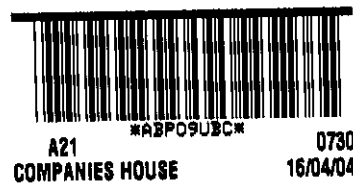


Registered no: 2366661

## **Thames Water Utilities Limited**

Annual Report and Financial Statements

For the year ended 31 December 2003



# Thames Water Utilities Limited

## Annual report for the year ended 31 December 2003

	Pages
Directors and secretary	2
Chairman's review	3 - 6
Corporate governance	7 - 10
Report on remuneration policy and remuneration	11
Directors' report	12 - 18
Report of the independent auditors	19 - 20
Profit and loss account	21
Balance sheet	22
Cash flow statement	23
Notes to the cash flow statement	24
Notes to the financial statements	25 - 45

# Thames Water Utilities Limited

## Directors and secretary at 31 December 2003

### Directors

W J Alexander	Chairman, RWE Thames Water Division Chief Executive
J R Sexton	Managing Director
W U Böttcher	Managing Director RWE Thames Water Europe
C Anderson	Finance Director
S C Walker	RWE Thames Water Division Investment Director

### Independent non-executive directors

C Bowe	Deputy Chairman
P T Warry	
S Slipman	

(See page 13 for changes in directors since 31 December 2002).

### Company Secretary and Registered Office

K G Johnson  
Clearwater Court  
Vastern Road  
Reading  
RG1 8DB

# Thames Water Utilities Limited

## Chairman's review

Thames Water Utilities Ltd, serving the London and the Thames Valley area, is the largest water and wastewater company in the United Kingdom, based on the number of customers served. The Company is committed to serving the needs of its customers, the communities within which it operates and the environment in an efficient and effective way. It is also determined to rise to the ever increasing challenges posed by climate change, growth of population and an ageing network.

We know that reliable and high quality water supply is one of the highest priorities for our customers. Through our investment programme and operating practices we have continued to achieve excellent drinking water quality: 99.9% fully compliant with the current exacting standards. Similarly, our wastewater treatment works, which are required to meet the highest standards in the United Kingdom, have achieved very high levels of treated effluent quality: 99.9% fully compliant. We also achieved 100% compliance with regulations covering the use of sewage sludge in agriculture, for the ninth consecutive year.

Our water and effluent treatment processes are becoming ever more technically complex, and they are essential for the health and well-being of our society and its economy. They also make a major contribution to river water quality and flows, as well as to the ecology and sustainability of the Thames Valley. The river Thames is widely acknowledged as one of the cleanest metropolitan rivers in the world, supporting a growing range of aquatic life.

This performance, coupled with the fact that we continue to have the lowest average combined water and wastewater charges in England and Wales, demonstrates good value for our customers.

### Price Review

In August 2003 we submitted our Draft Strategic Business Plan for the period 2005-2010. Our proposals, if accepted, will allow us to make significant progress in areas vital to our customers and the future security of water supply in our region.

Customer research has shown clear support for the priorities that we have been promoting which would secure the quality advances made over the past decade with some incremental improvement, and provide a firm platform for future growth in demand from population increase.

In our draft plan we propose to renew a significant portion of the older water mains in central London, the area where the greatest proportion of leakage is found. We aim to greatly increase investment in the care and maintenance of our assets, to provide relief for a substantial number of the properties that are currently at risk of sewer flooding and to develop additional water resources. We will also continue to raise quality levels for drinking water and wastewater effluent in line with the obligations determined by Government.

### A Changing Climate

2003 was a challenging year, with floods in winter followed by exceptionally warm and dry summer weather, which extended well into the autumn. The year as a whole was the third driest for over 100 years. Despite these problems, with depleted water resources available in the latter part of the year due to the extended period of low rainfall, we succeeded in maintaining water supplies to our customers without any restrictions imposed, such as hosepipe, or sprinkler bans. In the Oxford and Swindon areas it was necessary to obtain Drought Permits during November to increase the amount of water that could be abstracted from the aquifer and the river Thames to maintain adequate storage levels at our Farmoor Reservoir. We also undertook an extensive media campaign in the area to encourage our customers to be wise in their use of water and we are grateful to all of those who responded positively to our request.

