail activity and retail competition for non households. We believe that retail competition is only likely to bring substantial benefits if it is coupled with competition for water resources and should not therefore be pursued as an end in itself.

We have also spoken at events and responded to consultation documents on a wide range of regulatory and competition issues with the aim of encouraging the development of the framework to meet the new challenges facing the industry.

We continue to engage with the Environment Agency to explore the trade offs between the environmental benefits of improving river water quality and the increased energy use this improvement involves. Our aim is to safeguard the needs of the environment and address climate change while keeping our bills as low as possible for our customers.

Maintaining investor confidence

The interests of our customers and our investors are inextricably linked and we need access to finance to maintain and improve our services to customers, and lower financing costs mean lower bills. In the current economic environment, both customers and investors are placing increasing value on stability.

As we look forward, the continuing large capital investment programme will drive further borrowing requirements, with our Final Business Plan anticipating a borrowing requirement of around £200 million a year on average over AMP5. The future visibility of returns and cash flow are important in sustaining investor confidence in Severn Trent Water and the wider water sector. A key element in this is the setting of an appropriate cost of capital which ensures that water remains sufficiently attractive over the long term to both debt and equity investors to secure financing for our planned investment programme. Our Final Business Plan assumes a cost of capital of 5.0% real, post tax, consistent with maintaining an appropriate credit rating to allow the company to raise the funds it requires to finance future investment at a reasonable rate and deliver an appropriate return to equity investors. The component parts of the assumed cost of capital are: real post tax cost of equity of 7.7% (AMP4 7.7%), real post tax cost of debt of 3.3% (AMP4 3.0%) and 60% gearing (AMP4 55%).

The successful execution of our plans in the current AMP4 period, and the basis of our PR09 Final Business Plan submission to Ofwat underpin our ability to:

- deliver a sustainable and progressive dividend to our equity investors, and
- maintain an appropriate financial structure, including sustaining a strong investment grade credit rating, which can absorb the impact of business cycle changes and enable the funding of our long term investment plan.

Focus on great people

KSI: Having the right skills to deliver

We are committed to continuously improving the engagement, skills and working environment of our people. Below are examples of how our work programmes and KPIs contribute to improvements in this area.

Increasing employee motivation

In 2008/09, we achieved our stretching KPI employee motivation target of 83%, improving on last year's 77%. We measure this KPI through an annual employee survey and three mini surveys to gain a clear ongoing measure of staff morale and motivation.

This excellent performance has been achieved in a year of continued emphasis on the key enablers that drive our commitment to highest standards, lowest possible charges and great people. These enablers are upskilling, simple processes that work, an improved workplace, improved technology that works, and being paid for doing the right things for our customers.

Developing the skills of our people

We have focused on establishing one way of working for all our people and giving everyone the encouragement, tools and techniques to work that way. To this end, we have been increasing the skills of our managers and of the workforce.

We have formal succession and talent management reviews throughout the year. This process reaches across the organisation so that we can identify and develop talent to help people achieve their potential.

We are continuously investing in ways to improve the skills of our people, working environments and communication. We are, for example, enhancing our internal communication programme so that employees can get easier access to the information they need.

Improving our management skills

In 2008, we launched the Line Manager Journey to clarify roles and equip managers with the right skills, tools and techniques to be able to get the best out of their teams. From the Chief Executive to the most junior manager, all our managers now have one common process of managing performance.

We have launched a leadership model and rolled out a behavioural model for all employees. It is part of our commitment to develop a modern workplace, where people treat each other in a supportive, adult to adult way and share and develop improvement plans to achieve both business and personal goals.



Coventry is undergoing a £9.4 billion transformation and Severn Trent is a key part of our exciting future.

Councillor Gary Ridley,
cabinet member for
city development

Creating a diverse workforce

We are committed to improving the diversity of our workforce. Building on the work we have already done, in 2008 we set up a Diversity Working Group and developed an action plan in line with our stated belief that a diverse and inclusive culture is a key factor to a successful business. During the year we commissioned some benchmarking work to better understand our diversity performance and identify areas for improvement. Our key diversity statistics are available on our website and in our Corporate Responsibility Summary Report.

Simple processes that work

We have introduced lean management practices across our water, waste water and other business areas. As a result, our people – in water treatment works, sewage depots and call centres, have been able to connect what they do on a day by day basis to our overall strategic direction and KPIs. Critically, they have been given the encouragement, training and tools to start making their own improvements with the support of their managers. This in turn has resulted in cost reductions, improvements in customer service and higher engagement levels among our workforce.

We are identifying and fixing issues faster, more efficiently and more fundamentally, getting more things right first time, eliminating waste from our processes. As a result, our performance is improving on interruptions to supply, leakage, reducing energy use and more. To date, around 1,500 of our 5,624 people have been introduced to the tools and techniques and are now using them in their day to day work. Building on our successes this year, we will continue to invest in our safer, better, faster ways of working throughout the business. We are developing lean change champions and an academy of experts to help ensure this way of working continues to be our way of working. Alongside our training in process improvement we continue to invest in developing the technical and professional qualifications of our people through apprenticeships and continuous learning.

An improved workplace

We are investing in our workplace to reflect the quality of the way we work, creating great environments for great people.

Our property portfolio includes 7,000 sites across the 21,000 km² Severn Trent Water region. As reported last year, we have been working to a strategy of creating a portfolio of workspace for the business at the right cost, the right quality, of the right amount in the right location and held for the right period of time.

This includes the development of the new Severn Trent Centre in Coventry, which is progressing well, with a number of key milestones being achieved in 2008/09. Severn Trent Centre is part of the programme of workplace improvements to set new standards for our working environments and we plan to implement them across all of our remaining sites.

Improving health and safety standards

Creating a safe place to work is at the heart of our commitment to creating a great place to work. We continually focus on improving safety, quality and standards across the organisation.

Reducing lost time incidents

In 2008/09, we improved our performance on our health and safety KPI of lost time incidents per 100,000 hours by 30% – down to 0.43, compared with 0.61 in 2007/08. In achieving this significant improvement, we beat our target of 0.51.

Our RIDDOR (Reporting of Injuries, Diseases and Dangerous Occurrences (Regulations)) rate is 0.33 – a 39% improvement on our 2007/08 rate of 0.54.

Demonstrating safety improvement plans

Last year, we set out a 10 point strategy plan on safety, quality and standards. The plan covers setting a standard for personal protective equipment; improving our incident investigation; developing safety hazard workshops for the senior managers; developing an audit programme based on hazard and risk priority work; working to improve the performance of our contractors; engaging our employee representatives in safety committees and having our directors carry out safety and environmental tours. This year, we have been cascading the plan down through the organisation, with line managers producing their own safety improvement plans reflecting the 10 points.

Our Safe and Unsafe Acts (SUSA) safe behavioural management system is very much an active part of the way we build behavioural safety into our everyday business. This year we put additional effort into ensuring management teams achieved their target number of SUSA discussions.

In 2008/09, we had four British Safety Council audits at a variety of facilities. One site received five stars, the highest grade, and three received four stars.

We also entered 19 of our business units for Royal Society for the Prevention of Accidents safety awards. 17 business units received a range of awards, with Severn Trent overall, achieving a Gold Award for safety improvements.

We are committed to improving the long term physical quality, security and safety of the assets as well as the safety of our people. This is why we focus on sustainable improvements not only in our health and safety culture but also in the quality of our assets through our extensive safety review and engineering modifications and refurbishments.

Comprehensive site safety review

We completed a comprehensive health and safety process review of the engineering and operational assets at all our water and waste water sites in 2007/08. In total we surveyed 6,646 sites. During 2008/09, we carried out a wide range of improvements prioritising work based on the level of risk.

Our engineering standards organisation continues to look at asset safety on more unified standards for the engineering, safety and design of our future assets. A substantial proportion of our new design templates for AMP5 contracts are now in place.

Safety for suppliers

During the year, we held five supply chain forums for health and safety and quality management. We ran three for contractor health and safety, one at the quality working day for suppliers and one for excavation contractors on the risks of high voltage cable strikes. Over 100 supplier companies have attended one or more of these forums across the year.

We closely monitor the safety and health performance of our contractors. Overall, our contractors have a RIDDOR reportable incident rate of 0.38 events per 100,000 hours worked. We also actively audit how our contractors manage health and safety risks on their sites. Drawing on the data gathered from these monitoring programmes, we work with our contractors to identify improvement initiatives.

Working as one with our suppliers

We are investing in ever stronger relationships with our contractors and suppliers. We aim to manage the whole supply chain responsibly, from suppliers through to customers.

We make sure that we are working with responsible suppliers, based on their environmental, health and safety, ethics and human rights track record. We are also looking at identifying areas where our suppliers will be able to help us achieve some of our strategic objectives, such as reducing our carbon footprint.

We appointed our AMP5 contractors in March 2009, well ahead of others in the industry. This is a key step in our One Supply Chain approach, where everyone involved in the delivery of our AMP5 programme, will work together as one team.

It is a continuation of our work in 2007/08 to smooth the so called investment rollercoaster, where investment rises steeply in years 2, 3 and 4 of the AMP cycle before falling off sharply in year 5. Smoothing this out so that there is a steady amount of investment throughout the five years is beneficial for our contractors, because it allows them to plan their resources more easily and cost effectively, and for us, because we can gain from efficiencies.

In keeping with our aim to have fewer, deeper and more mutually beneficial relationships, we are dealing with fewer contractors for AMP5, 11 rather than 22 for AMP4.

Our 11 AMP5 contractors are Balfour Beatty, Barhale Construction, Biwater Treatment Ltd, CostainMWH, Enterprise, Interserve, LoRImtech, May Gurney, Mott MacDonald Bentley, Morgan Est and North Midland Construction.

Our award winning two year supply chain management programme with Nottingham Trent University draws participants from throughout our business and our contractors and suppliers. The programme allows our employees, contractors and suppliers to work together on areas of joint interest, in a positive environment to deliver business benefits. Key outputs from this programme have already been implemented in the company this year or are part of our strategy around AMP5.

Improved technology that works

In 2008/09, we aligned our IT investment to our eight KSIs and focused it on helping us provide our day to day business services more efficiently and effectively. We also reorganised the IT team around service delivery, development and strategy on the supply side and around our core business groups on the demand side.

The key objective is to ensure that IT supports our business as effectively as possible. To this end, we are investing in technology to improve key processes that enable us to work better together and improve our performance in water, waste water, customer relations and our finance, HR and procurement functions. A key element of this investment is our SAP programme and the process improvement it will deliver. We have completed the detailed design

for this programme and have begun the implementation phase. We are also looking at how to implement new technology to support a far more flexible and mobile workforce and set of working practices, so that our people can work as effectively as possible from wherever they need to be.

Looking ahead

We intend to continue to deliver on our promises and to build on the wide ranging performance improvements we have achieved in 2008/09 against our 20 KPIs and in line with our eight KSIs.

We believe we have submitted a high quality Final Business Plan for PR09 that balances the interests of all stakeholders: customers, employees, suppliers, economic and environmental regulators, and investors. In the coming months, we look forward to continuing our preparations for AMP5, including working towards final determination of our plan.

We intend to continue working closely with everyone concerned on regulatory reforms, notably competition and the adoption of private sewers. We welcome these changes and will make sure we are in the best position for our customers and our shareholders.

In these challenging economic times where quality, prudence and long term thinking are at a premium, we will look to apply our robust funding strategy in order to continue securing the finance we need to fund investment over the next 25 years and beyond.

Above all, we intend to make sure we are constantly looking at the long term stewardship of the business to ensure we continuously improve standards, keep on lowering costs and further develop our great people in the years ahead.

Tony Wray
Chief Executive
Severn Trent Water

Financial performance

The past year has seen an unprecedented period of disruption to financial markets, the banking sector and other financial institutions. These events have combined to create the so called 'credit crunch' and a wider economic recession. The speed of these events has also presented its own challenge and we have witnessed first, a rapid rise in retail price inflation followed by a rapid decline with annual RPI inflation at a negative 0.4% and declining by the March 2009 year end. The group reacted quickly to events, meeting the challenges, sustaining a sound financial performance throughout the year and ending it in a strong liquidity position. When it became apparent that credit was becoming more difficult to obtain, with some traditional funding sources and markets effectively closed, the board took the decision to 'pre fund' a major part of our investment and cash needs for up to the next two years. Following this decision, we took a number of steps including successfully issuing new bonds to the sterling market in January, raising £400 million repayable in January 2018. These decisions have, of course, a short term economic cost as we are now holding cash, deposited on lower rates than our current borrowing costs. However, it is the view of the board that, despite the cost, in these unprecedented times, we should secure the funding required, maintaining our services to customers and sustaining our investment programme.

The board continues to watch carefully the evolution of both the credit markets and the general economic situation so we may seek out the best options to manage the business in these volatile economic times but the group finished the year ended 31 March 2009 in a strong liquidity position.

The financial statements on pages 23 to 48 report both the company and consolidated results of the Severn Trent Water Limited group of companies. The group report provides a complete view of activities, as certain financing arrangements for the benefit of the group are facilitated through the company's subsidiaries. This financial review therefore refers to the consolidated results of the Severn Trent Water Limited group.

Results

The group's turnover increased by 4.7% in 2008/09, to £1,324.9 million. Sales prices increased by 5.07% (including inflation) from 1 April 2008, with a decline in commercial consumption reducing revenues by around £20 million. The rapid rise in the first half year and then fall in retail price inflation (RPI) has presented a number of challenges. The company, which operates under an RPI model as regulated by Ofwat, faced rising costs in the first half year which we worked hard to contain, while seeking to obtain value from the falling rates in the latter half. In the company's business, lead times on procured items, particularly on the capital investment programme, are longer and this challenge has been difficult.

Operating profit before exceptional items (underlying operating profit) increased by 3.8% on the previous year to £488.3 million. Beyond the increase in turnover, a number of factors impacted underlying operating profit, principally: an increase in energy and commodity costs of £10.4 million, an increase in the bad debt charge of £6.6 million, increase in depreciation charges of £15.6 million and other increases in our cost base, net of efficiencies, of £4.2 million.

There was a net exceptional charge of £19.4 million (2008: £63.3 million) comprising:

- restructuring costs of £13.7 million arising from the programme to restructure and realign the business;
- a net credit of £1.5 million arising from the flooding incidents that affected the company's water and sewerage networks during the summer of 2007; and
- a charge of £7.2 million arising from the settlement and closure of the regulatory issues that arose in previous years. This includes a Court imposed fine of £2.0 million and costs of £0.2 million from two offences relating to leakage data supplied to Ofwat in 2001 and 2002 and a provision of £5.0 million for additional contributions to the Severn Trent Charitable Trust as agreed with Ofwat.

The group's net interest payable was £187.3 million (2008: £166.8 million). Finance costs on pension obligations increased by £13.3 million as a result of a higher discount rate, whilst the expected return on assets was lower because the value of investments declined.

The total tax charge for the year was £117.6 million (2008: £43.3 million) of which current tax represented a charge of £65.2 million (2008: £64.8 million) and deferred tax a charge of £52.4 million (2008: £21.5 million credit). The current tax charge before adjustments in respect of prior years represents 26.3% (2008: 30.3%) of the group's profits before tax.

Profit for the financial year was £164.0 million (2008: £197.0 million).

Capital structure

The group is funded using a mixture of equity and debt (including fixed rate, index linked and floating rate). The group continues to believe that the appropriate long term gearing level of the company is 60% net debt:RCV. However, given the current and ongoing uncertainties in the credit markets, the board believes it is prudent in the near term to retain as much liquidity and flexibility as possible. As such the board does not expect to pursue the target gearing level of 60% net debt:RCV until the credit markets improve.

	2009 £m	2008 £m
Cash and short term deposits	(160.0)	(448.7)
Bank overdrafts	0.2	383.0
Bank loans	547.8	620.5
Other loans	2,964.7	2,540.3
Obligations under finance leases	343.9	385.0
Net debt	3,696.6	3,480.1
Equity shareholders' funds	1,175.8	1,243.0
Total capital	4,872.4	4,723.1

Net debt at 31 March 2009 was £3,696.6 million (2008: £3,480.1 million). Of the net debt 64% (2008: 60%) was represented by fixed interest borrowings and 91% (2008: 90%) was represented by amounts payable after five years.

Cash flows

Operating activities generated a net cash inflow of £767.9 million (2008: £676.3million). An outflow of £161.4 million (2008: £139.8 million) was utilised in the servicing of financing

arrangements. Net investing activities used £588.8 million (2008: £543.9 million) which mainly included the continuing capital expenditure to meet the company's obligations under the AMP4 capital programme. Dividend outflows amounted to £154.7 million (2008: £263.1 million).

Treasury management

The Severn Trent Water group's treasury affairs are managed centrally as part of the Severn Trent Plc group and in accordance with its Treasury Procedures Manual and Policy Statement. The treasury operation's primary role is to manage liquidity, funding, investment and the group's financial risk, including risk from volatility in interest and, to a lesser extent, currency rates and counterparty credit risk. Its activities are subject to a set of controls commensurate with the magnitude of the borrowings and investments under its management. The board determines matters of treasury policy and its approval is required for certain treasury transactions.

The group uses financial derivatives solely for the purposes of managing risk associated with financing its normal business activities. The group does not hold or issue derivative financial instruments for financial trading purposes. The group uses a limited number of currency swaps and interest rate swaps to redenominate external borrowings into the currencies and interest rate coupon required for group purposes. The group's policy for the management of interest rate risk is to have a balanced portfolio of debt with a mix of term and interest rate structures that diversifies its risk and is appropriate to the long life of its asset base. The details are periodically reviewed to respond to changing market and regulatory conditions and with regard to regulatory pronouncements. The group's business does not involve significant exposure to foreign exchange transactions.

The group renewed for five years a £200 million bank facility in July 2008. The group has £160 million in cash and cash equivalent, following the issue of a £400 million 6% nine year sterling bond in January 2009. The group also has an undrawn £500 million committed bank facility that matures in 2013 and post year end has signed a further European Investment Bank (EIB) facility of £150 million, which is available for the group to draw down over the next two years. The group is funded for its investment and cash flow needs for up to the next two years.

Cash is invested in deposits with highly rated (A+) banks and liquidity funds (AAA) and the list of counterparties is regularly reviewed and reported to the board. The group's 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 2009, interest rates for some 64% of the group's net debt of £3,696.6 million were fixed.

The long term credit ratings of Severn Trent Water Limited are:

Long term ratings	Severn Trent Water
Moody's*	A2
Standard & Poor's**	A

* On 20 May 2009, Moody's confirmed the ratings for the group and announced that they have placed the ratings under review for possible downgrade.

** On 23 December 2008, Standard and Poor's confirmed the ratings for the group, and announced that they were subject to a 'negative outlook'.

Further details of the group's borrowings, investments and financial instruments are contained in note 12 to the financial statements.

Critical accounting policies

In the process of applying the group's accounting policies, the directors are required to make certain judgments, estimates and assumptions that they believe are reasonable based on the information available. The more significant judgments and key assumptions and sources of estimation uncertainty are summarised below:

Depreciation and carrying amounts of tangible fixed assets

Calculating the depreciation charge and hence the carrying value for tangible fixed assets 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 1 d to the financial statements.

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 17 to the financial statements.

Tax provisions

Assessing the outcome of uncertain tax positions requires judgments to be made regarding the result of negotiations with, and enquiries from, tax authorities. The assessments made are based on advice from independent tax advisers and the status of ongoing discussions with the relevant tax authorities.

Provisions for liabilities and charges

Assessing the financial outcome of uncertain commercial and legal positions requires judgments 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.

Investment

The financial year 2008/09 was the fourth year of the AMP4 period (covering 2005-10). During the financial year, the company invested £635.3 million (before contributions to infrastructure assets) in fixed assets. Adjusting for minor timing differences and modifications to the AMP4 capital programme (notified to Ofwat through the change control process) we continue to be in line to achieve this programme with capital expenditure, net of grants, contributions and other income (UK GAAP) of £2.6 billion. Details of the investment programme are set out in the business review.

Directors' report

The directors present their report, together with the audited financial statements for the year ended 31 March 2009.

Principal activities

The company is a wholly owned subsidiary of Severn Trent Plc.

The principal activities of the company and its subsidiary undertakings are the supply of water and the treatment and disposal of sewage in the UK. There have not been any significant changes to the company's principal activities in the year under review. The directors are not aware, at the date of this report, of any likely major changes in the company's activities in the next year.

Business review

The company is required to set out in this report a fair review of the business of the company during the financial year ended 31 March 2009, the position of the company at the end of the financial year and a description of the principal risks and uncertainties facing the company (known as a 'business review').

The information that fulfils the requirements of the business review can be found in the following sections of the operating and financial review:

Review of results	Page 4–12, 14–15
Operational performance	Page 6–13
Financial performance	Page 14–15
KPIs	Page 4–12
Severn Trent Water final business plan 2010/15	Page 3

Principal risks and uncertainties are detailed on page 21 of the Governance and risk assurance report.

Dividends and reserves

The company's dividend policy is to declare dividends which are consistent with the company's regulatory obligations. The amount declared is expected to vary each year further to consideration of these obligations. The ordinary dividend declared by the company in 2009 amounted to £154.7 million (2008: £263.1 million).

Transfers to reserves are set out in note 15 to the financial statements.

Directors

The directors of the company who served during the year and up to the date of this report are set out below:

Tony Ballance	
Bernard Bulkin*	
Richard Davey*	
Sir John Egan*	
Martin Houston*	Retired 23 January 2009
Martin Kane	
Martin Lamb*	
Michael McKeon	
Baroness Noakes*	
Andy Smith	
Tony Wray	

*non-executive director

Gordon Fryett was appointed as a non-executive director with effect from 1 July 2009

Directors' interests

All of the directors at the year end are also directors of Severn Trent Plc. In accordance with the UKLA Listing Rule 9.8.6, their interests in the share capital of Severn Trent Plc are disclosed in the Annual Report and Accounts of that company for the year ended 31 March 2009.

None of the directors retain any notifiable interest in the shares of the company or any other subsidiaries as at 31 March 2009.

Directors' remuneration and annual bonus plan

Remuneration for executive directors comprises the following elements:

- base salary and benefits
- annual bonus plan
- long term incentive plan
- pension plan

As all directors are also directors of Severn Trent Plc, details of their emoluments can be found in the Annual Report and Accounts of Severn Trent Plc.

As outlined in the Severn Trent Plc Report and Accounts, the non-executive Chairman, Sir John Egan, and non-executive directors, do not participate in the company's incentive arrangements, i.e. annual bonus or share schemes.

Base salaries

Base salaries are reviewed annually for each director and are determined with regard to the market median for similar roles in publicly quoted utility companies of a comparable size and so far as practicable, undertaking similar activities. Salaries are set with reference to individual performance, experience and contribution together with developments in the relevant employment market and internal relativities.

In addition directors receive a benefits package which includes car allowance, membership of company pension scheme or cash allowance in lieu, private medical insurance, life assurance and incapacity benefits scheme.

Annual bonus plan

The directors' bonus plan focuses on the achievement of specific strategic goals that are closely linked to the company's KPIs and which are intended to drive the creation of operational efficiencies. The bonus outturn operates on a balanced scorecard of measures, based on the 20 KPIs which include operational performance, leakage and customer service. The plan attributes a points score to each KPI and bonus entitlement is determined by reference to the aggregate number of points achieved across all the KPIs. Zero bonus is payable if performance against each KPI is less than or equal to the 2007/08 outturn. Bonus targets were set and measured for the period 1 April 2008 to 31 March 2009.

All of the targets 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. As such, directors' remuneration is clearly linked to the standards of performance in connection with the carrying out of functions of a relevant undertaker.

Consistent with the latest developments in institutional guidelines, the rules of the annual bonus plan now provide that the committee may reclaim 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.

The annual bonus opportunity for the executive directors was 120% of salary. For the achievement of target performance, 60% of salary would be earned.

The table below shows the extent to which the KPI targets were achieved during 2008/09:

KPI	Measure	07/08 outturn	08/09 outturn	Points scored
1	Lost time incidents per 100,000 hours worked	0.61	0.43	180
2	Employee motivation %	77%	83%	100
3	Water quality (test failure rate) ppm	240.1	200.4	100
4	Customer written complaints per 1,000 properties	10.90	6.44	145
5	First time call resolution for billing %	85%	88%	116
6	Unplanned interruptions > 6 hours per 1,000 properties	21.86	7.29	174
7	Properties at risk of low pressure per 1,000 properties	0.46	1.21	0
8	First time job resolution %	85%	96%	100
9	Non performance against regulatory obligations %	15%	10%	100
10	Capex (Gross) vs final determination %	1.7%	5.0%	100
11	Capital process quality (no of defects per £100k)	0.03	0.00	100
12	Debtor days	37.4	33.1	51
13	Opex vs final determination (UK GAAP) £m	480.9	500.9	100
14	Cost to serve per property - £	236.82	236.53	0
15	Pollution incidents (cat 1, 2 and 3) per 1,000 properties	0.11	0.08	273
16	Sewer flooding incidents - other causes per 1,000 properties	0.21	0.17	64
17	Sewage treatment works - breach of consents %	0.0%	0.0%	100
18	Security of supply	95	98	145
19	Net energy use - kWh/MI	608	622	0
20	Leakage MI/d	491	492	172
Total KPI points achieved				2,120

The score of 2,120 points delivers a bonus payment of 61.8% of the bonus maximum. The actual bonus payments awarded to each director are detailed below:

Director	Value of bonus award £
Tony Ballance	124,589
Martin Kane	137,196
Michael McKeon	315,180
Andy Smith	185,400
Tony Wray	333,720

50% of the above bonus awards is deferred into shares to be held for three years following payment and subject to continued employment unless the Severn Trent Plc Remuneration Committee determines it is appropriate to release the shares in 'good leaver' cases. In the case of below board level executives, one third of the bonus award is deferred into shares.

Details of bonus awards for the year ended 31 March 2009 are shown in the table of directors' emoluments in the Severn Trent Plc Annual Report and Accounts.

Share Matching Plan

At the 2009 Annual General Meeting of Severn Trent Plc, shareholder approval is being sought to introduce a Share Matching Plan. The plan will allow executive directors to receive matching share awards over those shares which have been acquired under the deferred share component of the annual bonus plan as described above. Further details of the proposed Share Matching Plan can be found in the Severn Trent Plc Annual Report and Accounts.

Long Term Incentive Plan

Directors may also participate in the Severn Trent Plc Long Term Incentive Plan (LTIP). Under this plan conditional awards of performance shares are made to directors up to an annual maximum limit. This seeks to reward the creation of long term value and align the company's incentive arrangements with the interests of shareholders. Further details are contained in the Severn Trent Plc Annual Report and Accounts.

Share Incentive Plan

In 2007 the company relaunched an all employee Share Incentive Plan which included a performance condition based on achievement of 18 of the KPIs. Employees of Severn Trent Plc and Severn Trent Water Limited participate in the plan. For the year 2008/09 the performance condition is based on all 20 KPIs and awards of shares to the value of £463 will be made to all eligible employees.

Directors' and officers' indemnities

Directors and officers are 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.

Policy on the payment of creditors

The company either uses its own standard terms and conditions entitled 'General Conditions of Contract relating to the supply of Goods/Services or the Execution of Work' (copies are available from the Purchasing Department, Severn Trent Water Limited, 2297 Coventry Road, Birmingham B26 3PU) or nationally agreed terms and conditions of contract such as ICE 6th Edition for Civil Engineering Works and G90 terms and conditions for Mechanical and Electrical Works.

Terms of payment are stated on each purchase order issued by the company. Suppliers are able to negotiate their own payment terms which can differ from these, as part of the tender process. Trade creditors at year end reflected 26 days purchases (2008: 30 days).

Research and development

Expenditure on research and development was £3.8 million including £0.53 million spent on fixed assets (2008: £4.3 million including £0.7 million on fixed assets). Details of the research and development activity undertaken by the company during the year are set out in the operating and financial review on pages 6 to 15.

Employees

The average number of employees during the year was 5,624 (2008: 5,578).

Regulation: 'Ring fencing'

In accordance with the requirements of the Water Services Regulatory Authority, the board confirmed that, as at 31 March 2009, it had available to it sufficient rights and assets, not including financial resources, which would enable a special administrator to manage the affairs, business and property of the company in order that the purposes of a special administration order could be achieved if such an order were made.

Regulation: 'Cross directorships'

It is the policy of the company that directors and employees of the company may be directors of related companies when this is in the best interests of the company, and where appropriate arrangements are in place to avoid conflicts of interest.

Conflict of interests

The Companies Act 2006 (the Act) rules on directors' conflicts came into force on 1 October 2008. These rules provide four statutory duties:

- a duty not to accept benefits from third parties;
- a duty to disclose any interest in a proposed transaction or arrangement with the company and a separate and independent duty to disclose any interest in an existing transaction or arrangement with the company (transactional conflicts); and
- a duty to avoid conflicts of interest (situational conflicts) unless authorised.

The Act allows board authorisation of situational conflicts where the directors have the relevant powers.

In September 2008, the directors of Severn Trent Water Limited were requested to complete a questionnaire to determine whether any actual or potential conflicts needed authorisation. The board fully reviewed the completed questionnaires and noted that no conflicts arose.

For any actual or potential conflicts that arise post 1 October 2008, 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 Severn Trent Plc 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 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.

Going Concern

The company 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 company and the group are well placed to manage their business risks despite the current uncertain economic outlook. The company and the group are funded for their investment and cash flow needs for up to the next two years.

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, we continue to adopt the going concern basis in preparing the annual report and accounts.

Auditors

In accordance with Section 386 of the Companies Act 1985, the company has elected to dispense with the obligation to appoint auditors annually. Deloitte LLP will, therefore, remain as auditors until further notice.

In the case of each of the persons who are directors of the company at the date when this report was approved:

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

Relevant audit information means information needed by the company's auditors in connection with preparing their report.

This confirmation is given and should be interpreted with the provisions of section 234ZA of the Companies Act 1985.

By order of the board



Fiona Smith
General Counsel and Company Secretary
28 May 2009

Governance and risk assurance

Severn Trent Governance

Severn Trent Plc is the ultimate holding company of Severn Trent Water Limited. Since March 2007, as part of the strategy of focusing on water, the boards of directors of Severn Trent Plc and Severn Trent Water Limited have been identical.

Severn Trent Plc and Severn Trent Water Limited 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, and are assisted through the management of separate agendas, meetings and minutes by the Company Secretariat and are advised in their meetings by the Company Secretary where appropriate.

The relationships between Severn Trent Water Limited, the regulated entity, and our non regulated companies such as Severn Trent Services are monitored and controlled to ensure that we comply with our Ofwat obligations on arm's length transactions.

Throughout the year ended 31 March 2009, Severn Trent Plc was compliant in its application of the June 2006 Financial Reporting Council Combined Code, with the exception of Code provision A.3.2 which requires that at least half the board, excluding the chairman, should comprise non-executive directors determined by the board to be independent. Martin Houston retired from the board as an independent non-executive director on 23 January 2009 and the board announced its intention to commence the search for a suitable independent non-executive director to appoint to the board at that date. On 22 May 2009, the board announced the appointment of Gordon Freyett with effect from 1 July 2009.

The Severn Trent Plc board has established an effective committee structure to assist in the discharge of its responsibilities to the group. The terms of reference of the Audit, Remuneration and Nominations Committees comply with the provisions of the 2006 Combined Code and are available for inspection, together with the terms of reference of the Corporate Responsibility Committee and Executive Committee, on the Severn Trent Plc website (www.severntrent.com) or on written request from the Company Secretary at the address given on the back cover of this document.

In 2008, the board undertook a review of the Severn Trent Governance Framework. The purpose of the review was to ensure that:

- the framework accurately reflected the Severn Trent organisation and structure;
- the framework set out and reinforced Severn Trent's values and supported the group in working and behaving in the right way;
- the risk and assurance processes were a robust and integral part of the framework; and
- the framework reflected best governance practices.

The review completed in November 2008. At the request of the board, Company Secretariat has embarked on a plan to embed the framework throughout Severn Trent which is due to complete in March 2010.

Severn Trent Water Limited

Operating structure

Day to day operational priorities within Severn Trent Water are led by the Chief Executive and his executive management team, who together comprise the Executive Committee. During the year, the Executive Committee comprised the executive directors and senior executive managers responsible for key central and operational areas.

The Executive Committee oversees the development and execution of the Severn Trent strategy and has accountability for delivering business results.

The operational structure aligns the organisation with the processes that matter to customers and drives greater efficiency.

Internal control and risk management

The board has overall responsibility 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, compliance and risk management, at least annually in accordance with the requirements of the Combined Code and the guidance set out within it. The system of internal control is reviewed 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 board reviews risk management and the effectiveness of the system of internal control through the Severn Trent Plc Audit Committee. The board also keeps under review ways in which to enhance the control and audit arrangements in the group. The Audit Committee receives reports every six months from the Chief Executive on the significant risks 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. Any significant control weaknesses that have been identified as requiring remedy are also reported to the Audit Committee. The auditors also report on significant control issues to this committee. The Internal Audit department provides objective assurance and advice on risk management and control.

The board confirms that procedures providing an ongoing process for identifying, evaluating and managing the principal risks faced by the group have been in place for the year to 31 March 2009 and up to the date of the approval of the Annual Report.

Statement of directors' responsibilities

Key elements of the group's processes and procedures are:

- clearly defined and communicated strategic and business objectives;
- an organisation structure with clear lines of accountability and responsibility;
- performance management and succession planning systems;
- regular, structured reviews of business risk by senior management and the Executive Committee, including a self assessment of control effectiveness;
- a scheme of delegated authority; approval of plans, budgets and significant investments;
- robust business planning including the identification and implementation of relevant improvement plans;
- monthly reporting and monitoring of financial results, regulatory compliance and other operational performance indicators; and
- independent assurance provided by both internal and external auditors.

Principal risks and uncertainties

The board considers the principal risks and uncertainties affecting the business activities of the company to be those detailed below:

- external financial market factors could adversely impact on our financial position;
- compliance requirements, particularly changes in law or regulation in the types of business in which we operate, could have an adverse affect on our business and operations;
- the results of our operations depend on a number of factors including achieving an acceptable final determination from Ofwat for Severn Trent Water and our ability to achieve sustainable benefits through the Severn Trent Water change programme;
- the failure of our assets, processes or systems could affect our ability to carry out critical operations and could have a significant impact on the Health and Safety of our people or customers, or on our financial position and our reputation; and
- our ability to influence customer behaviour or to operate in an environmentally responsible way could affect our financial position and our reputation.

Statement of directors' responsibilities

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). The financial statements are required by law to give a true and fair view of the state of affairs of the company and of the group and of the profit or loss of the company and group for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent; and
- 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.

The directors are responsible for keeping proper accounting records that 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 1985. 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.

Independent auditors' report

to the members of Severn Trent Water Ltd

We have audited the group and company financial statements (the financial statements) of Severn Trent Water Limited for the year ended 31 March 2009 which comprise the group and company profit and loss accounts, the group and company balance sheets, the group cash flow statement, the group and company statements of total recognised gains and losses, the group and company reconciliations of movements in shareholders funds, and the related notes 1 to 20. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. 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 auditors' 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 auditors

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the directors' report is consistent with the financial statements. The information given in the directors' report includes that specific information presented in the chief executive's review and the performance reviews that are cross referred from the business review section of the directors' report.