# Thames Water Utilities Limited

## Chairman's review (continued)

### Customer Service

One of our principal aims is to be responsive to service requests and enquiries from our customers at all times. This is particularly vital in emergencies, when the calls made by our customers increase greatly in numbers and importance. We have been reviewing the way in which our customer service centre and our operational teams in the field work together to improve communications and back-up arrangements to ensure that we can respond with speed to operational incidents and customer enquiries.

We take care to provide extra support for our customers in particular need. We administer a customer assistance fund which helps people who are having difficulty paying their water bills to clear past debts and make a fresh start. We have introduced new services for our disabled customers. We now offer an e-mail billing service for blind or partially-sighted customers who have screen reading software on their computers, individually tailored letters and forms which special needs customers can forward to their new water company, if they are moving out of our service area, and bill information printed on yellow paper for people suffering from dyslexia. This is in addition to the established services that we provide to fulfil our duties under the Disability Discrimination Act which include large print and Braille communications, audio-tape, talking bills, textphone (Minicom), sign language and other facilities.

### Operations

Unfortunately things do sometimes go wrong and although our general record on avoiding interruptions in supplies has been good, three major mains bursts in London led to flooding of some premises and to significant numbers of our customers being without water while remedial works were carried out. We very much regret the disruption and inconvenience caused to our customers through these incidents. Full investigations of the causes and our response have been undertaken. We believe that we have learnt lessons from these events and that our response and management arrangements have improved significantly as a result.

In the last few years we have also had some of the most severe wet weather in recent history. This has led to flooding of rivers and of some sewers, affecting customers' premises. We very much regret that some of our customers have had to suffer this appalling experience. Although relatively few homes are now affected, we are determined to keep reducing this most distressing problem. We have allocated more investment to bring forward effective ways of reducing the risks of sewer flooding, with support from our Regulator. In the light of the welcome clarification recently given to the law in this area in the House of Lords, we are seeking further significant investment in our Strategic Business Plan for the 2005-2010 Periodic Review period.

In the UK, enforcement of legislation governing discharges to the water environment is applied under the terms of 'strict liability'. We take these duties particularly seriously and all incidents are carefully reviewed so that steps can be taken to reduce the risk of failure in the future. Some of these incidents resulted in the Company being prosecuted on four occasions in the year, which we very much regret. We have reviewed our incident prevention, control and response arrangements and we will continue to work in conjunction with the Regulator and the Environment Agency to establish areas where procedures and performance can be further improved. We have introduced improved operational practices and planned further investment at our major Mogden wastewater treatment works in west London to reduce problems of odour.

Our core operations were reviewed during 2003, with the creation of separate Water and Wastewater operating units. Asset Management and Engineering units have also been refocused to improve processes between Asset Planning and Investment and Asset Operations across the whole of the Utility business.

# Thames Water Utilities Limited

## Chairman's review (continued)

### Environment, Conservation and Social Responsibility

We are committed to being a socially responsible company and to playing our part in the challenge that society faces in achieving sustainable development. This means working in partnership with the communities that we serve and protecting the natural environment that lies at the very heart of our core business. We aim for continual environmental improvement through the effective management of our operations.

Our investment in our water and wastewater treatment processes and infrastructure has helped maintain our excellent record of compliance with UK drinking water and effluent quality standards, and we also continue to respond to a range of broader environmental challenges. For example, a new combined heat and power plant has been installed at Long Reach wastewater treatment works in Dartford which supports the Government's renewable energy generation policy through the generation of renewable electricity from biogas, with the aim of making the site self-sufficient in electricity. The new Reading wastewater treatment works was graded excellent in the Civil Engineering Environmental Quality Assessment and Awards Scheme. This £80m investment continues on programme, with commissioning planned for 2004.

In 2003 we were pleased that our work for the environment and conservation was recognised by a number of awards. We received two British Trust for Ornithology-Hanson Bird Challenge for Business awards for our Rye Meads and Kempton Nature Reserves and the River Thames Society Annual Trophy for our work with the Wildlife Trust Otters and Rivers Project. In east London, the nature reserve established at our major Crossness wastewater treatment works won both the London Borough of Bexley Environmental Challenge award and a National Green Apple Award.