In addition we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the other information contained in the Annual Report as described in the contents section, and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any further information outside the Annual Report.

Basis of audit opinion

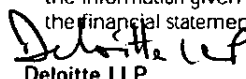
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's and company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the group's and the company's affairs as at 31 March 2009 and of the group's and company's profit for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the directors' report is consistent with the financial statements.



Deloitte LLP

Chartered Accountants and Registered Auditors
Birmingham, UK
28 May 2009



Profit and loss accounts

Year ended 31 March 2009

	Notes	Group		Company	
		2009 £m	2008 £m	2009 £m	2008 £m
Turnover		1,324.9	1,265.3	1,324.9	1,265.3
Operating costs before exceptional items	2	(840.0)	(798.8)	(855.8)	(814.1)
Exceptional operating costs	2	(19.4)	(63.3)	(19.4)	(63.3)
Total operating costs	2	(859.4)	(862.1)	(875.2)	(877.4)
Other income		3.4	3.9	3.4	3.9
Operating profit		468.9	407.1	453.1	391.8
Income from shares in other group undertakings		-	-	14.8	-
Net interest payable	4	(187.3)	(166.8)	(186.5)	(164.1)
Profit on ordinary activities before taxation		281.6	240.3	281.4	227.7
Taxation on profit on ordinary activities – current tax	5	(65.2)	(64.8)	(62.6)	(62.6)
– deferred tax	5	(52.4)	21.5	(52.4)	21.5
Taxation	5	(117.6)	(43.3)	(115.0)	(41.1)
Profit for the financial year	15	164.0	197.0	166.4	186.6

The results arise from continuing operations in both the current and preceding year.

Statements of total recognised gains and losses

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Profit for the financial year	164.0	197.0	166.4	186.6
Actuarial loss	(110.4)	(38.1)	(110.4)	(38.1)
Tax on actuarial loss	30.9	10.7	30.9	10.7
Adjustment in respect of tax rate change on deferred tax	-	0.8	-	0.8
Total recognised gains and losses for the financial year	84.5	170.4	86.9	160.0

Reconciliations of movements in shareholders' funds

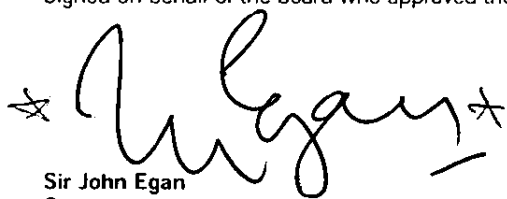
	Notes	Group		Company	
		2009 £m	2008 £m	2009 £m	2008 £m
Profit for the financial year		164.0	197.0	166.4	186.6
Dividends	6	(154.7)	(263.1)	(154.7)	(263.1)
Retained profit/(loss) for the financial year		9.3	(66.1)	11.7	(76.5)
Share based payments		3.0	3.1	3.0	3.1
Net actuarial loss		(79.5)	(27.4)	(79.5)	(27.4)
Adjustment in respect of tax rate change on deferred tax		-	0.8	-	0.8
Net reduction to shareholders' funds		(67.2)	(89.6)	(64.8)	(100.0)
Opening shareholders' funds		1,243.0	1,332.6	1,456.6	1,556.6
Closing shareholders' funds		1,175.8	1,243.0	1,391.8	1,456.6

Balance sheets

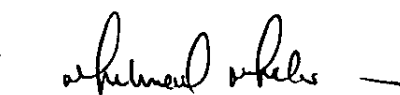
As at 31 March 2009

	Notes	Group		Company	
		2009 £m	2008 £m	2009 £m	2008 £m
Fixed assets					
Tangible assets	7	5,684.9	5,417.5	5,682.9	5,415.5
Investments	8	-	-	235.7	235.7
		5,684.9	5,417.5	5,918.6	5,651.2
Current assets					
Stocks		8.0	6.2	8.0	6.2
Debtors: amounts falling due within one year	9a	278.7	299.1	286.0	295.9
Debtors: amounts falling due after more than one year	9b	2.4	2.1	32.8	27.3
Short term deposits	12b	147.1	448.7	147.1	448.7
Cash at bank and in hand		12.9	-	11.7	-
		449.1	756.1	485.6	778.1
Creditors: amounts falling due within one year	10	(593.1)	(889.1)	(634.1)	(1,467.7)
Net current liabilities		(144.0)	(133.0)	(148.5)	(689.6)
Total assets less current liabilities		5,540.9	5,284.5	5,770.1	4,961.6
Creditors: amounts falling due after more than one year	11	(3,705.2)	(3,467.8)	(3,718.4)	(2,931.3)
Provisions for liabilities and charges	13	(509.1)	(493.4)	(509.1)	(493.4)
Net assets excluding pension deficit		1,326.6	1,323.3	1,542.6	1,536.9
Pension deficit	17	(150.8)	(80.3)	(150.8)	(80.3)
Net assets including pension deficit		1,175.8	1,243.0	1,391.8	1,456.6
Capital and reserves					
Called up share capital	14	1,000.0	1,000.0	1,000.0	1,000.0
Profit and loss account	15	175.8	243.0	391.8	456.6
Shareholders' funds		1,175.8	1,243.0	1,391.8	1,456.6

Signed on behalf of the board who approved the accounts on 28 May 2009.



Sir John Egan
Chairman



Michael McKeon
Finance Director

Group cash flow statement

Year ended 31 March 2009

	Notes	2009 £m	2009 £m	2008 £m	2008 £m
Net cash inflow from operating activities	19a		767.9		676.3
Returns on investments and servicing of finance					
Interest received		12.5		8.8	
Interest paid		(157.7)		(128.0)	
Interest element of finance lease rental payments		(16.2)		(20.6)	
			(161.4)		(139.8)
Taxation			(57.8)		(52.7)
Capital expenditure and financial investment					
Purchase of tangible fixed assets		(624.2)		(591.0)	
Grants and contributions received		29.4		44.2	
Sale of tangible fixed assets		6.0		2.9	
			(588.8)		(543.9)
Equity dividends paid			(154.7)		(263.1)
Net cash outflow before management of liquid resources and financing			(194.8)		(323.2)
Management of liquid resources			301.6		(446.8)
Net cash flow before financing			106.8		(770.0)
Financing					
Finance leases repaid		(41.1)		(23.1)	
Loans received		410.5		1,124.3	
Loans repaid		(78.8)		(102.5)	
Share based payments made on LTIP awards vesting in the period		(1.7)		-	
			288.9		998.7
Net increase in cash			395.7		228.7
Reconciliation of net cash flow to movement in net debt					
	Notes	2009 £m	2009 £m	2008 £m	2008 £m
Net increase in cash as above		382.8		228.7	
Cash flow from movement in net debt		(290.6)		(998.7)	
Cash flow from movement in liquid resources		(288.7)		446.8	
Change in net debt resulting from cash flows			(196.5)		(323.2)
Rolled up interest on debt			(20.0)		(37.0)
Increase in net debt			(216.5)		(360.2)
Opening net debt			(3,480.1)		(3,119.9)
Closing net debt	19b		(3,696.6)		(3,480.1)

Notes to the financial statements

Year ended 31 March 2009

1 Accounting policies

a) Accounting convention

The financial statements have been prepared on the going concern basis under the historical cost convention in accordance with applicable United Kingdom Accounting Standards and, except for the treatment of certain grants and contributions, comply with the requirements of the United Kingdom Companies Act 1985 (the Act). An explanation of this departure from the requirements of the Act is given in the policy on grants and contributions below.

b) Consolidation

The consolidated profit and loss account and balance sheet include the results of the company and its subsidiary undertakings listed in note 8 prepared for the year ended 31 March 2009. Intra group sales and profits are eliminated fully on consolidation.

The company has taken advantage of the exemption in FRS 1 'Cash Flow Statements' and has not presented a cash flow statement.

c) Turnover

Turnover represents income receivable from regulated water activities, excluding value added tax and trade discounts, in the ordinary course of business for services provided within the United Kingdom.

Income includes an estimation 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.

Turnover is not recognised in respect of unoccupied properties. Properties are classified as unoccupied when:

- The company is informed that a customer has left a property and it is not expected to be reoccupied immediately;
- New properties are connected but are not occupied; or
- Properties are disconnected following a customer's request.

Where properties are not classified as unoccupied but the identity of the customer is unknown, the properties are classified as 'The Occupier' premises. Income is only recognised for such premises when:

- Cash is received; or
- The identity of the occupier becomes known.

Where amounts invoiced are being recovered through charges on income, turnover is recognised in accordance with the policy set out above and provisions are charged to operating costs to reflect the company's assessment of the risk of non recoverability.

d) Tangible fixed assets and depreciation

Tangible fixed assets comprise:

i) Infrastructure assets

Infrastructure assets comprise a network of systems being: mains and sewers; impounding and pumped raw water storage reservoirs; dams; and sludge pipelines.

Expenditure on infrastructure assets relating to increases in capacity or enhancements of the network and on maintaining the operating capability of the network in accordance with the defined standards of service is treated as an addition and included at cost after deducting grants and contributions (see note 1f).

The depreciation charged for infrastructure assets is the estimated, anticipated level of annual expenditure required to maintain the operating capability of the network less the estimated, anticipated level of relevant annual grants and contributions, based on the company's independently certified asset management plan (see note 1f).

ii) Other assets

Other assets are included at cost less accumulated depreciation. Additions are included at cost.

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
Operational structures	40 - 80
Fixed plant	20 - 40
Vehicles, mobile plant and computers	2 - 15

Assets in the course of construction are not depreciated until commissioned.

e) 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 value of the minimum lease payments is 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.

f) Grants and contributions

Grants and contributions received in respect of non infrastructure assets are treated as deferred income and are recognised in the profit and loss account over the useful economic life of those assets.

In accordance with industry practice, grants and contributions relating to infrastructure assets have been deducted from the cost of fixed assets. This is not in accordance with Schedule 4 to the Act, which requires assets to be shown at their purchase price or production cost and hence grants and contributions to be presented as deferred income. This departure from the requirements of the Act is, in the opinion of the directors, necessary to give a true and fair view as, while a provision is made for depreciation of infrastructure assets, finite lives have not been determined for these assets, and therefore no basis exists on which to recognise grants and contributions as deferred income. The effect of this departure is that the cost of fixed assets is £550.3 million lower than it would otherwise have been (2008: £522.4 million).

Those grants and contributions relating to the maintenance of the operating capability of the infrastructure network are taken into account in determining the depreciation charged for infrastructure assets.

1 Accounting policies continued

g) Impairment of goodwill and fixed assets

Impairments of goodwill and fixed assets are calculated as the difference between the carrying value of the 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.

h) Investments

Investments held as fixed assets are stated at cost less amounts written off.

i) Stocks

Stocks are stated at cost less any provision necessary to account for any damage and obsolescence.

j) Insurance

Provision is made for claims notified and for claims incurred but which have not yet been notified, based on advice from the group's external insurance advisers.

k) Pension costs

The group and company operate both defined benefit and defined contribution schemes.

For defined benefit schemes the amounts charged to operating profit are the current service costs and gains and losses on settlements and curtailments. They are included as part of staff costs. Past service costs are recognised immediately in the profit and loss account if the benefits have vested. If the benefits have not vested immediately the costs are recognised over the period until vesting occurs. The interest costs and the expected return on assets is shown as a net amount of other finance costs or credits adjacent to interest. Actuarial gains and losses are recognised immediately in the statement of total recognised gains and losses.

Defined benefit schemes are funded, with the assets of the scheme held separately from those of the group, in separate trustee administered funds. Pension scheme assets are measured at fair value and liabilities are measured on an actuarial basis using the projected unit method and discounted at a rate equivalent to the current rate of return on a high quality corporate bond of equivalent currency and term to the scheme liabilities. The actuarial valuations are obtained at least triennially and are updated at each balance sheet date. The resulting defined benefit asset or liability, net of the related deferred tax, is presented separately after other net assets on the face of the balance sheet.

Costs of defined contribution pension schemes are charged to the profit and loss account in the period in which they fall due.

l) Research and development

Expenditure on tangible fixed assets relating to research and development projects is capitalised and written off over the expected useful life of those assets.

Other research and development expenditure is charged to the profit and loss account in the year in which it is incurred.

m) Current and deferred taxation

Current taxation is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred taxation is provided in respect of timing differences between the treatment of certain items for taxation and accounting purposes only to the extent that the group has an obligation to pay more tax in the future or a right to pay less tax in the future. Material deferred taxation balances arising are discounted by applying an appropriate risk free discount rate. For the purposes of discounting, the period over which accelerated capital allowances in respect of infrastructure assets reverse is determined by the estimated annual cost of maintaining the operating capability of the network, based on an allocation of the infrastructure renewals charge to existing and future infrastructure assets.

n) Goodwill

Goodwill represents the excess of the fair value of purchase consideration over the fair value of the net assets acquired.

Goodwill arising on acquisitions prior to 1 April 1998 remains eliminated against reserves.

o) Derivatives and other financial instruments

Debt instruments

The costs of debt instruments are charged to the profit and loss account over the term of the debt at a constant rate on the carrying amount.

Such costs include the cost of issue and any discount to face value arising on issue, or any premium arising on maturity.

Derivative financial instruments

Financial instruments, in particular, interest rate swaps and to a lesser extent currency swaps, are used to manage the financial risks arising from the business activities of the group and the financing of those activities. There is no trading activity in financial instruments. Financial instruments are accounted for as follows:

Interest rate swaps are used to hedge the group's exposure to movements in interest rates. The interest payable or receivable on such swaps is accrued in the same way as interest arising on deposits or borrowings. Interest rate swaps are not revalued to fair value.

Currency swaps are used to hedge the group's exposure to movements in foreign exchange rates. The interest payable or receivable on such swaps is accrued in the same way as interest arising on deposits or borrowings. Currency swaps are not revalued to fair value but are recognised in the balance sheet at the difference between the swap rate and the spot rate at the balance sheet date.

1 Accounting policies continued**Derivatives and other financial instruments continued**

The aggregate fair value at the balance sheet date of the hedging instruments described above are disclosed in note 12 to the financial statements.

p) Pre-contract costs

Pre-contract costs incurred are written off as an expense, until such time as award of the contract becomes virtually certain.

Deferred costs are amortised over the life of the contract.

q) Share based payments

The group operates a number of equity settled, share based compensation plans for employees utilising the shares of the

ultimate parent company. 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 Analysis of total operating costs and exceptional items

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Analysis of total operating costs				
Raw materials and consumables (including exceptional costs £0.3 million (2008: £6.4 million))	40.2	41.2	40.2	41.2
Staff costs (including exceptional costs £0.9 million (2008: £8.0 million))	212.8	207.8	212.8	207.8
Depreciation and other amounts written off tangible assets	338.0	322.4	338.0	322.4
Other operating costs	343.8	365.1	359.6	380.4
Own work capitalised	(75.4)	(74.4)	(75.4)	(74.4)
Total operating costs	859.4	862.1	875.2	877.4
Staff costs comprise:				
Wages and salaries	172.4	165.2	172.4	165.2
Social security costs	14.6	12.4	14.6	12.4
Pension costs (note 17)	25.8	30.2	25.8	30.2
Total staff costs	212.8	207.8	212.8	207.8
Depreciation and other amounts written off tangible assets comprise:				
Depreciation on owned assets: non infrastructure	197.4	182.0	197.4	182.0
Depreciation on owned assets: infrastructure	118.5	117.9	118.5	117.9
Depreciation on assets held under finance leases	22.1	22.5	22.1	22.5
	338.0	322.4	338.0	322.4
Other operating costs comprise:				
Power (including exceptional costs £nil million (2008: £0.2 million))	51.1	37.6	51.1	37.6
Rates	58.4	59.5	58.4	59.5
Service charges	30.0	28.6	30.0	28.6
Other operating costs (including exceptional costs £16.1 million (2008: £45.6 million))	73.4	113.9	92.7	113.9
Deferred income released	(3.3)	(2.8)	(3.3)	(2.8)
Hired and contracted services (including exceptional costs £2.1 million (2008: £1.9 million))	123.7	116.5	104.2	116.5
Hire of plant and machinery (including exceptional costs £nil million (2008: £1.2 million))	6.8	7.1	6.8	7.1
Other operating leases	2.6	2.2	18.6	17.5
Research and development expenditure	5.1	4.1	5.1	4.1
Profit on disposal of fixed assets	(4.0)	(1.6)	(4.0)	(1.6)
Total other operating costs	343.8	365.1	359.6	380.4

2 Analysis of total operating costs and exceptional items continued

Exceptional items

	2009 £m	2008 £m
Exceptional restructuring costs and termination of operations	(13.7)	(13.9)
Exceptional flood costs net of insurance recoveries	1.5	(13.6)
Exceptional fines and penalties	(7.2)	(35.8)
	(19.4)	(63.3)

A £13.7 million exceptional charge was incurred (2008: £13.9 million) arising from the programme to restructure and realign the business.

An exceptional credit of £1.5 million (2008: charge of £13.6 million) arose from the flooding incidents that affected the water and sewerage networks during the summer of 2007. This includes costs of £13.1 million less insurance recoveries of £14.6 million.

A charge of £7.2 million was incurred relating to the settlement of the regulatory issues that arose in previous years. This includes a court imposed fine of £2.0 million and costs of £0.2 million from offences relating to leakage data supplied to Ofwat in 2001 and 2002 and a charge of £5.0 million for additional contributions to the Severn Trent Charitable Trust as agreed with Ofwat.

An exceptional charge of £35.8 million arose in 2008 from Ofwat's proposal to fine the company in relation to the misreporting of customer service data and failing to meet Guaranteed Standards of Service.

Auditors' remuneration

During the year Deloitte LLP earned the following fees:

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Fees payable to the company's auditors for the audit of the company's annual accounts	0.2	0.2	0.4	0.2
Fees payable to the company's auditors and their associates for other services to the group:				
The audit of the company's subsidiaries pursuant to legislation	0.2	0.1	-	0.1
Total audit fees	0.4	0.3	0.4	0.3
Other services pursuant to legislation:				
Other services	-	0.1	-	0.1
Total non audit fees	-	0.1	-	0.1

Fees in respect of other services in 2008 related to a review of internal controls.

3 Information regarding directors and employees

Directors:

a) Directors' interests

All of the directors as at the end of the year are also directors of Severn Trent Plc, the ultimate parent undertaking, and their interests in the share capital of that company are disclosed in the Annual Report and Accounts of that company for the year ended 31 March 2009. Share options were granted and exercised in accordance with the Severn Trent Share Option Scheme and the Severn Trent Sharesave Scheme as appropriate.

The executive directors have further interests in Severn Trent Plc ordinary shares of 97¹/₁₉₉ each by virtue of having received contingent awards of shares under the Severn Trent Plc Long Term Incentive Plan (LTIP) on 19 June 2006, 18 July 2007 and 14 July 2008. 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. The performance criteria for the awards are based on Severn Trent Plc's Total Shareholder Return (TSR).

The individual interests, which represent the maximum aggregate number of shares to which each individual could become entitled, are disclosed in the Annual Report and Accounts of Severn Trent Plc for the year ended 31 March 2009.

3 Information regarding directors and employees continued**b) Emoluments**

	2009 £000	2008 £000
Aggregate emoluments (excluding pension contributions)	3,426.5	2,267.4

- i) Non cash benefits included in aggregate emoluments consist mainly of the provision of cars and health care insurance.
- ii) No emoluments were paid by the company to certain of the directors in respect of their services to the company. Their emoluments are paid by other companies within the Severn Trent group.
- iii) Retirement benefits are accruing to three directors (2008: three directors) under a defined benefit scheme.

c) Highest paid director

	2009 £000	2008 £000
Aggregate emoluments (excluding pension contributions)	921.3	620.5

The highest paid director in 2009 is the same as that in 2008.

The accrued pension at 31 March 2009 for the highest paid director was £15,949 (2008: £11,538). The pension entitlement is that which would be paid annually on retirement based on service to the end of the year. The highest paid director did not exercise any share options during the year. LTIP awards over 8,974 shares vested in respect of the highest paid director during the year.

d) Employees

	Group and company	
	2009 Number	2008 Number
Average number of employees during the year	5,624	5,578

4 Net interest payable

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Interest receivable and similar income	14.1	8.8	14.6	11.6
Finance income on defined benefit pension schemes	79.8	83.0	79.8	83.0
Interest receivable	93.9	91.8	94.4	94.6
Interest payable and similar charges on:				
Bank loans and overdrafts	(4.7)	(13.4)	(4.7)	(13.4)
Other loans	(178.7)	(153.0)	(38.2)	(43.7)
Finance leases	(16.1)	(20.6)	(16.1)	(20.5)
Amounts due to subsidiary undertaking	-	-	(140.2)	(109.5)
Interest cost on defined benefit pension schemes	(81.7)	(71.6)	(81.7)	(71.6)
Interest payable	(281.2)	(258.6)	(280.9)	(258.7)
	(187.3)	(166.8)	(186.5)	(164.1)

5 Taxation on profit on ordinary activities

a) Analysis of charge in the year

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Current tax				
UK corporation tax at 28% (2008: 30%)				
Current year	31.8	34.5	28.3	30.9
Adjustment in respect of prior years	(14.2)	(8.1)	(14.2)	(8.1)
Group relief payable at 28% (2008: 30%)				
Current year	42.3	38.2	43.2	39.6
Adjustment in respect of prior years	5.3	0.2	5.3	0.2
Total current tax	65.2	64.8	62.6	62.6
Deferred tax				
Origination and reversal of timing differences				
Current year	(23.8)	(4.3)	(23.8)	(4.3)
Adjustment in respect of prior year	8.4	(92.8)	8.4	(92.8)
Decrease in discount	40.4	64.1	40.4	64.1
Total deferred tax charge/(credit)	25.0	(33.0)	25.0	(33.0)
Deferred tax included in statement of recognised gains and losses	27.4	11.5	27.4	11.5
Deferred tax charge/(credit) included in profit and loss account	52.4	(21.5)	52.4	(21.5)
Total tax charge	117.6	43.3	115.0	41.1

b) Factors affecting the tax charge in the year

The current tax assessed for the year is lower than the standard rate of corporation tax in the United Kingdom (28%).

The differences are explained below:

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Profit on ordinary activities before tax	281.6	240.3	281.4	227.7
Profit on ordinary activities multiplied by the standard rate of corporation tax of 28% (2008: 30%)	78.8	72.1	78.8	68.3
Effects of:				
Items not taxable or not deductible for tax purposes	(1.8)	(1.8)	(4.4)	(0.2)
Capital allowances for period in excess of depreciation	(3.2)	(1.8)	(3.2)	(1.8)
Utilisation of/movement in short term timing difference	0.3	4.2	0.3	4.2
Adjustment to tax charge in respect of prior periods	(8.9)	(7.9)	(8.9)	(7.9)
	65.2	64.8	62.6	62.6

Of the current year charge, £1.9 million (2008: £5.5 million) relates to current tax credits on exceptional items and £2.9 million credit (2008: £1.6 million credit) in respect of deferred tax.

5 Taxation on profit on ordinary activities continued

c) Tax charged directly to equity

In addition to the amount charged to the profit and loss account the following amounts have been credited directly to equity:

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Current tax relief on pension contributions in excess of amounts charged to the profit and loss account	(3.5)	-	(3.5)	-
Deferred tax on actuarial gains and losses	(27.4)	(11.5)	(27.4)	(11.5)
Tax credited directly to equity	(30.9)	(11.5)	(30.9)	(11.5)

d) Factors affecting future tax rates

The group's current tax charge of £74.1 million (2008: £72.7 million) before adjustments to the tax charge in respect of prior periods represents 26.3% (2008: 30.3%) of the group's profit before tax.

The company's current tax charge of £71.5 million (2008: £70.5 million) before adjustments to the tax charge in respect of prior periods represents 25.4% (2008: 30.9%) of the company's profit before tax.

The group and the company's tax charge will continue to be affected in future years by the requirements of AMP4 which will impact both depreciation and capital allowances.

In 2008 the deferred tax adjustment in respect of prior years included an amount to reflect the decrease in the main corporation tax rate to 28% with effect from 1 April 2008, being the rate at which deferred tax will reverse and an adjustment of £29.7 million to remove the element of deferred tax which related to industrial buildings.

The group and company's deferred tax charge in future years is difficult to predict as it is impacted by changes to interest rates from one balance sheet date to the next.

6 Dividends

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Dividends paid	154.7	263.1	154.7	263.1

The company's dividend policy is to declare dividends which are consistent with the company's regulatory obligations and at a level which is decided each year after consideration of a number of factors, including regulatory uncertainty, market expectations, actual and potential efficiencies, future cash flow requirements and balance sheet considerations.

The amount declared is expected to vary each year as the impact of these factors changes. The ordinary dividend declared and paid by the company in 2008/09 amounted to £154.7 million, being 15.47p per share (2008: 26.31p per share).

9 Debtors**a) Amounts falling due within one year**

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Trade debtors	120.1	129.6	120.1	129.6
Amounts owed by parent and fellow subsidiary undertakings	2.3	2.5	6.9	4.5
Other debtors	12.9	17.3	12.9	15.4
Prepayments and accrued income	143.4	149.7	146.1	146.4
	278.7	299.1	286.0	295.9

b) Amounts falling due after more than one year

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Trade debtors	-	0.1	-	0.1
Other debtors	-	0.1	-	0.1
Amounts owed by parent and fellow subsidiary undertakings	-	-	30.4	27.1
Prepayments and accrued income	2.4	1.9	2.4	-
	2.4	2.1	32.8	27.3
Total debtors	281.1	301.2	318.8	323.2

10 Creditors: amounts falling due within one year

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Bank overdrafts	0.2	383.0	-	419.9
Bank loans	100.0	78.6	100.0	78.6
Loans due to parent and fellow subsidiary undertakings	15.0	-	-	-
Other loans	31.7	-	-	-
Obligations under finance leases	43.4	39.6	43.4	39.6
Borrowings (note 12)	190.3	501.2	143.4	538.1
Trade creditors	20.2	15.7	20.2	15.7
Amounts owed to parent and fellow subsidiary undertakings	32.0	28.4	157.1	38.9
Amounts owed to subsidiary undertakings	-	-	-	532.7
Other creditors	2.4	10.7	7.2	8.9
Taxation and social security	4.4	4.8	4.4	4.8
Corporation tax payable	45.7	42.8	42.8	43.9
Accruals and deferred income	298.1	285.5	259.0	284.7
	593.1	889.1	634.1	1,467.7

11 Creditors: amounts falling due after more than one year

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Bank loans	447.8	541.9	447.8	541.9
Loans due to subsidiary undertakings	-	-	2,918.0	2,003.8
Other loans	2,918.0	2,540.3	-	-
Obligations under finance leases	300.5	345.4	300.5	345.4
Borrowings (note 12)	3,666.3	3,427.6	3,666.3	2,891.1
Deferred income	34.4	36.1	34.4	36.1
Other creditors	4.5	4.1	17.7	4.1
	3,705.2	3,467.8	3,718.4	2,931.3

12 Financial instruments

The group's policy in respect of interest rate risk management and the related use of financial instruments are set out in the accounting policy note 10 on page 27.

a) Borrowings analysed by maturity date

	Group				
	Overdrafts £m	Loans with other repayment terms £m	Finance leases £m	2009 £m	2008 £m
Financial liabilities due within one year (note 10)	0.2	146.7	43.4	190.3	501.2
Between one and two years	-	-	46.9	46.9	175.3
Between two and five years	-	191.8	47.6	239.4	122.2
After more than five years	-	3,174.0	206.0	3,380.0	3,130.1
Total financial liabilities after one year	-	3,365.8	300.5	3,666.3	3,427.6
	0.2	3,512.5	343.9	3,856.6	3,928.8

£548.0 million (2008: £542.0 million) of funding instruments contain certain financial covenants, breach of which can trigger early repayment.

Loans repayable partly or wholly after five years comprise:

	Group		
	Rate of interest %	2009 £m	2008 £m
European Investment Bank loans – 2016-17 (2008: 2013-17)	1.8–2.8	300.0	441.9
European medium term loan notes – 2014-67 (2008: 2014-67)	1.4–6.6	1,763.7	1,750.0
Sterling bonds – 2018-29 (2008: 2024-29)	6.0–6.3	1,110.3	710.4
		3,174.0	2,902.3

7 Tangible fixed assets

	Group				
	Land and buildings £m	Infrastructure assets £m	Plant and equipment £m	Vehicles and mobile plant £m	Total £m
Cost					
At 1 April 2008	2,174.5	3,813.2	2,934.1	47.6	8,969.4
Additions	145.6	195.1	286.0	8.6	635.3
Grants and contributions	-	(27.9)	-	-	(27.9)
Assets sold or written off	(5.5)	-	(59.5)	(8.9)	(73.9)
At 31 March 2009	2,314.6	3,980.4	3,160.6	47.3	9,502.9
Depreciation					
At 1 April 2008	673.6	1,369.2	1,485.8	23.3	3,551.9
Charge for year	47.7	118.5	165.8	6.0	338.0
Assets sold or written off	(5.5)	-	(59.5)	(6.9)	(71.9)
At 31 March 2009	715.8	1,487.7	1,592.1	22.4	3,818.0
Net book value					
At 31 March 2009	1,598.8	2,492.7	1,568.5	24.9	5,684.9
At 31 March 2008	1,500.9	2,444.0	1,448.3	24.3	5,417.5

	Company				
	Land and buildings £m	Infrastructure assets £m	Plant and equipment £m	Vehicles and mobile plant £m	Total £m
Cost					
At 1 April 2008	2,174.5	3,810.9	2,934.2	47.6	8,967.2
Additions	145.6	195.1	286.0	8.6	635.3
Grants and contributions	-	(27.9)	-	-	(27.9)
Assets sold or written off	(5.5)	-	(59.5)	(8.9)	(73.9)
At 31 March 2009	2,314.6	3,978.1	3,160.7	47.3	9,500.7
Depreciation					
At 1 April 2008	673.6	1,369.0	1,485.8	23.3	3,551.7
Charge for year	47.7	118.5	165.8	6.0	338.0
Assets sold or written off	(5.5)	-	(59.5)	(6.9)	(71.9)
At 31 March 2009	715.8	1,487.5	1,592.1	22.4	3,817.8
Net book value					
At 31 March 2009	1,598.8	2,490.6	1,568.6	24.9	5,682.9
At 31 March 2008	1,500.9	2,441.9	1,448.4	24.3	5,415.5

7 Tangible fixed assets continued

i) Included in tangible fixed assets are assets held under finance leases as follows:

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Cost	411.7	416.4	409.3	414.0
Accumulated depreciation	(143.9)	(126.6)	(143.6)	(126.3)
Net book value	267.8	289.8	265.7	287.7

ii) Grants and contributions received relating to infrastructure assets have been deducted from the cost of fixed assets in order to show a true and fair view as set out in note 1f.

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

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Freehold	1,598.5	1,500.6	1,598.5	1,500.6
Short leasehold	0.3	0.3	0.3	0.3
	1,598.8	1,500.9	1,598.8	1,500.9

iv) Included below are the following tangible fixed assets not subject to depreciation:

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Land	23.7	22.6	23.7	22.6
Assets in the course of construction	571.7	425.2	571.7	425.2
	595.4	447.8	595.4	447.8

8 Investments

	Group	
	Other investments £m	Total £m
Cost and net book value at 1 April 2008 and 31 March 2009	-	-

	Company			
	Shares in subsidiary undertakings £m	Loans to subsidiary undertakings £m	Other investments £m	Total £m
Cost and net book value at 1 April 2008 and 31 March 2009	170.1	65.5	0.1	235.7

	Country of registration and operation	Percentage and class of share capital held	Nature of business
Subsidiary undertakings (all directly held)			
Biogas Generation Limited	England and Wales	100% ordinary	Power generation
East Worcester Water Limited	England and Wales	100% ordinary and 100% non voting ordinary	Water undertaking
Severn Trent Power Generation Limited	England and Wales	100% ordinary	Power generation
Severn Trent Reservoirs Limited	England and Wales	100% ordinary	Finance company
Severn Trent Utilities Finance Plc	England and Wales	100% ordinary	Finance company

In the opinion of the directors the fair values of the group's and company's investments are not less than the amount at which they are stated in the balance sheet.

12 Financial instruments continued**b) Investment in interest earning assets**

	Group	
	2009 £m	2008 £m
Cash at bank and in hand	12.9	–
Sterling deposits	147.1	448.7
	160.0	448.7

Sterling deposits include £1.8 million (2008: £1.8 million) held on short term deposit with a maturity date of less than one year as security for self insurance obligations.

Sterling deposits receive interest based on LIBID.

c) Borrowings analysed by interest rate after taking account of various interest rate swaps entered into by the group and company

	Group			
	Fixed interest rate £m	Floating interest rate £m	Index linked rate £m	Total £m
Maturity profile:				
Less than one year	123.3	66.8	–	190.1
Between one and two years	11.5	35.4	–	46.9
Between two and five years	45.1	46.5	147.8	239.4
Between five and twenty years	1,526.5	505.7	158.4	2,190.6
In more than twenty years	416.3	38.6	734.5	1,189.4
Total borrowings excluding overdrafts	2,122.7	693.0	1,040.7	3,856.4
Overdrafts	–	0.2	–	0.2
Total borrowings including overdrafts	2,122.7	693.2	1,040.7	3,856.6
Impact of interest rate swaps entered into by the group and company	420.7	(420.7)	–	–
Total borrowings after the impact of interest rate swaps	2,543.4	272.5	1,040.7	3,856.6
Short term deposits and cash at bank and in hand	(160.0)	–	–	(160.0)
Net debt as at 31 March 2009	2,383.4	272.5	1,040.7	3,696.6
Total borrowings after the impact of interest rate swaps as at 31 March 2008	2,094.8	813.3	1,020.7	3,928.8
Short term deposits and cash at bank and in hand	–	(448.7)	–	(448.7)
Net debt at 31 March 2008	2,094.8	364.6	1,020.7	3,480.1

Fixed interest debt incurs interest at a weighted average rate of 5.9% (2008: 5.8%). Interest on these borrowings is fixed for a weighted average period of 12.7 years (2008: 16.9 years).

Included in the fixed interest debt above, the group has entered into a number of forward start accruing interest rate swaps. These have a notional value of £31.7 million and accrete notional value up to 2032. The maximum notional value of these swaps is £135 million (2008: £135 million). These swaps are floating to fixed and bear fixed interest at between 5.25% and 5.52%.

The group has two forward dated swaps (floating to fixed) with a total notional value of £106 million (2008: £138 million) that bear interest at 4.61% and 4.87%. These interest rate swaps commenced on 6 May 2009 and terminate in 2010.

Floating rate borrowings bear interest based on LIBOR.

The principal outstanding under index linked debt is adjusted by the change in the Retail Prices Index at regular intervals. Interest is charged at fixed rates on the adjusted amount.

12 Financial instruments continued**d) Fair value of financial instruments**

The group uses financial derivatives solely for the purposes of managing the interest rate and currency risks associated with financing business activities. The group's policy for the management of interest rate risk is to have a balanced portfolio of debt with a mix of term and interest rate structures that diversifies its risk and is appropriate to the long life of its asset base. The details are periodically reviewed to respond to changing market conditions and to have regard to regulatory pronouncements. At 31 March 2009 interest rates on 65.9% of the group's borrowings were fixed for periods up to 26 years.