We are an extensive landowner and take our responsibilities for protecting biodiversity on both our own and third party land seriously. A total of 477 new capital programme projects across the Thames catchment were rigorously checked for any environmental impacts. Our award-winning screening procedure was used to ensure we minimise our impacts on nature conservation, archaeology and the landscape whilst carrying out essential water and wastewater system improvements on our own sites and across the wider Thames region.

The five year Upper River Kennet Rehabilitation Project downstream of Marlborough in Wiltshire has now reached its final reporting stage. The enhancement works, recognised for a national environment award in 2002, have been completed in partnership with the Environment Agency, English Nature, Action for the River Kennet, local landowners and river keepers.

Our community engagement activities in 2003 included continued support for our customers living and working alongside the River Wandle in south London. Thames Water helped to establish JETSET, a charity which aims to educate young people to appreciate, use, "own" and conserve the river. One successful and innovative activity was raising brown trout from eggs in school classrooms and releasing them into the river.

We are an essential part of the communities we serve and we actively encourage voluntary participation among our employees. During 2003 we encouraged our staff to volunteer in their own time and around 2,500 hours of company time were spent carrying out activities with schools and community groups and helping Young Enterprise, a voluntary organisation whose mission is to inspire and equip young people to learn and succeed through enterprise. The Company is an active supporter of WaterAid, the principal UK charity delivering water and sanitation solutions in the developing world.

More details on our environmental performance, conservation and recreation activities and community engagement can be found in our Corporate Responsibility Review, which is available from our Customer Service Centre.

# Thames Water Utilities Limited

## Chairman's review (continued)

### Looking to the future

By its very nature, the operating environment of Thames Water in London presents some unique challenges. The nation's capital has some of the oldest infrastructure serving the largest and densest population in the country, with very high concentrations of traffic and economic activity all round the clock. This population is steadily rising and inevitably putting increased demands on our network, the maintenance cost of which has accelerated in recent years partly due to extreme weather conditions. It is clear that for the continued well-being of the capital we will need to increase investment to improve the sustainability of its essential infrastructure and this is reflected in our plans for the rest of this decade.

Since 1989 the focus of investment has been on water and wastewater quality improvements that were essential to meet both public expectations and legal obligations. We are determined to reduce leakage from our pipes so that overall we deliver a more sustainable supply. The renewal of ageing water mains will be a key element in securing supplies at least cost, together with leakage control, the promotion of water efficiency, a year on year increase in the number of metered properties and the development of new, sometimes innovative, water resources.

We are in a long-term business. Our asset management programmes must ensure reliability of services for current and future generations, and it is being increasingly recognised on all sides that prices will have to reflect this need in the forthcoming Periodic Review. It is crucial that this Periodic Review achieves an appropriate balance between the interests and concerns of our customers, the community and the environment.

### Our employees

Thames Water Utilities Ltd is proud to be part of RWE Thames Water Division, the third largest water business in the world. Our employees have continued to play a key role in the success of the Company, demonstrating a flexible approach and a willingness to embrace change. I would particularly like to commend those employees who have increased their skills in the year through our extensive training programmes. I was very pleased that Thames Water was able to participate in the Government's Ambition:Energy initiative by helping a number of long-term unemployed and disadvantaged people gain on-the-job training in new skills which will equip them for new careers in our industry.

I would like to extend my personal thanks to all our employees for their enthusiastic hard work and commitment, sometimes in challenging circumstances. Along with our contractors and their employees, our employees do a vital job in securing the health and safety of the public through our essential water and wastewater services.



**Bill Alexander**

Chairman

# Thames Water Utilities Limited

## Corporate governance

The Company is committed to high standards of corporate governance. The Company's shares are not listed on the Stock Exchange, however in conducting the appointed water and wastewater business the Directors have particular regard to the principles of good governance in the Combined Code as approved for the purposes of the Listings Rules of the Financial Services Authority. In determining the scope and content of this report it has been our aim to maintain a proper level of disclosure in keeping with those Combined Code provisions which are considered to be applicable to the Company's particular circumstances.