The group's business does not involve significant exposure to foreign exchange transactions. Cross currency swaps are employed to exchange foreign currency borrowings for sterling.

Financial instrument by category: Asset/(liability)	Group			
	Book value £m	2009 Fair value £m	Book value £m	2008 Fair value £m
Primary financial instruments held or issued to finance business activities				
Short term deposits	147.1	147.1	448.7	448.7
Cash at bank and in hand	12.9	12.9	-	-
Short term debtors and creditors	70.2	70.2	88.8	88.8
Borrowings falling due within one year	(190.3)	(231.6)	(500.9)	(465.0)
Borrowings falling due after more than one year	(3,666.3)	(4,616.1)	(3,475.8)	(3,277.5)
Derivative financial instruments held to manage the currency and interest rate profile				
Interest rate swaps and similar instruments	-	(101.5)	-	(42.9)
Currency instruments – cross currency swaps	205.9	197.1	47.9	40.2
Total net financial liabilities	(3,420.5)	(4,521.9)	(3,391.3)	(3,207.7)
Other long term assets				
Other fixed asset investments	0.1	0.1	-	-

Where available, market rates have been used to determine fair values. When market prices are not available, fair values have been calculated by discounting cash flows at prevailing interest rates.

e) Borrowing facilities

The group and company had the following undrawn committed facilities available at 31 March 2009:

	Group and company	
	2009 £m	2008 £m
Expiring within one year	-	-
Expiring in more than one year but not more than two years	-	41.7
Expiring after two years but less than five years	500.0	458.3
	500.0	500.0

These facilities are held jointly by with Severn Trent Plc.

12 Financial instruments continued

f) Unrecognised gains and losses on hedges at 31 March 2009

Gains or losses on derivative instruments are not recognised until the exposure that is being hedged is itself recognised. Unrecognised gains or losses on hedges at the balance sheet date are summarised in the table below. These gains or losses represent the expected future benefit or cost of interest rate and foreign currency hedges to the group and company at 31 March 2009 given prevailing economic conditions.

	Group		
	Gains £m	Losses £m	Total net gains/(losses) £m
Unrecognised gains and losses on hedges 1 April 2008	4.5	(55.2)	(50.7)
Arising in previous years that were recognised in the year	–	24.7	24.7
Arising before 1 April 2008 that were not recognised in the financial year	4.5	(30.5)	(26.0)
Unrecognised gains and losses arising during the financial year	18.7	(103.0)	(84.3)
Unrecognised gains and losses at 31 March 2009	23.2	(133.5)	(110.3)
Expected to be recognised			
In one year or less	–	(4.8)	(4.8)
In later years	23.2	(128.7)	(105.5)

13 Provisions

Provisions for liabilities and charges comprise:

	Group			
	Balance at 1 April 2008 £m	Charged/ (credited) to profit and loss account £m	Utilised £m	Balance at 31 March 2009 £m
Restructuring	2.8	0.4	(2.7)	0.5
Insurance	1.1	(0.1)	(0.1)	0.9
Dilapidation and onerous leasehold properties	2.8	1.8	(0.2)	4.4
Fines and penalties	35.8	2.2	(38.0)	–
Deferred tax	450.9	52.4	–	503.3
	493.4	56.7	(41.0)	509.1

	Company			
	Balance at 1 April 2008 £m	Charged/ (credited) to profit and loss account £m	Utilised £m	Balance at 31 March 2009 £m
Restructuring	2.8	0.4	(2.7)	0.5
Insurance	1.1	(0.1)	(0.1)	0.9
Dilapidation and onerous leasehold properties	2.8	1.8	(0.2)	4.4
Fines and penalties	35.8	2.2	(38.0)	–
Deferred tax	450.9	52.4	–	503.3
	493.4	56.7	(41.0)	509.1

13 Provisions continued

The restructuring provision reflects costs to be incurred in respect of committed programmes. All of the associated outflows are expected to occur within one year (2008: one year) of the balance sheet date.

Provision is made for insurance claims notified and for claims incurred but which have not yet been notified. The associated outflows are expected to arise over a period of up to four years (2008: up to four years) from the balance sheet date.

Provision is made for dilapidation costs and leasehold property costs. The associated outflows are expected to arise over a period of up to nine years from the balance sheet date.

On 8 April 2008, Ofwat published its proposals to fine the company £35.8 million for misreporting customer service data and failure to meet Guaranteed Standard of Service in 2005/06. This amount was paid in the year ended 31 March 2009.

Deferred tax

The full deferred tax liability, calculated at a tax rate of 28% (2008: 28%) is:

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Capital allowances	820.3	809.0	820.3	809.0
Other timing differences	(11.4)	(12.1)	(11.4)	(12.1)
Deferred tax asset relating to pension liability	(58.7)	(31.2)	(58.7)	(31.2)
Undiscounted provision for deferred tax	750.2	765.7	750.2	765.7
Discount	(305.6)	(346.0)	(305.6)	(346.0)
Discounted provision for deferred tax	444.6	419.7	444.6	419.7
Adjustment for deferred tax asset relating to pension liability (included in note 17)	58.7	31.2	58.7	31.2
Deferred tax as disclosed in provisions	503.3	450.9	503.3	450.9
Provision at start of year	450.9	484.4	450.9	484.4
Deferred tax charge included in profit and loss account	52.4	(21.5)	52.4	(21.5)
Deferred tax charge included in statement of recognised gains and losses	(27.4)	(11.5)	(27.4)	(11.5)
Adjustment for deferred tax relating to pension liability (included in note 17)				
Included in profit and loss account charge	-	(12.0)	-	(12.0)
Included in statement of recognised gains and losses charge	27.4	11.5	27.4	11.5
Provision at end of year	503.3	450.9	503.3	450.9

14 Share capital

	Group		Company	
	2009 £m	2008 £m	2009 £m	2008 £m
Authorised				
1,000,000,000 ordinary shares of £1 each (2008: 1,000,000,000)	1,000.0	1,000.0	1,000.0	1,000.0
Issued and fully paid				
1,000,000,000 ordinary shares of £1 each (2008: 1,000,000,000)	1,000.0	1,000.0	1,000.0	1,000.0

15 Profit and loss account

	Group	Company
	£m	£m
At 1 April 2008	243.0	456.6
Profit for the financial year	164.0	166.4
Share based payments	3.0	3.0
Actuarial loss	(110.4)	(110.4)
Tax on actuarial loss	30.9	30.9
Dividends paid	(154.7)	(154.7)
At 31 March 2009	175.8	391.8

At 31 March 2009 cumulative goodwill written off against group reserves amounted to £29.2 million (2008: £29.2 million).

16 Commitments and contingent liabilities**a) Investment expenditure commitments**

	Group and company	
	2009	2008
	£m	£m
Contracted for but not provided in the financial statements	182.3	261.5

In addition to these commitments, the group and company have longer term expenditure plans which include investments to achieve improvements in performance mandated by the Director General of Water Services and to provide for growth in demand for water and sewerage services.

b) Operating lease commitments

The group is committed to making the following payments during the next year in respect of operating leases which expire as follows:

	2009		2008	
	Land and buildings £m	Other £m	Land and buildings £m	Other £m
Within one year	0.2	0.6	0.2	0.1
Between one and five years	0.7	-	0.1	0.5
After five years	1.4	-	1.5	-
	2.3	0.6	1.8	0.6

The company is committed to making the following payments during the next year in respect of operating leases which expire as follows:

	2009		2008	
	Land and buildings £m	Other £m	Land and buildings £m	Other £m
Within one year	0.2	0.6	0.2	0.1
Between one and five years	0.7	-	0.1	0.5
After five years	17.4	-	17.3	-
	18.3	0.6	17.6	0.6

16 Commitments and contingent liabilities continued

c) Banking arrangements

The banking arrangements for both the group and company operate on a pooled basis with certain other group undertakings.

Under these arrangements participating companies guarantee each others' overdrawn balances to the extent of their credit balances. Credit balances can be offset against overdrawn balances of participating companies. The contingent liability as at 31 March 2009 is £nil million (2008: £nil million).

17 Pensions

The group and company participates in the Severn Trent Water Pension Scheme (STPS) and the Severn Trent Mirror Image Scheme (STMIS) (together 'the Schemes'), both of which are defined benefit schemes and are funded to cover future salary and pension increases. The assets of the schemes are held in a separate fund administered by trustees.

As from 1 April 2004, the STPS was amended with new defined benefit and defined contribution sections introduced.

The UK defined benefit schemes and the date of their last formal actuarial valuation are as follows:

UK defined benefit scheme	Date of last formal actuarial valuation
Severn Trent Pension Scheme*	31 March 2007
Severn Trent Mirror Image Pension Scheme	31 March 2006

* The STPS is by far the largest of the group's UK defined benefit schemes. The Severn Trent Senior Staff Pension Scheme was merged with the STPS on 31 March 2009.

Following the valuation of the STPS, the employers' contribution rates were increased to 33.24%, 27.70% or 16.62% of pensionable pay until 1 July 2008 when rates were set at 22.4%. STPS members' contributions continue at a rate of 6%, 5% or 3% of pensionable pay.

The Schemes are closed to new entrants and hence the current service costs are expected to increase as members in the Schemes approach retirement.

The actuarial liabilities and market values of the assets at 31 March 2009 of the group's defined benefit schemes, details of which are provided above, have been assessed by the group's actuaries in accordance with the requirements of FRS 17.

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:

	2009	2008
Valuation Method	Projected unit	Projected unit
Price inflation	2.90%	3.40%
Salary increase	3.90%	4.90%
Pension increases in payment*	3.00%	3.40%
Pension increases in deferment*	2.90%	3.40%
Discount rate	6.70%	6.40%
Longevity at age 65 for pensioners retiring now		
– men	20.1	20.1
– women	23.2	23.2
Longevity at age 65 for pensioners retiring in 20 years		
– men	20.9	20.9
– women	23.9	23.9

* In excess of any Guaranteed Minimum Pension.

17 Pensions continued

Amounts recognised in the profit and loss account in respect of these defined benefit schemes are as follows:

	Group and company	
	2009 £m	2008 £m
Amounts charged to operating costs		
Current service cost	(21.2)	(29.8)
Past service costs	(0.5)	–
	(21.7)	(29.8)
Amounts charged to net finance costs		
Interest cost	(81.7)	(71.6)
Expected return on scheme assets	79.8	83.0
	(1.9)	11.4
Total amount charged in profit and loss account	(23.6)	(18.4)

Actuarial gains and losses have been reported in the statement of recognised gains and losses.

An element of the service cost is capitalised in line with the group's accounting policies.

The amount included in the balance sheet arising from the group's obligations under defined benefit schemes is as follows:

	Group and company	
	2009 £m	2008 £m
Present value of defined benefit obligations – funded schemes	(1,162.4)	(1,295.5)
Total fair value of assets	956.6	1,184.0
	(205.8)	(111.5)
Asset not recognised	(3.7)	–
Liability recognised in the balance sheet (before deferred tax)	(209.5)	(111.5)
Deferred tax	58.7	31.2
Liability recognised in the balance sheet	(150.8)	(80.3)

Movements in the present value of the defined obligation were as follows:

	Group and company	
	2009 £m	2008 £m
At 1 April	1,295.5	1,314.1
Service cost	21.2	29.8
Past service costs	0.5	–
Interest cost	81.7	71.6
Contributions from scheme members	7.6	7.7
Actuarial gain	(184.5)	(71.7)
Benefits paid	(59.6)	(56.0)
At 31 March	1,162.4	1,295.5

17 Pensions continued

Movements in the fair value of the schemes assets were as follows:

	Group and company	
	2009 £m	2008 £m
At 1 April	1,184.0	1,208.6
Expected return on scheme assets	79.8	83.0
Contributions	26.8	38.9
Special contributions	9.2	11.6
Contributions from scheme members	7.6	7.7
Actuarial loss	(291.2)	(109.8)
Benefits paid	(59.6)	(56.0)
At 31 March	956.6	1,184.0

The analysis of the assets in the schemes and the expected rates of return were:

	Group and company			
	Expected return	2009 Fair value of assets £m	Expected return	2008 Fair value of assets £m
Equities	8.00%	484.2	8.00%	674.6
Gilts	4.20%	208.4	4.55%	320.7
Corporate bonds	6.70%	205.0	6.40%	111.0
Property	6.10%	46.5	6.30%	68.3
Cash	0.50%	12.5	5.25%	9.4
Total fair value of assets		956.6		1,184.0

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 obligations. For gilts and corporate bonds the expected rates of return are based on market yields at the previous balance sheet date.

For equities, an equity risk premium has been added to the gilt rate.

The actual return on scheme assets was a loss of £211.4 million (2008: £26.8 million loss).

The estimated amount of normal contributions expected to be paid to the schemes during the year ending 31 March 2010 is £30.4 million and lump sum deficit contributions of £9.3 million are planned.

The history of the actual and expected performance of pension scheme assets and liabilities is:

	Group and company				
	2009 £m	2008 £m	2007 £m	2006 £m	2005 £m
Difference between actual and expected return on scheme assets	(291.2)	(109.8)	(10.9)	137.5	29.5
Percentage of scheme assets	30.4%	9.3%	0.9%	12.5%	3.6%
Experience adjustments on scheme liabilities	184.5	71.7	(8.9)	(111.5)	5.8
Percentage of scheme liabilities	15.9%	5.5%	0.7%	8.9%	0.6%
Actuarial (loss)/gain in the statement of recognised gains and losses	(106.7)	(38.1)	(19.8)	26.0	35.3
Percentage of scheme liabilities	9.2%	2.9%	1.5%	2.1%	3.4%

Defined contribution schemes

The group also operates defined contribution arrangements for certain of its UK 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 £4.0 million (2008: £0.4 million) represents contributions payable to these schemes by the group at rates specified in the rules of the schemes. As at 31 March 2009 all (2008: 100%) contributions due in respect of the current reporting period have been paid over to the schemes.

18 Share based payments

The group operates a number of share based remuneration schemes for employees and details of the share awards outstanding during the year are as follows:

	Employee Sharesave Scheme		Approved Share Option Scheme		Unapproved Share Option Scheme	
	Number of share options	Weighted average exercise price	Number of share options	Weighted average exercise price	Number of share options	Weighted average exercise price
Outstanding at 1 April 2007	3,414,767	736p	16,558	801p	20,292	729p
Granted during the year	583,803	1,221p	-	-	-	-
Forfeited during the year	(73,442)	869p	-	-	-	-
Cancelled during the period	173,496	678p	-	-	-	-
Exercised during the period	(866,224)	554p	(3,035)	988p	(5,498)	771p
Expired during the period	(8,226)	743p	-	-	-	-
Transferred to other group companies	-	-	(3,145)	705p	(6,253)	692p
Outstanding at 1 April 2008	3,224,174	866p	10,378	776p	8,541	729p
Granted during the year	1,566,089	862p	-	-	-	-
Forfeited during the year	(49,413)	971p	-	-	-	-
Cancelled during the period	(268,840)	1,333p	-	-	-	-
Exercised during the period	(881,148)	659p	(3,838)	899p	-	-
Expired during the period	(20,585)	762p	(3,416)	688p	(8,541)	702p
Transferred to other group companies	(123,094)	965p	-	-	-	-
Outstanding at 31 March 2009	3,447,183	876p	3,124	720p	-	-

The weighted average share price during the period was £12.70 (2008: £14.20).

a) Share Option Schemes

The options outstanding at the end of the period are exercisable as shown below.

i) Employee Sharesave Scheme

Under the terms of the Sharesave Scheme, the Severn Trent Plc board may grant those employees who have entered into an HM Revenue and Customs approved Save As You Earn contract for a period of three or five years, the right to purchase ordinary shares in Severn Trent Plc. Options outstanding at 31 March 2009 were as follows:

Date of grant	Normal date of exercise	Option price	2009	Number of shares 2008
January 2001	2008	568p	-	55,346
January 2002	2009	548p	63,899	68,358
January 2003	2008 or 2010	536p	75,784	415,556
January 2004	2009 or 2011	592p	242,076	253,835
January 2005	2008, 2010 or 2012	759p	324,075	713,957
January 2006	2009, 2011 or 2013	823p	537,724	664,742
January 2007	2010, 2012 or 2014	1,172p	322,203	470,359
January 2008	2011 or 2013	1,221p	318,431	582,021
January 2009	2012 or 2014	862p	1,562,991	-
			3,447,183	3,224,174

ii) Share Incentive Plan (SIP)

Under the SIP the board of Severn Trent Plc may grant awards to employees of Severn Trent group companies. During the year the board of Severn Trent Plc has announced that it will make awards under the SIP based on performance against the company's KPI targets. Eligible employees will be entitled to shares to a maximum value of £750. It is expected that these awards will be made in August 2009. SIP shares rest with employees on the date of grant.

18 Share based payments continued**iii) Approved Share Option Scheme**

Under the terms of the Share Option Scheme (formerly Executive Share Option Scheme), the Severn Trent Plc board has granted directors and other executives options to purchase ordinary shares in Severn Trent Plc. Options outstanding under this scheme at 31 March 2009 were as follows:

Date of grant	Normal date of exercise	Option price	2009	Number of shares 2008
June 1999	2002-09	934p	-	3,211
June 2000	2003-10	688p	-	3,416
June 2002	2005-12	720p	3,124	3,751
			3,124	10,378

iv) Unapproved Share Option Scheme

The Severn Trent Plc board has granted executives options to purchase ordinary shares in Severn Trent Plc under an unapproved share option scheme. There were no options outstanding under this scheme at 31 March 2009.

Date of grant	Normal date of exercise	Option price	2009	Number of shares 2008
June 1999	2002-09	934p	-	108
June 2000	2003-10	688p	-	5,449
June 2002	2005-12	720p	-	2,984
			-	8,541

b) Long Term Incentive Plan (LTIP)

Under the LTIP conditional awards of Severn Trent Plc shares may be made to executive directors and senior staff. Awards are subject to performance conditions and continued employment throughout the vesting period.

The LTIP awards are subject to total shareholder return for Severn Trent Plc measured relative to the companies ranked 51-150 by market capitalisation in the FTSE index (excluding investment trusts).

c) Fair values of awards made in the year

	Number	2009 Fair value £m	Number	2008 Fair value £m
LTIP awards	123,743	0.9	89,539	0.4
Sharesave options	1,566,089	4.2	583,803	1.8

The fair value of the LTIP awards was calculated using the Monte Carlo method. The principal assumptions were as follows:

LTIP award year	2008/09	2007/08
Share price at grant date	1,280p	1,370p
Number of shares awarded	123,743	89,539
Number of employees	23	20
Vesting period (years)	3	3
Expected volatility	17%	15%
Expected life (years)	3	3
Expected dividend yield	n/a	n/a
Proportion of employees expected to cease employment before vesting	0%	0%
Expectation of meeting economic profit performance criteria	n/a	n/a
Fair value per share (EP scheme/TSR scheme)	749p	477p

18 Share based payments continued**c) Fair values of awards made in the year** continued

The fair value of the Sharesave options was calculated using the Black Scholes model. The principal assumptions were as follows:

Scheme year	2008/09		2007/08		2006/07		
	3 year	5 year	3 year	5 year	3 year	5 year	7 year
Scheme type	3 year	5 year	3 year	5 year	3 year	5 year	7 year
Share price at grant date	862p	862p	1,520p	1,520p	1,428p	1,428p	1,428p
Number of options granted	858,622	707,467	350,196	233,607	294,531	156,000	36,547
Number of employees	1,880	827	1,638	630	1,420	511	96
Vesting period (years)	3	5	3	5	3	5	7
Expected volatility	17%	17%	15%	15%	15%	15%	15%
Option life (years)	3.5	5.5	3.5	5.5	3.5	5.5	7.5
Expected life (years)	3.25	5.25	3.25	5.25	3.25	5.25	7.25
Risk free rate	2.24%	2.74%	4.24%	4.29%	5.19%	5.04%	4.92%
Expected dividend yield	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%
Proportion of employees expected to cease employment before vesting	15.0%	17.0%	15.0%	17.0%	15.0%	17.0%	13.0%
Fair value per share – sharesave	272p	268p	307p	312p	295p	305p	306p

Volatility is based on historical observations as adjusted for unusual market fluctuations.

During the period, the group recognised total expenses of £4.7 million (2008: £3.4 million) related to equity settled share based payment transactions.

19 Group cash flow statement**a) Reconciliation of profit before interest to net cash inflow from operating activities**

	2009 £000	2008 £000
Operating profit	468.9	407.1
Depreciation charge (note 7)	338.0	322.4
Profit on disposal of fixed assets	(4.0)	(1.6)
Deferred income received	1.4	0.1
Deferred income credited to profit and loss account	(3.3)	(2.8)
Provisions for liabilities and charges charged to profit and loss account	4.3	41.3
Utilisation of provisions for liabilities and charges	(41.0)	(3.4)
Pension service cost less contributions paid	(14.3)	(20.7)
Increase in stocks	(1.8)	(0.2)
Decrease/(increase) in debtors	3.6	(23.7)
Increase/(decrease) in creditors	11.4	(45.2)
Investment written off	-	(0.1)
Share based payments charge	4.7	3.1
Net cash inflow from operating activities	767.9	676.3

19 Group cash flow statement continued**b) Analysis of changes in net debt**

	At 1 April 2008 £m	Cash flow £m	Other non cash changes £m	At 31 March 2009 £m
Cash at bank and in hand	-	12.9	-	12.9
Overdrafts (note 10)	(383.0)	382.8	-	(0.2)
Net cash	(383.0)	395.7	-	12.7
Debt due within one year (note 10)	(78.6)	(68.1)	-	(146.7)
Debt due after one year (note 11)	(3,082.2)	(263.6)	(20.0)	(3,365.8)
Finance leases (note 10 and 11)	(385.0)	41.1	-	(343.9)
Short term deposits (note 12)	448.7	(301.6)	-	147.1
Net debt (note 12)	(3,480.1)	(196.5)	(20.0)	(3,696.6)

20 Ultimate and immediate parent company and related party transactions

The ultimate parent undertaking and controlling entity is Severn Trent Plc which is registered in England and Wales. The immediate parent undertaking is Severn Trent (W&S) Limited which is registered in England and Wales. Copies of the Annual Report and Accounts of Severn Trent Plc, are available from the Company Secretary, Severn Trent Plc, 2297 Coventry Road, Birmingham B26 3PU.

Alternatively, the report can be viewed and downloaded from Severn Trent Plc's website at: www.severntrent.com/reports2009

As a wholly owned subsidiary, the company has taken advantage of the exemption from disclosing related party transactions with other group undertakings in accordance with the accounting standard FRS 8 'Related Party Disclosures'.

Regulatory accounts

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Water Industry Act 1991

Further to the requirements of company law, the directors are required to prepare financial statements which comply with the requirements of Condition F Instrument of Appointment of the company as a water and sewerage undertaker under the Water Industry Act 1991 and Regulatory Accounting Guidelines issued by the Water Services Regulation Authority. This additionally requires the directors to:

- a) Confirm that, in their opinion, the company has sufficient financial and management resources for the next twelve months;
- b) Confirm that, in their opinion, the company has sufficient rights and assets which would enable a special administrator to manage the affairs, business and property of the company;
- c) Report to the Water Services Regulation Authority changes in the company's activities which may be material in relation to the company's ability to finance its regulated activities;
- d) Undertake transactions entered into by the appointed business, with or for the benefit of associated companies or other businesses or activities of the appointed business, at arm's length; and
- e) Keep proper accounting records which comply with Condition F.

Diversification and the protection of the core business – Condition F6a

Severn Trent Water Limited and its subsidiary East Worcester Water Limited (together referred to as 'the Appointees') hereby advise:

- a) That in the opinion of the directors, the Appointees will have available to them sufficient financial resources and facilities to enable them to carry out, for at least the next 12 months, the Regulated Activity (including the investment programme necessary to fulfil the Appointees' obligations under the Appointment); and
- b) That in the opinion of the directors, the Appointees will for at least the next 12 months, have available to them management resources which are sufficient to enable them to carry out those functions.

Tony Wray
Chief Executive
For and on behalf of the board
28 May 2009

Report of the auditors

to the Water Services Regulation Authority

Independent auditors' report to the Water Services Regulation Authority (WSRA) and Severn Trent Water Limited and subsidiary undertakings (the group)

We have audited the Regulatory Accounts of the group which incorporates East Worcester Water Limited and its other subsidiary undertakings for the year ended 31 March 2009 set out on pages 52 to 67 which comprise:

- the regulatory historical cost accounting statements for the group, comprising the regulatory historical cost profit and loss account and the regulatory historical cost balance sheet; and
- the regulatory current cost accounting statements for the Appointed Business comprising the current cost profit and loss account, the current cost balance sheet, the current cost cash flow statement and the related notes numbered 1 to 12 to the current cost financial statements including the statement on accounting policies on which the Regulatory Accounts have been prepared.

This report is made, on terms that have been agreed, solely to the company and the WSRA in order to meet the requirements of Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the company as water and sewerage undertaker under the Water Industry Act 1991 (the Regulatory Licence). Our audit work has been undertaken so that we might state to the company and the WSRA those matters that we have agreed to state to them in our report, in order (a) to assist the company to meet its obligations under the company's Instrument of Appointment to procure such a report and (b) to facilitate the carrying out by the WSRA of its regulatory functions, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the WSRA, for our audit work, for this report, or for the opinion we have formed.

Basis of preparation

The Regulatory Accounts have been prepared in accordance with Condition F of the Regulatory Licence and the Regulatory Accounting Guidelines (being versions 1.04, 2.03, 3.06, 4.03 and 5.04), the accounting policies set out in the statement of accounting policies and, in the case of the regulatory historical cost accounting statements, under the historical cost convention.

The Regulatory Accounts are separate from the statutory financial statements of the group. There are differences between United Kingdom Generally Accepted Accounting Principles ('UK GAAP') and the basis of preparation of information provided in the regulatory accounts because the Regulatory Accounting Guidelines specify alternative treatment or disclosure in certain respects. Where the Regulatory Accounting Guidelines do not specially address an accounting issue, they then require UK GAAP to be followed. Financial information other than that prepared wholly on the basis of UK GAAP may not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in financial statements prepared in accordance with the Companies Act 1985.

Respective responsibilities of the Regulator, the directors and auditors

The nature, form and content of Regulatory Accounts are determined by the WSRA. It is not appropriate for us to assess whether the nature of the information being reported upon is suitable or appropriate for the WSRA's purposes. Accordingly, we make no such assessment.

The directors' responsibilities for preparing the Regulatory Accounts in accordance with the Regulatory Accounting Guidelines are set in the statement of directors' responsibilities for regulatory information on page 21.

Our responsibility is to audit the Regulatory Accounts in accordance with the International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board, except as stated in the 'Basis of audit opinion' below and having regard to the guidance contained in Audit Technical Release 05/03 'Reporting to Regulators of Regulated Entities'.

We report to you our opinion as to whether the regulatory historical cost accounting statements present fairly, under the historical cost convention, the revenues and costs, assets and liabilities of the Appointee and the Appointed Business in accordance with the company's Instrument of Appointment and Regulatory Accounting Guideline 2.03 (Guideline for classification of expenditure), Regulatory Accounting Guideline 3.06 (Guideline for the contents of regulatory accounts) and Regulatory Accounting Guideline 4.03 (Guideline for the analysis of operating costs and assets) and whether the regulatory current cost accounting statements on pages 54 to 67 have been properly prepared in accordance with Regulatory Accounting Guidelines 1.04 (Guideline for accounting for current costs and regulatory capital values), Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03. We also report to you if, in our opinion, the company has not kept proper accounting records as required by paragraph 3 of Condition F of the Regulatory Licence and whether the information is in agreement with the Appointees' accounting records and has been properly prepared in accordance with the requirements of Condition F and as appropriate, Regulatory Accounting Guideline 1.04, Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03.

We read the other information contained within the Regulatory Accounts, including any supplementary schedules on which we do not express an audit opinion, and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Regulatory Accounts. The other information comprises the performance review, the notes on regulatory information and the additional information required by the Regulatory licence.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board except as noted below. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Regulatory Accounts. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the Regulatory Accounts, and of whether the accounting policies are appropriate to the company circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Regulatory Accounts are free from material misstatement, whether caused by fraud or other irregularity or error. However, as the nature, form and content of Regulatory Accounts are determined by the WSRA, we did not evaluate the overall adequacy of the presentation of the information, which would have been required if we were to express an audit opinion under Auditing Standards.

Our opinion on the Regulatory Accounts is separate from our opinion on the statutory accounts of the company on which we report, which are prepared for a different purpose. Our audit report in relation to the statutory accounts of the company (our 'Statutory' audit) was made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our Statutory audit work was undertaken so that we might state to the company's members those matters we are required to state to them in a statutory auditors' report and for no other purpose.

In those circumstances, to the fullest permitted by law, we do not accept or assume any responsibility to anyone other than the company and the company's members as a body, for our Statutory audit work, for our Statutory audit report, or for the opinions we have formed in respect of that Statutory audit.

The regulatory historical cost accounting statements on pages 52 to 53 have been drawn up in accordance with Regulatory Accounting Guideline 3.06 in that infrastructure renewals accounting as applied in previous years should continue to be applied and accordingly that the relevant sections of Financial Reporting Standards 12 and 15 be disapplied. This represents a departure from Generally Accepted Accounting Principles, and a reconciliation of the balance sheet drawn up on this basis with that drawn up under Companies Act 1985 is given in note 11.

Audit opinion

In our opinion the Regulatory Accounts of the Company for the year ended 31 March 2009 fairly present in accordance with Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the company as water and sewerage undertaker under the Water Industry Act 1991, the Regulatory Accounting Guidelines issued by the WSRA and the accounting policies set out in note 2 to the Regulatory Accounts the state of the company's affairs at 31 March 2009 on a historical cost and current cost basis, the historical cost and current cost profit for the year and the current cost cash flow for the year and have been properly prepared in accordance with those conditions, guidelines and accounting policies.

We are also required to report in respect of various specific obligations of the company as set out in its Instrument of Appointment. In respect of these obligations, we report that in our opinion:

- a) proper accounting records have been kept by the Appointees as required by paragraph 3 of Condition F of the Instrument;
- b) the information is in agreement with the Appointees' accounting records and has been properly prepared in accordance with the requirements of Condition F and, as appropriate, Regulatory Accounting Guidelines 1.04, Regulatory Accounting Guidelines 2.03, Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03 issued by the WSRA;
- c) the regulatory historical cost accounting statements on pages 52 to 53 present fairly, under the historical cost convention, the revenues and costs, assets and liabilities of the company and its appointed business in accordance with the Appointees' Instrument of Appointment and Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03 issued by the WSRA;
- d) The regulatory current cost accounting statements on pages 54 to 67 have been properly prepared in accordance with Regulatory Accounting Guideline 1.04, Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03 issued by the WSRA.

Deloitte LLP

Deloitte LLP
Chartered Accountants
Birmingham UK
28 May 2009

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The maintenance and integrity of the Severn Trent Water's website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters or any changes that may have occurred to the financial statements since they were initially presented on the website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Regulatory accounts – historical cost financial statements

Group profit and loss account year ended 31 March 2009

	Appointed business 2009 £m	Non appointed business 2009 £m	Inter segment 2009 £m	2009 £m	Appointed business 2008 £m	Non appointed business 2008 £m	Inter segment 2008 £m	2008 £m
Turnover	1,309.5	7.1	(0.1)	1,316.5	1,256.8	9.4	(0.9)	1,265.3
Operating costs	(623.2)	(13.0)	7.9	(628.3)	(683.7)	(13.2)	7.5	(689.4)
Historical cost depreciation	(216.2)		-	(216.2)	(201.7)	-	-	(201.7)
Other operating income	4.0	7.8	(7.8)	4.0	1.7	6.6	(6.6)	1.7
Operating profit	474.1	1.9	-	476.0	373.1	2.8	-	375.9
Other income	1.4	2.0	-	3.4	1.7	2.2	-	3.9
Net interest payable	(187.3)	-	-	(187.3)	(166.8)	-	-	(166.8)
Profit on ordinary activities before taxation	288.2	3.9	-	292.1	208.0	5.0	-	213.0
Taxation on profit on ordinary activities								
Current tax	(64.1)	(1.1)	-	(65.2)	(62.0)	(2.8)	-	(64.8)
Deferred tax	(52.4)	-	-	(52.4)	21.5	-	-	21.5
Taxation	(116.5)	(1.1)	-	(117.6)	(40.5)	(2.8)	-	(43.3)
Profit on ordinary activities after taxation	171.7	2.8	-	174.5	167.5	2.2	-	169.7
Dividends	(151.9)	(2.8)	-	(154.7)	(260.9)	(2.2)	-	(263.1)
Retained profit/(loss) for the financial year	19.8	-	-	19.8	(93.4)	-	-	(93.4)

Statement of total recognised gains and losses year ended 31 March 2009

	Appointed business 2009 £m	Non appointed business 2009 £m	Inter segment 2009 £m	2009 £m	Appointed business 2008 £m	Non appointed business 2008 £m	Inter segment 2008 £m	2008 £m
Profit for the financial year	171.7	2.8	-	174.5	167.5	2.2	-	169.7
Actuarial loss	(110.4)	-	-	(110.4)	(38.1)	-	-	(38.1)
Tax on actuarial loss	30.9	-	-	30.9	10.7	-	-	10.7
Adjustment in respect of tax rate change on deferred tax	-	-	-	-	0.8	-	-	0.8
Total recognised gains and losses for the financial year	92.2	2.8	-	95.0	140.9	2.2	-	143.1

The group results presented are for Severn Trent Water Limited and its subsidiary undertakings including East Worcester Water Limited.