### The Board

The primary responsibility of the Board is to determine the strategic direction of the Company and to promote good corporate governance. It meets bi-monthly, or as required, to monitor executive management and review operating and financial performance. The Board has adopted a formal schedule of matters reserved to the Board, which is reviewed annually and can only be amended by the Board. In reaching its decisions the Board takes account of the interests of the owners, customers and employees, as well as the Company's responsibilities to the environment.

Executive directors are appointed on one year rolling contracts. Independent non-executive directors are appointed to the Board on the basis of their achievements in other companies and organisations and the experience and broader vision, which they can contribute. The aim is that they should be persons of standing, with experience, local knowledge and understanding of the interests of the Company's customers. All independent non-executive directors are required to stand for re-election at least every three years, generally serving for a period of up to six years.

The Deputy Chairman of the Board, C Bowe, is regarded as the senior independent non-executive director.

### Roles of the Chairman and Managing Director

There is a clear division of responsibility between the Chairman and the Managing Director of the Company. Although a director of the immediate parent company, RWE Thames Water plc, the Chairman is a non-executive director of the Company. The Chairman (or in his absence, the Deputy Chairman) is responsible for the effective running of the Board and ensuring that all directors, executive and non-executive, are consulted to enable them to play their full part in the Company's affairs. The Managing Director is responsible for the day-to-day management of the Company and the implementation of the policies and strategies adopted by the Board.

### Board Committees

Four formal committees have been established, as described below. Each of these has written terms of reference, which define the roles and responsibilities of the committee, and these are reviewed annually. In addition, the Board can form committees, as and when required, with delegated authority in relation to specific issues. The minutes of all committees are reported to the Board.



# Thames Water Utilities Limited

## Corporate governance (continued)

### Executive Committee

The main role of the Executive Committee is the executive management of the business, formulation of strategy and the approval of matters which are not specifically reserved for the Board and which have not been specifically delegated to another board committee. Within the Committee's role is primary responsibility for approval of capital investment, and this is discharged through the TWUL Investment Committee, a formal sub-committee of the Board.

**Members:** The members of the Executive Committee consist of at least two executive directors of the Board and such other senior executives of the Company whom the Chairman and Managing Director agree shall be members of the Executive Committee.

### Audit Committee

The primary objective of the Audit Committee is to assist the Board of Directors in fulfilling its responsibilities relating to the adequacy and effectiveness of the Company's systems of internal control. This includes reviewing the Company's interim and annual financial statements, its accounting policies, and the management of its financial and business risks; the effectiveness of the Company's internal audit function; and the independence, objectivity and effectiveness of the Company's external auditors. It makes recommendations to the Board in relation to the external auditor's appointment and remuneration. The terms of reference of the Committee include all matters indicated by the Combined Code, and the Committee considers any other corporate governance issues referred to it by the Board.

**Members:** C Bowe (Chairman), P T Warry, S Slipman

The Audit Committee, which meets at least three times a year is composed exclusively of independent non-executive directors. It meets with executive directors and management as well as privately with the external and internal auditors.

### Environmental and Social Responsibility Review Committee

The principal activities of the Environmental and Social Responsibility Review Committee are reviewing the Company's environmental strategy, performance, reporting, and the sustainability and the social impact of the Company's activities. The Environmental and Social Responsibility Review Committee reviews the Company's discharge of its responsibilities for Conservation, Access and Recreation and approves the publication of the annual statutory Conservation Access and Recreation Report.

**Members:** P T Warry (Chairman), S Slipman, J R Sexton

# Thames Water Utilities Limited

## Corporate governance (continued)

### The Remuneration Committee

The role of the Remuneration Committee is to determine the salaries and other remuneration of the executive directors. The Remuneration Committee is exclusively comprised of the independent non-executive directors of the Board and meets during the year as necessary. The Remuneration Committee is authorised by the Board to obtain external professional services, or consultants' advice, as necessary. The Chairman of the Board or his delegate attends meetings of the Remuneration Committee, but is not a member and does not vote on recommendations.

Members of the Remuneration Committee do not participate in decisions concerning their own remuneration. The Chairman determines the non-executive directors salaries, after considering the advice of the Human Resources Director and independent benchmarking information. The Remuneration Committee approves an appropriate report for inclusion in the Company's Annual Report.