Group balance sheet as at 31 March 2009

	Notes	Appointed business 2009 £m	Non appointed business 2009 £m	Inter segment 2009 £m	2009 £m	Appointed business 2008 £m	Non appointed business 2008 £m	Inter segment 2008 £m	2008 £m
Fixed assets									
Tangible assets	11	5,673.9	2.6	-	5,676.5	5,420.7	-	-	5,420.7
Investments		-	-	-	-	-	-	-	-
		5,673.9	2.6	-	5,676.5	5,420.7	-	-	5,420.7
Current assets									
Stocks		8.0	-	-	8.0	6.2	-	-	6.2
Debtors	11	281.1	-	-	281.1	301.2	-	-	301.2
Short term deposits		147.1	-	-	147.1	448.7	-	-	448.7
Cash at bank and in hand		12.9	-	-	12.9	-	-	-	-
		449.1	-	-	449.1	756.1	-	-	756.1
Creditors: amounts falling due within one year									
Overdrafts		(0.2)	-	-	(0.2)	(383.0)	-	-	(383.0)
Creditors		(351.8)	(2.6)	-	(354.4)	(342.4)	-	-	(342.4)
Borrowings		(190.1)	-	-	(190.1)	(118.2)	-	-	(118.2)
Corporation tax payable		(45.7)	-	-	(45.7)	(42.8)	-	-	(42.8)
Infrastructure renewal accrual		(8.4)	-	-	(8.4)	(30.5)	-	-	(30.5)
		(596.2)	(2.6)	-	(598.8)	(916.9)	-	-	(916.9)
Net current liabilities		(147.1)	(2.6)	-	(149.7)	(160.8)	-	-	(160.8)
Total assets less current liabilities		5,526.8	-	-	5,526.8	5,259.9	-	-	5,259.9
Creditors: amounts falling due after more than one year									
Borrowings		(3,666.3)	-	-	(3,666.3)	(3,427.6)	-	-	(3,427.6)
Other creditors		(4.5)	-	-	(4.5)	(4.1)	-	-	(4.1)
		(3,670.8)	-	-	(3,670.8)	(3,431.7)	-	-	(3,431.7)
Provision for liabilities and charges									
- Deferred taxation		(503.3)	-	-	(503.3)	(450.9)	-	-	(450.9)
- Other provisions		(5.8)	-	-	(5.8)	(42.5)	-	-	(42.5)
Deferred income		(37.1)	-	-	(37.1)	(38.8)	-	-	(38.8)
Pension deficit		(150.8)	-	-	(150.8)	(80.3)	-	-	(80.3)
Net assets		1,159.0	-	-	1,159.0	1,215.7	-	-	1,215.7
Capital and reserves									
Called up share capital		1,000.0	-	-	1,000.0	1,000.0	-	-	1,000.0
Profit and loss account		159.0	-	-	159.0	215.7	-	-	215.7
Shareholders' funds		1,159.0	-	-	1,159.0	1,215.7	-	-	1,215.7

Regulatory accounts – current cost financial statements

Group profit and loss account: appointed business year ended 31 March 2009

	Notes	2009 £m	2008 £m
Turnover	3a	1,309.5	1,256.8
Current cost operating costs	3d	(896.4)	(939.6)
Other operating income	3b	3.9	1.6
		417.0	318.8
Working capital adjustment	3c	0.1	(0.4)
Current cost operating profit		417.1	318.4
Other income		1.4	1.7
Net interest payable		(187.3)	(166.8)
Financing adjustment		(10.6)	104.9
Current cost profit before taxation		220.6	258.2
Taxation on profit on ordinary activities			
Current tax		(64.1)	(62.0)
Deferred tax		(52.4)	21.5
Taxation		(116.5)	(40.5)
Current cost profit attributable to shareholders after taxation		104.1	217.7
Dividend		(151.9)	(260.9)
Current cost loss retained		(47.8)	(43.2)

Statement of total recognised gains and losses: appointed business year ended 31 March 2009

	2009 £m	2008 £m
Current cost profit for the financial year	104.1	217.7
Actuarial loss	(110.4)	(38.1)
Tax on actuarial loss	30.9	10.7
Adjustment in respect of tax rate change on deferred tax	-	0.8
Total recognised gains and losses for the financial year	24.6	191.1

Group balance sheet: appointed business as at 31 March 2009

	Notes	2009 £m	2008 £m
Fixed assets			
Tangible assets	4c	30,134.9	29,937.4
Third party contributions since 1989/90		(1,611.2)	(1,507.8)
		28,523.7	28,429.6
Working capital		6.3	28.7
Short term deposits		160.0	448.7
Overdrafts		(0.2)	(383.0)
Infrastructure renewals accrual		(8.4)	(30.5)
Net operating assets		28,681.4	28,493.5
Non operating assets and liabilities			
Borrowings		(190.1)	(118.2)
Non trade debtors		2.2	3.5
Non trade creditors due within one year		(71.2)	(67.2)
Corporation tax payable		(45.7)	(42.8)
Total non operating assets and liabilities		(304.8)	(224.7)
Creditors: amounts falling due after more than one year			
Borrowings		(3,666.3)	(3,427.6)
Other creditors		(4.5)	(4.1)
		(3,670.8)	(3,431.7)
Provision for liabilities and charges			
- Deferred taxation		(503.3)	(450.9)
- Other provisions		(5.8)	(42.5)
Pension deficit		(150.8)	(80.3)
Net provisions		(659.9)	(573.7)
Total assets		24,045.9	24,263.4
Capital and reserves			
Called up share capital		1,000.0	1,000.0
Profit and loss account	6	(427.1)	(302.8)
Current cost reserve	7	23,473.0	23,566.2
		24,045.9	24,263.4

Group cash flow statement year ended 31 March 2009

	Notes	Appointed business		Non appointed business		Total		Appointed business		Non appointed business		Total	
		2009 £m	2009 £m	2009 £m	2009 £m	2009 £m	2009 £m	2008 £m	2008 £m	2008 £m	2008 £m	2008 £m	2008 £m
Net cash inflow from operating activities	8	761.4		6.5		767.9		671.3		5.0			676.3
Returns on investments and servicing of finance													
Interest received		12.5		-		12.5		8.8		-			8.8
Interest paid		(157.7)		-		(157.7)		(128.0)		-			(128.0)
Interest element of finance lease rental payments		(16.2)		-		(16.2)		(20.6)		-			(20.6)
Net cash flow from returns on investment and servicing of finance		(161.4)		-		(161.4)		(139.8)		-			(139.8)
Taxation		(56.7)		(1.1)		(57.8)		(49.9)		(2.8)			(52.7)
Capital expenditure													
Purchase of tangible fixed assets		(491.5)		(2.6)		(494.1)		(479.7)		-			(479.7)
Grants and contributions received		29.4		-		29.4		44.2		-			44.2
Infrastructure renewals expenditure		(130.1)		-		(130.1)		(111.3)		-			(111.3)
Disposal of fixed assets		6.0		-		6.0		2.9		-			2.9
Net cash flow from investing activities		(586.2)		(2.6)		(588.8)		(543.9)		-			(543.9)
Equity dividends paid		(151.9)		(2.8)		(154.7)		(260.9)		(2.2)			(263.1)
Net cash outflow before management of liquid resources and financing		(194.8)		-		(194.8)		(323.2)		-			(323.2)
Management of liquid resources		301.6		-		301.6		(446.8)		-			(446.8)
Net cash flow before financing		106.8		-		106.8		(770.0)		-			(770.0)
Financing													
Finance leases repaid		(41.1)		-		(41.1)		(23.1)		-			(23.1)
Loans advanced		410.5		-		410.5		1,124.3		-			1,124.3
Loans repaid		(78.8)		-		(78.8)		(102.5)		-			(102.5)
Purchase of shares		(1.7)		-		(1.7)		-		-			-
		288.9		-		288.9		998.7		-			998.7
Net increase in cash		395.7		-		395.7		228.7		-			228.7

Reconciliation of net cash flow to movement in net debt

	Appointed business		Non appointed business		Total		Appointed business		Non appointed business		Total	
	2009 £m	2009 £m	2009 £m	2009 £m	2009 £m	2009 £m	2008 £m	2008 £m	2008 £m	2008 £m	2008 £m	2008 £m
Net increase in cash as above	395.7		-		395.7		228.7		-		228.7	
Cash flow from movement in net debt	(290.6)		-		(290.6)		(998.7)		-		(998.7)	
Cash flow from movement in liquid resources	(301.6)		-		(301.6)		446.8		-		446.8	
Change in net debt resulting from cash flows		(196.5)		-		(196.5)		(323.2)		-		(323.2)
Rolled up interest on debt		(20.0)		-		(20.0)		(37.0)		-		(37.0)
Increase in net debt		(216.5)		-		(216.5)		(360.2)		-		(360.2)
Opening net debt		(3,480.1)		-		(3,480.1)		(3,119.9)		-		(3,119.9)
Closing net debt		(3,696.6)		-		(3,696.6)		(3,480.1)		-		(3,480.1)

Notes to the current cost financial statements

Year ended 31 March 2009

1 Regulatory reporting

The regulatory accounts as reported on pages 52 to 68 should be read in conjunction with the operating and financial review on pages 3 to 15 for further understanding of the performance of the business.

It should also be noted that the company has reassessed its forecast for infrastructure renewal expenditure and thus the infrastructure renewals charge has been reduced to reflect this.

In particular, attention is drawn to pages 16 and 17 of the Directors' report which sets out the link between Directors' pay and standards of performance and page 19 of the Directors' report in respect of the statement of disclosure of information to auditors.

2 Accounting policies

a) Basis of preparation

The regulatory financial statements have been prepared on a group basis for Severn Trent Water Limited and its subsidiary undertakings to meet the requirements of the Water Services Regulation Authority (WSRA).

The regulatory financial statements have been prepared in accordance with Condition F of the Instruments of Appointment of the Water and Sewerage Undertakers and the Regulatory Accounting Guidelines as issued by the WSRA, the accounting policies set out in the statement of accounting policies and, in the case of the regulatory historical cost accounting statements, under the historical cost convention.

These accounts have been prepared in accordance with guidance issued by the WSRA for modified real term financial statements suitable for regulation in the water industry. They measure profitability on the basis of real financial capital maintenance, in the context of assets which are valued at their current cost value to the business, with the exception of specialised operational and infrastructure assets.

The regulatory financial statements are separate from the statutory financial statements of the company. There are differences between United Kingdom Generally Accepted Accounting Principles (UK GAAP) and the basis of preparation of information provided in the regulatory accounts because the Regulatory Accounting Guidelines specify alternative treatment or disclosure in certain respects. Where the Regulatory Accounting Guidelines do not specifically address an accounting issue, then they require UK GAAP to be followed. Financial information other than that prepared wholly on the basis of UK GAAP may not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in financial statements prepared in accordance with the Companies Act 1985.

b) General

The accounting policies used are the same as those adopted in the statutory historical cost financial statements on pages 23 to 48, except as set out below.

c) Operating costs

Income relating to electricity generation is deducted from operating costs. The difference between this treatment and that adopted in the statutory accounts is described in note 11.

In prior years the group has treated the income and costs generated by this activity as turnover and operating costs respectively within the non appointed business.

This change has been adopted prospectively. In 2008 turnover for the non appointed business included £2.7 million arising from power generation and £0.6 million of related operating costs. If the guidance in PRO9/14 had been adopted retrospectively these amounts would have been reclassified to operating expenditure of the appointed business.

d) Tangible fixed assets

Assets in operational use are valued at the replacement cost of their operating capability. To the extent that the regulatory regime does not allow such assets to earn a return high enough to justify that value, this represents a modification of the value to the business principle. Also, no provision is made for the possible funding of future replacements of assets by contributions from third parties and, to the extent that some of the tangible fixed assets would on replacement be so funded, replacement cost again differs from value to the business. Redundant assets are valued at their recoverable amounts.

An Asset Management Plan (AMP) survey of existing assets as at 31 March 1998 was undertaken during 1998/99 and the adjustments to asset values as a result of that exercise, were included within the tangible fixed asset note. In the intervening years, between AMP surveys, values are restated to take account of changes in the general level of inflation, as measured by changes in Retail Price Index (RPI), and any other significant changes in asset records identified during the year.

i) Non infrastructure assets

Specialised operational assets:

The gross replacement cost of specialised operational assets has been derived using the latest cost information provided by the AMP.

The unamortised portion of third party contributions received is deducted in arriving at net operating assets (as described below in note 1d).

Non specialised operational assets:

Non specialised operational assets are valued on the basis of open market value for existing use at 31 March 1991 and have been expressed in current terms by adjusting for movements in property values.

ii) Infrastructure assets

Mains, sewers, impounding and pumped raw water storage reservoirs, dams and sludge pipelines are valued at replacement cost, determined principally on the basis of unit cost data provided by the AMP.

iii) Other assets

All other assets are valued on the basis of data provided by the AMP.

iv) Surplus land

Surplus land was valued at current market value for the purposes of the AMP. Any proceeds on disposal to be passed onto customers will be taken into account, in accordance with the requirements contained in Condition B of the Instruments of Appointment as Water and Sewerage Undertakers.

2 Accounting policies continued**e) Grants and other third party contributions**

Grants, infrastructure and other third party contributions received since 31 March 1990 are carried forward to the extent that any balance has not been credited to revenue. The balance carried forward is restated for the change in RPI for the year.

f) Real financial capital maintenance adjustments

These adjustments are made to historical cost operating profit in order to arrive at profit after the maintenance of financial capital in real terms:

Working capital adjustment – this is calculated by applying the change in RPI over the year to the opening total of trade debtors and stock, less trade creditors.

Financing adjustment – this is calculated by applying the change in RPI over the year to the opening balance of net finance, which comprises all assets and liabilities in the balance sheet apart from those included in working capital and excluding fixed assets, deferred taxation provision, index linked debt and dividends payable.

3 Analysis of current cost turnover and operating costs**a) Turnover**

	Water services £m	Sewerage services £m	2009 Total £m	Water services £m	Sewerage services £m	2008 Total £m
Unmeasured – household	322.0	365.9	687.9	318.0	347.1	665.1
Unmeasured – non household	2.7	4.8	7.5	2.5	4.0	6.5
Unmeasured	324.7	370.7	695.4	320.5	351.1	671.6
Measured – household	127.5	136.2	263.7	113.9	129.4	243.3
Measured – non household	114.8	154.3	269.1	115.1	140.1	255.2
Measured	242.3	290.5	532.8	229.0	269.5	498.5
Trade effluent	-	12.0	12.0	-	17.6	17.6
Large user tariffs and special agreements	24.0	29.7	53.7	24.0	26.9	50.9
Revenue grants	-	0.4	0.4	-	0.4	0.4
Non potable large user tariffs and special agreements	-	-	-	-	-	-
Rechargeable works	1.6	0.5	2.1	1.5	0.2	1.7
Bulk supplies/inter company	4.0	-	4.0	4.2	-	4.2
Other	4.0	0.1	4.1	4.1	0.3	4.4
Third parties	9.6	0.6	10.2	9.8	0.5	10.3
Other sources	1.8	3.2	5.0	3.2	4.3	7.5
Total turnover	602.4	707.1	1,309.5	586.5	670.3	1,256.8
b) Other operating income						
Current cost profit on disposal of tangible fixed assets	1.1	2.8	3.9	0.8	0.8	1.6
Total	1.1	2.8	3.9	0.8	0.8	1.6
c) Working capital adjustment	0.1	-	0.1	(0.1)	(0.3)	(0.4)

3 Analysis of current cost turnover and operating costs continued**d) Analysis of operating costs and tangible fixed assets**

	Water services			Sewerage services					Business analysis			2009
	Resources and treatment £m	Distribution £m	Water services subtotal £m	Sewerage £m	Sewage treatment £m	Sludge treatment and disposal £m	Sewage treatment /disposal subtotal £m	Sewerage services subtotal £m	Customer services £m	Scientific services £m	Cost of regulation £m	Total £m
Direct costs												
Employment costs	6.7	16.7	23.4	7.4	11.8	5.8	17.6	25.0				
Power	10.2	16.9	27.1	5.6	10.7	(3.0)	7.7	13.3				
Agencies	-	-	-	-	-	-	-	-				
Hired and contracted	4.1	13.2	17.3	8.9	5.1	15.4	20.5	29.4				
Associated companies	1.0	0.1	1.1	-	-	-	-	-				
Materials and consumables	7.9	3.2	11.1	1.1	4.5	7.7	12.2	13.3				
Service charges	11.4	-	11.4	3.2	5.9	-	5.9	9.1				
Bulk supply imports	9.0	-	9.0	-	-	-	-	-				
Other direct costs	0.3	4.5	4.8	1.3	0.7	0.4	1.1	2.4				
Total direct costs	50.6	54.6	105.2	27.5	38.7	26.3	65.0	92.5	36.5	11.1	6.1	251.4
General and support	26.6	28.6	55.2	24.3	35.9	17.5	53.4	77.7	9.2	1.4	1.3	144.8
Functional expenditure	77.2	83.2	160.4	51.8	74.6	43.8	118.4	170.2	45.7	12.5	7.4	396.2
Business activities recharge			31.5					34.1	(45.7)	(12.5)	(7.4)	-
Rates			37.7					18.3				56.0
Doubtful debts			13.9					16.4				30.3
Exceptional items			8.6					10.8				19.4
			252.1					249.8				501.9
Services for third parties			11.6					1.6				13.2
Total operating expenditure			263.7					251.4				515.1
Capital costs												
Infrastructure renewals charge	3.0	64.4	67.4	40.6				40.6				108.0
Current cost depreciation	55.4	49.8	105.2	32.9	105.2	32.8	138.0	170.9				276.1
Amortisation of deferred income			(1.3)					(1.9)				(3.2)
Business activity capital costs			-					-				-
			171.3					209.6				380.9
Services for third parties depreciation			0.4					-				0.4
Total capital maintenance			171.7					209.6				381.3
Total operating costs			435.4					461.0				896.4
Analysis of tangible fixed assets												
Service activities	1,736.5	7,361.6	9,098.1	18,472.7	1,767.3	342.9	2,110.2	20,582.9				29,681.0
Business activities			138.0	50.4			87.0	137.4				275.4
Service totals			9,236.1	18,523.1			2,197.2	20,720.3				29,956.4
Services for third parties			178.5					-				178.5
Total			9,414.6					20,720.3				30,134.9

3 Analysis of current cost turnover and operating costs continued

d) Analysis of operating costs and tangible fixed assets continued

Included within customer service costs is £3.5 million (2008: £4.5 million) and within exceptional items is £5.0 million (2008: nil) payable to the Severn Trent Trust Fund.

The tables on the analysis of operating costs have been prepared in accordance with Regulatory Accounting Guideline number 4.03 on the analysis of operating costs and assets. Direct costs have been charged directly to the service to which they relate. General and support costs are where possible allocated directly to the service to which they relate. Any remaining general and support costs which cannot be directly allocated to a service are then allocated over the service activity costs on a pro-rata basis, based on the value of direct costs and overhead costs already directly allocated. Business activity costs are analysed firstly on a direct basis, then together with the general and support costs allocated, are apportioned again over the service activity using relevant activity drivers where possible.