**Members:** S Slipman (Chairman), C Bowe, P T Warry

### Nominations to the Board

The establishment of a formal Nominations Committee was considered, but was not felt to be necessary in the particular circumstances of the Company as a non-listed private subsidiary company. Board level appointments, are normally dealt with by the Chairman in consultation with fellow directors. A Nominations Committee, made up of the independent non-executive directors and the Chairman of the Board, by whom it is chaired, meets on an ad hoc basis to consider candidates for particular roles.

### Internal Control

The Board has overall responsibility for maintaining a sound system of internal control, including financial, operational and compliance controls and risk management, and for reviewing its effectiveness. The internal control system is designed to manage, rather than eliminate, the risk of failure to meet business objectives and can only provide reasonable, and not absolute, assurance against material misstatement or loss. Key features of the overall system of internal control include:

- Regular board meetings with a formal schedule of matters reserved to the Board for decision.
- Clearly defined organisation structures, appropriate delegated authorities, and established policies and procedures, reviewed annually, for conducting all significant aspects of the Company's business.
- A clear business process for the identification, evaluation and mitigation of risks, including regular reporting to the Audit Committee and the Board.
- A detailed five year business plan, comprehensive annual budget, and a clear process of monitoring business performance against that budget on a monthly basis. Revised financial forecasts are prepared quarterly.
- Established policies and procedures for the approval and control of major items of capital expenditure, and for the acquisition and disposal of material assets or entering into of any arrangement which could give rise to a material liability for the Company.
- Formal arrangements for an independent internal audit department to carry out reviews of information systems, and adherence to business and financial control procedures, under a broadly based programme of work approved by the Audit Committee.

# Thames Water Utilities Limited

## Corporate governance (continued)

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

- Regular presentations to the Board and to the Executive Committee by directors of individual business units and functional heads, describing their risk management strategies and detailing the status of significant business risks.
- Quarterly reports to the Risk Management Committee, which although not a formal committee of the Board, is chaired by the Managing Director. This committee receives regular advice and reports from a professional support group comprising senior managers from all parts of the Company's business whose role is to review and challenge the robustness of risk management procedures applied within the business. Any significant changes to the Company's overall risk profile arising from the work of the Risk Management Committee are reported to the Audit Committee and the Board.
- Regular reports to the Audit Committee from the internal audit department on their independent audits of financial and other controls across the Company.

In addition, the directors have conducted an annual review of the effectiveness of the Company's system of internal control, which includes the period up to the date of this annual report. This included a process of self-certification by all business units, supervised by the internal audit department, through which executive directors and heads of business units were required to confirm compliance with prevailing internal control policies and procedures.

# Thames Water Utilities Limited

## Report on remuneration policy and remuneration

The Company's remuneration policy has particular regard to the principles set out in the current edition of the Combined Code on corporate governance. In relation to executive directors the policy is:

- To establish a firm link between an executive's performance and his/her total remuneration
- To establish a firm link between the organisation's performance and the executive's total remuneration
- To position base pay so that it takes account of individual contribution and experience, and has regard to the market so that the Company will attract and retain the required calibre of business leader

Roles are evaluated using external advice and the Hay Guide Chart Profile Method of Evaluation. This is the most widely used job method being used by approximately 8,000 organisations worldwide. The remuneration package includes salary, performance-related bonus, a long-term incentive plan, and pension provision. To date the Company's executive salaries have been typically positioned between median and upper quartile. Base pay is reviewed annually in April (but may be reviewed at any time in exceptional circumstances), and the Remuneration Committee approves all elements of the Company's remuneration of its executive directors. The increases in certain Directors remuneration, as shown in note 5 on pages 30 and 31, reflect increases in responsibility undertaken and performance related bonuses earned. The increase in the remuneration of C Bowe reflects her appointment as Deputy Chairman of the Board.

The Company's bonus scheme aims to reward significant improvement in the Company's performance and recognises the executive's personal contribution to that performance. Performance measures are a combination of RWE Thames Water Division and the Company's financial targets, which are set at the beginning of the financial year combined with the Company's operational and customer service targets (notably Ofwat's DG measures), together with personal performance measures. The Company has taken a lead in the water industry by ensuring that these DG measures translate directly into bonus plans. Top-up pension schemes are provided by way of an Inland Revenue approved pension scheme and a funded unapproved retirement benefit scheme.

As an element of retention strategy, the Company's executive directors participate in a RWE Thames Water Division Long-Term Incentive Plan (LTIP) scheme that aims to encourage, reward, recognise and retain key people. Under the LTIP, executives are awarded conditional rights over a number of RWE shares based on the performance of RWE Thames Water Division. The Divisional Board determines annually whether the underlying financial performance of the Division justifies an award. There is no automatic right to participate in the LTIP and each year executives are selected at the discretion of the Divisional Board.

Details of the remuneration of the Managing Director and the three independent non-executive directors who served during the year under report are set out in note 5 on pages 30 and 31. Significant elements of the responsibilities of the Managing Director of RWE Thames Water Europe and of the Finance Director relate to their wider management roles within the RWE Thames Water Division beyond Thames Water Utilities Limited. The same was true of the Managing Director of Thames Water UK & Ireland while he was a Board director. The non-executive Chairman is not remunerated by the Company, but is instead remunerated by RWE Thames Water plc, and his remuneration is disclosed in the RWE Thames Water plc Annual Report and Accounts. The Division Investment Director receives remuneration in his role as an employee of RWE Thames Water plc, and is not remunerated by the Company, in respect of his role as a non-executive director of the Company.

# Thames Water Utilities Limited

## Directors' report for the year ended 31 December 2003

The directors present their report and the audited financial statements for the year ended 31 December 2003.

### Principal activities and review of the year

The principal activities of the Company are the supply of water to over 3.6 million premises and the collection and treatment of sewage from over 5.5 million premises, serving around 13 million customers in London and the Thames Valley.

Details of the progress made and information relating to the various activities of the Company during the year and plans for the future are given in the Chairman's Review on pages 3 to 6.

### Financial review

The results for the year are set out in the profit and loss account on page 21.

Turnover of £1,136.2m for the year (9 month period ended 31 December 2002: £831.8m), was up 2.5% on the same period in 2002. 1.5% of turnover growth was due to inflationary price increases. The remaining 1.0% of turnover growth was due to sales volume increases as the result of increases in customer base due to new properties built in the area, continuing increases in consumer usage, and billing efficiencies.

Profit on ordinary activities before taxation was £258.6m for the year (9 month period ended 31 December 2002: £212.6m). The year ended December 2003 results were adversely affected by an increased pension cost to the Company, with a total pension cost (SSAP 24 cost) for the year of £13.0m (9 month period ended December 2002: £nil). Additionally operating profit continues to be adversely impacted by additional costs associated with our investment programme, which continues to focus on leakage reduction and security of customer supplies. These increased charges have been substantially offset by the positive impacts of continuing operational efficiency programmes.

The pension cost has increased following independent actuary advice and an interim actuarial valuation undertaken at 31 August 2003, which indicated a reduced pension surplus. To ensure our future pension obligations to employees are met, the Company pension scheme contribution rate has been increased. The Company made contributions of £7.9m for the year ended 31 December 2003 (9 month period ended 31 December 2002: £4.0m) into the Company's pension schemes. Other information about the Company's pension schemes is set out in note 23 on pages 43 to 45 of these accounts.

Capital investment in the period has been particularly targeted towards security of drinking water supplies to our customers, leakage reduction, water and wastewater quality programmes and the alleviation of sewer flooding. Gross capital investment of £605.7m (9 month period ended 31 December 2002: £391.4m), including net infrastructure renewal expenditure of £65.0m (9 month period ended 31 December 2002: £50.8m), was made during the year this substantial investment programme is reflected in the depreciation charge of £268.7m (9 month period ended 31 December 2002: £202.0m).

### Dividends

The Company paid an interim dividend of £44.7m and proposed a second interim dividend of £91.4m in respect of the year. The total dividend for the year of £136.1m compares with a total dividend of £130.9m for the 9 month period ended December 2002.