	Water services			Sewerage services					Business analysis			2008
	Resources and treatment £m	Distribution £m	Water services subtotal £m	Sewerage £m	Sewage treatment £m	Sludge treatment and disposal £m	Sewage treatment /disposal subtotal £m	Sewerage services subtotal £m	Customer services £m	Scientific services £m	Cost of regulation £m	Total £m
Direct costs												
Employment costs	6.2	15.1	21.3	7.9	12.3	6.6	18.9	26.8				
Power	8.4	13.7	22.1	4.0	9.8	-	9.8	13.8				
Agencies	-	-	-	-	-	-	-	-				
Hired and contracted	1.8	11.6	13.4	9.9	6.6	13.0	19.6	29.5				
Associated companies	1.3	0.1	1.4	-	-	-	-	-				
Materials and consumables	6.6	2.8	9.4	1.1	3.4	6.5	9.9	11.0				
Service charges	10.5	-	10.5	3.2	5.3	-	5.3	8.5				
Bulk supply imports	9.1	-	9.1	-	-	-	-	-				
Other direct costs	-	5.4	5.4	1.3	-	0.1	0.1	1.4				
Total direct costs	43.9	48.7	92.6	27.4	37.4	26.2	63.6	91.0	36.3	13.0	5.0	237.9
General and support	27.1	25.9	53.0	22.4	37.1	17.0	54.1	76.5	9.9	2.0	1.2	142.6
Functional expenditure	71.0	74.6	145.6	49.8	74.5	43.2	117.7	167.5	46.2	15.0	6.2	380.5
Business activities recharge			30.9					36.5	(46.2)	(15.0)	(6.2)	-
Rates			35.9					21.1				57.0
Doubtful debts			10.6					12.1				22.7
Exceptional items			27.2					36.1				63.3
			250.2					273.3				523.5
Services for third parties			13.0					2.0				15.0
Total operating expenditure			263.2					275.3				538.5
Capital costs												
Infrastructure renewals charge	1.5	94.0	95.5	49.7				49.7				145.2
Current cost depreciation	52.1	48.6	100.7	26.0	100.5	31.1	131.6	157.6				258.3
Amortisation of deferred income			(1.3)					(1.5)				(2.8)
Business activity capital costs			-					-				-
			194.9					205.8				400.7
Services for third parties depreciation			0.4					-				0.4
Total capital maintenance			195.3					205.8				401.1
Total operating costs			458.5					481.1				939.6

3 Analysis of current cost turnover and operating costs continued**d) Analysis of operating costs and tangible fixed assets continued**

	Water services			Sewerage services				Business analysis			2008 Total £m	
	Resources and treatment £m	Distribution £m	Water services subtotal £m	Sewerage £m	Sewage treatment £m	Sludge treatment and disposal £m	Sewage treatment /disposal subtotal £m	Sewerage services subtotal £m	Customer services £m	Scientific services £m		Cost of regulation £m
Analysis of tangible fixed assets												
Service activities	1,695.2	7,359.0	9,054.2	18,412.4	1,692.9	340.8	2,033.7	20,446.1				29,500.3
Business activities			128.7	25.4			102.8	128.2				256.9
Service totals			9,182.9	18,437.8			2,136.5	20,574.3				29,757.2
Services for third parties			180.2					-				180.2
Total			9,363.1					20,574.3				29,937.4

e) Reactive and planned maintenance

Expenditure on reactive and planned maintenance included in operating costs for 2009 in respect of infrastructure assets amounted to £24.1 million on water services (2008: £21.1 million) and £16.1 million for sewerage services (2008: £14.1 million).

Expenditure on reactive and planned maintenance included in operating costs for 2009 in respect of non infrastructure assets amounted to £10.0 million on water services (2008: £10.9 million) and £33.7 million for sewerage services (2008: £30.7 million).

4 Analysis of tangible fixed assets by asset type within service**a) Water services tangible fixed assets analysed by asset type**

	Specialised operational assets £m	Non specialised operational assets £m	Infra-structure assets £m	Other assets £m	Total £m
Gross replacement cost					
At 1 April 2008	2,319.9	118.7	8,189.0	354.4	10,982.0
RPI and other adjustments	(9.1)	(0.5)	(30.8)	(1.8)	(42.2)
Additions	114.5	9.6	35.8	32.0	191.9
Disposals and amounts written off	(40.5)	(0.2)	-	(33.4)	(74.1)
At 31 March 2009	2,384.8	127.6	8,194.0	351.2	11,057.6
Depreciation					
At 1 April 2008	1,327.3	38.9	-	250.3	1,616.5
RPI and other adjustments	(6.6)	(0.2)	-	(1.6)	(8.4)
Charge for year	78.0	2.4	-	25.2	105.6
Disposals and amounts written off	(40.5)	(0.2)	-	(32.4)	(73.1)
At 31 March 2009	1,358.2	40.9	-	241.5	1,640.6
Net book value					
At 31 March 2009	1,026.6	86.7	8,194.0	109.7	9,417.0
At 1 April 2008	992.6	79.8	8,189.0	104.1	9,365.5

4 Analysis of tangible fixed assets by asset type within service continued**b) Sewerage services tangible fixed assets analysed by asset type**

	Specialised operational assets £m	Non specialised operational assets £m	Infra- structure assets £m	Other assets £m	Total £m
Gross replacement cost					
At 1 April 2008	4,450.2	136.8	18,157.7	325.5	23,070.2
RPI and other adjustments	(17.9)	(0.5)	(74.7)	4.0	(89.1)
Additions	235.1	9.0	119.7	29.8	393.6
Disposals and amounts written off	(63.6)	(0.3)	-	(39.0)	(102.9)
At 31 March 2009	4,603.8	145.0	18,202.7	320.3	23,271.8
Depreciation					
At 1 April 2008	2,242.1	37.1	-	219.1	2,498.3
RPI and other adjustments	(11.7)	(0.2)	-	(1.6)	(13.5)
Charge for year	136.1	2.4	-	32.4	170.9
Disposals and amounts written off	(63.6)	(0.2)	-	(38.0)	(101.8)
At 31 March 2009	2,302.9	39.1	-	211.9	2,553.9
Net book value					
At 31 March 2009	2,300.9	105.9	18,202.7	108.4	20,717.9
At 1 April 2008	2,208.1	99.7	18,157.7	106.4	20,571.9

c) Total tangible fixed assets analysed by asset type

	Specialised operational assets £m	Non specialised operational assets £m	Infra- structure assets £m	Other assets £m	Total £m
Gross replacement cost					
At 1 April 2008	6,770.1	255.5	26,346.7	679.9	34,052.2
RPI and other adjustments	(27.0)	(1.0)	(105.5)	2.2	(131.3)
Additions	349.6	18.6	155.5	61.8	585.5
Disposals and amounts written off	(104.1)	(0.5)	-	(72.4)	(177.0)
At 31 March 2009	6,988.6	272.6	26,396.7	671.5	34,329.4
Depreciation					
At 1 April 2008	3,569.4	76.0	-	469.4	4,114.8
RPI and other adjustments	(18.3)	(0.4)	-	(3.2)	(21.9)
Charge for year	214.1	4.8	-	57.6	276.5
Disposals and amounts written off	(104.1)	(0.4)	-	(70.4)	(174.9)
At 31 March 2009	3,661.1	80.0	-	453.4	4,194.5
Net book value					
At 31 March 2009	3,327.5	192.6	26,396.7	218.1	30,134.9
At 1 April 2008	3,200.7	179.5	26,346.7	210.5	29,937.4

5 Working capital

	2009 £m	2008 £m
Stocks	8.0	6.2
Trade debtors:		
Measured household	31.0	32.3
Unmeasured household	53.3	54.4
Measured non household	31.9	37.4
Unmeasured non household	1.1	1.1
Other	2.3	4.3
Measured income accrual	125.6	119.3
Prepayments and other debtors	33.7	48.9
Trade creditors	(20.3)	(15.7)
Deferred income – customer advance receipts	(115.8)	(104.8)
Capital creditors and accruals	(71.2)	(59.4)
Accruals and other creditors	(73.3)	(95.3)
	6.3	28.7

6 Reserves – profit and loss account

	£m
At 1 April 2008	(302.8)
Retained current cost loss for the year	(47.8)
Share based payments	3.0
FRS 17 actuarial loss	(110.4)
Tax on actuarial loss	30.9
At 31 March 2009	(427.1)

7 Reserves – current cost reserve

	2009 £m	2008 £m
At 1 April	23,566.2	22,656.9
AMP adjustment	-	-
RPI adjustments:		
Fixed assets	(109.4)	1,066.3
Working capital	(0.1)	0.4
Financing	10.6	(104.9)
Grants and third party contributions	5.7	(52.5)
At 31 March	23,473.0	23,566.2

8 Reconciliation of current cost operating profit to net cash inflow from operating activities

	2009 £m	2008 £m
Current cost operating profit	417.1	318.4
Working capital adjustment	(0.1)	0.4
Working capital changes	10.6	8.8
Other income	1.4	1.7
Current cost depreciation after amortisation of deferred income	273.3	255.9
Current cost profit on disposal of tangible fixed assets	(3.9)	(1.6)
Infrastructure renewals charge	108.0	145.2
Other non cash profit and loss items	(45.0)	(57.5)
Net cash inflow from operating activities	761.4	671.3

9 Analysis of net debt**Interest rate risk profile**

	Fixed interest rate £m	Floating interest rate £m	Index linked rate £m	Total £m
Maturity profile				
Less than one year	123.3	66.8	-	190.1
Between one and two years	11.5	35.4	-	46.9
Between two and five years	45.1	46.5	147.8	239.4
Between five and twenty years	1,526.5	505.7	158.4	2,190.6
In more than twenty years	416.3	38.6	734.5	1,189.4
Total borrowings excluding overdrafts	2,122.7	693.0	1,040.7	3,856.4
Overdrafts	-	0.2	-	0.2
Total borrowings including overdrafts	2,122.7	693.2	1,040.7	3,856.6
Impact of interest rate swaps entered into by the group and company	420.7	(420.7)	-	-
Total borrowings after the impact of interest rate swaps	2,543.4	272.5	1,040.7	3,856.6
Short term deposits and cash at bank and in hand	(160.0)	-	-	(160.0)
Net debt as at 31 March 2009	2,383.4	272.5	1,040.7	3,696.6
Total borrowings after the impact of interest rate swaps as at 31 March 2008	2,094.8	813.3	1,020.7	3,928.8
Short term deposits and cash at bank and in hand	-	(448.7)	-	(448.7)
Net debt at 31 March 2008	2,094.8	364.6	1,020.7	3,480.1

Fixed interest debt incurs interest at a weighted average rate of 5.9% (2008: 5.8%). Interest on these borrowings is fixed for a weighted average period of 12.7 years (2008: 16.9 years).

10 Reconciliation of HCA operating profit to CCA operating profit

	2009 £m	2008 £m
HCA operating profit per regulatory accounts	476.0	375.9
Less non appointed activities	(1.9)	(2.8)
Sub total HCA accounts	474.1	373.1
Less difference in profit on disposals	(0.1)	(0.1)
Add back working capital adjustment	0.1	(0.4)
Add HCA depreciation including infrastructure renewals charge	327.5	349.7
Less CCA depreciation	(276.5)	(258.7)
Less infrastructure renewals charge	(108.0)	(145.2)
CCA operating profit	417.1	318.4

As in previous years the principal reconciling item between the historical cost profit and the current cost profit is the difference in depreciation charges.

11 Reconciliation of regulatory accounts to statutory accounts**Fixed assets**

In preparation of its statutory accounts, the company has followed common industry practice and adopted the infrastructure renewals accounting basis as set out in FRS 15 'Tangible Fixed Assets'. However, for the purposes of the Regulatory Accounts, Ofwat has requested that FRS 15 is not applied for infrastructure renewals accounting, thereby providing a consistent basis with prior years. A reconciliation to the balance sheet shown in the statutory accounts is set out below:

	2009 £m	2008 £m
Infrastructure assets – cost		
As per regulatory accounts	8,006.8	7,603.4
Adjustment to opening balance	1,366.0	1,254.7
Disposal in year	-	-
Infrastructure renewals expenditure capitalised in year	130.1	111.3
Cost as per statutory accounts	9,502.9	8,969.4
Infrastructure assets – depreciation		
As per regulatory accounts	2,330.3	2,182.7
Adjustment to opening balance	1,369.2	1,251.3
Disposal in year	-	-
Depreciation charge in year	118.5	117.9
Depreciation as per statutory accounts	3,818.0	3,551.9
Infrastructure assets – net		
As per regulatory accounts	5,676.5	5,420.7
Infrastructure	8.4	(3.2)
Net book values as per statutory accounts	5,684.9	5,417.5

Deferred income – grants and contributions

In the statutory accounts deferred income relating to grants and contributions of £37.1 million (2008: £38.8 million) is classified as follows:

- Creditors due within one year £2.7 million (2008: £2.7 million)
- Creditors due after more than one year £34.4 million (2008: £36.1 million)

Turnover

In the statutory accounts all income relating to renewable energy exported to National Grid and all income from Renewable Obligation Certificates (ROCs) and ROC bonuses is included in turnover. No adjustment is made for energy generated and used by the company. However, for the purposes of the regulatory accounts, Ofwat has requested that all income relating to electricity generation is deducted from operating costs. A reconciliation to the turnover and operating costs shown in the statutory accounts is set out below:

	2009 £m
As per regulatory accounts	1,316.5
Income relating to exported energy ROCs, and ROC bonuses	8.4
Turnover per statutory accounts	1,324.9

In 2008 there was no difference between the statutory accounts and regulatory accounts in this respect.

12 Regulatory capital values

At each price review, The Office of Water Services sets price limits which it considers will enable companies to earn a reasonable return on capital. The Office of Water Services bases that return on the Regulatory Capital Value (RCV).

The projected outturn for the company's RCV from the December 2004 determination is as follows:

At 31 March

	2006 £m	2007 £m	2008 £m	2009 £m	2010 £m
Per determination (at 2002/03 prices)	4,853	4,981	5,107	5,191	5,292
Actual/estimated outturn (at average prices)	5,209	5,546	5,922	6,198	6,173

Regulatory capital values at 2008/09 prices:

	2009 £m
Opening regulatory capital value for the year	5,922
Indexation	176
Opening regulatory capital value at average 2008/09 prices	6,098
Capital expenditure	488
Infrastructure renewals expenditure	98
Grants and contributions	(42)
Depreciation	(296)
Infrastructure renewals charge	(96)
Outperformance of regulatory assumptions	(52)
Closing regulatory capital value	6,198
Average regulatory capital value	6,148

The RCVs in this table are based on those published by Ofwat in its letter RD08/06, inflated to 2008/09 prices. The value of the RCV is protected against inflation by increasing the value each year by RPI.

Capital expenditure and infrastructure renewals expenditure assumed in setting price limits are added to the RCV. Price setting assumptions on current cost depreciation, the infrastructure renewals charge, and capital grants and contributions received are deducted each year.

A company has an incentive to outperform Ofwat's regulatory assumptions and earn a higher rate of return than was assumed when setting price limits. The RCV is the mechanism used to reflect past capital outperformance and transfer the benefit of this to customers through lower price limits. The level of outperformance is assessed by comparing net actual capital expenditure in the year with Ofwat projections, with the outperformance adjustment deducted from the RCV. The benefits of the outperformance are passed on to customers five years after it has been achieved.

The RCV grows in real terms in the period to 2010, reflecting the scale of the capital programme.

Supplementary Regulatory Accounting Disclosures – unaudited

Year ended 31 March 2009

Information in respect of transactions during the year with any other business or activity of the Appointee or any Associated Company

a) Borrowings or sums lent

Sums borrowed by the Appointees during the year from associated companies were:

		Principal amounts £m	Repayment dates	Interest rates between %
Severn Trent Plc	Borrowed	45.0	January 2009	1.45-2.39
Severn Trent Utilities Finance Plc	Borrowed	17.5	August 2009	2.05
Severn Trent Reservoirs Limited	Borrowed	9.8	October 2009	6.41
Severn Trent Reservoirs Limited	Borrowed	9.9	October 2008	5.26
Severn Trent Utilities Finance Limited	Borrowed	400.0	January 2018	6.00

b) Dividends paid

The company's dividend policy is to declare dividends which are consistent with the company's regulatory obligations and at a level which is decided each year after consideration of a number of factors, including regulatory uncertainty, market expectations, actual and potential efficiencies, future cash flow requirements and balance sheet considerations.

The amount declared is expected to vary each year as the impact of these factors changes. The ordinary dividend declared and paid by the company in 2008/09 amounted to £154.7 million (2008: £263.1 million), being 15.47p per share (2008: 26.31p per share).

c) Transfer of assets/liabilities

During the course of the year the Appointees did not acquire any assets/liabilities from any associated business.

d) Supply of services

Services supplied by the Appointees to associated companies:

Nature of transactions	Company	Terms	£m
Rental of office accommodation	Various	Market rent	0.2
Service charges in respect of payroll, legal, transport and other	Various	Cost	0.9
Water, tankering, reception, treatment and disposal of waste	Various	Market rates	0.4
			1.5

Services supplied to the Appointees by associated companies:

Nature of transactions	Company	Competitive letting	Other market testing	No market	Total turnover £m
Asset management	Cognica Ltd	0.1	-	-	0.1
Provision of customer care facilities	Complete Credit Management Ltd	0.4	-	-	0.4
Insurance services	Derwent Insurance Ltd	-	3.5	-	3.5
Analytical services	Severn Trent Laboratories Ltd	6.5	-	-	6.5
Supply of materials	Severn Trent Metering Services Ltd	1.8	-	0.1	1.9
Meter installation and maintenance	Severn Trent Metering Services Ltd	10.5	-	-	10.5
Supply of materials and other engineering services	Severn Trent Services Ltd	0.7	-	0.5	1.2
Pass through costs	Severn Trent Plc	-	-	1.2	1.2
		20.0	3.5	1.8	25.3

Of the £25.3 million, £12.7 million was spent on investment expenditure.

e) Omission of rights

None

f) Waivers

None

g) Guarantees

None

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