# Thames Water Utilities Limited

## Directors' report for the year ended 31 December 2003 (continued)

### Board of Directors

The directors of the Company who served during the year are:

W J Alexander	(Non-Executive) Chairman
J R Sexton	Managing Director
T J V Jones	MD, Thames Water UK & Ireland (resigned 19 Sept 2003)
W U Böttcher	MD, RWE Thames Water Europe (appointed 19 Sept 2003)
C Anderson	Finance Director
S C Walker	(Non-Executive) Director

Independent non-executive directors who served during the year are:

C Bowe	Deputy Chairman
P T Warry	
S Slipman	

### Directors' Interests

None of the directors has any interest in the shares of RWE Thames Water plc, or its subsidiary companies. In accordance with Statutory Instrument 1985/802 the Directors' interests in shares of the ultimate parent company, RWE AG, have not been disclosed.

### Significant Contracts

During the year under review none of the directors had significant contracts with RWE AG, RWE Thames Water plc, or any other group company other than their contracts of service.

# Thames Water Utilities Limited

## Directors' report for the year ended 31 December 2003 (continued)

### Policy on Payment of Suppliers

The Company supports a number of initiatives to promote a prompt payment culture, including those proposed by the Construction Round Table and the CBI. The implementation of these principles in the Company's arrangements with its suppliers is managed by its procurement subsidiary Thames Water Procurement Limited, whilst arrangements with its main works contractors are managed through the Engineering Department. All payments to suppliers, service providers and contractors are made on the basis of mutually agreed terms and conditions. During the year the average amount due to trade creditors represented 54 days (9 months to December 2002: 53 days) purchases received from these creditors.

### Employees

We continue to recognise the essential role played by our employees in the successful operation of the Company, and in return, aim to provide employees with a safe and fulfilling environment in which to work and to develop their skills.

We have improved access for employees in gaining training and development, and we have further developed the range of training solutions available for a wide range of needs. In particular, we have continued our focus on developing excellence in people management.

Our graduate recruitment programme continues to prove attractive to a high quality of recruit, and we have been pleased to be able to offer our graduate recruits development opportunities in the form of secondments and training courses within the wider RWE group.

Directors and managers have been offered development to enhance their leadership, people and general business management skills, through continuing to provide access to formal qualifications and through links with UK and international business schools. We continue to see the benefits of informal and formal networking with colleagues in other parts of the RWE Group, in offering our leaders the opportunity to learn about and apply varied business models and approaches.

A new appraisal process for managers has been developed, to improve the identification of potential in the business and to assist in career and succession planning. The appraisal meeting provides an opportunity to identify skills and potential in our managers and to discuss career aspirations and succession.

We are pleased to continue to hold Investors In People accreditation in key areas of the business. Continuing to recognise the importance of customer service, we have supported a number of employees in successfully achieving external accreditation through the Institute of Customer Service awards, at various levels.

Formal consultation in the Company continues to be via a partnership agreement, and the Company and its recognised Trade Unions have been pleased to share their experience of working together in this way with other organisations and with the Department of Trade and Industry. We have plans in place to further embed partnership working in the Company.

# Thames Water Utilities Limited

## Directors' report for the year ended 31 December 2003 (continued)

We are committed to sharing information with employees on key business issues and our communications framework is subject to continual review and development. We have established a variety of communication channels, including the employee magazine "team:thameswater," team briefings and regular e-mail updates, together with the holding of team building conferences and events.

The Company's work-life balance policy helps to ensure that employees are able to meet the demands of their job while at the same time being offered support with their wider home responsibilities.

The Company recognises the importance of diversity. We have outlined our commitment to the recruitment, development and retention of employees with disabilities through our Disability Policy. The Company endeavours to continue to employ any person who has become disabled during the course of their employment. We are committed to ensuring that we treat people fairly and that we combat discrimination, through our Equal Opportunities Policy.

### Research and Development

Recent improvements in the technology and economics of large scale, municipal seawater desalination plants have improved the potential viability of supplementing limited fresh water resources with saline or brackish water resources, which can be more resilient to drought conditions. Research on such potential new water resources has been carried out in London. Two pilot scale brackish water intakes have been investigated, a surface intake direct from the Thames Tideway and a novel horizontally drilled borehole running under the riverbed. Large scale pilot plant trials using advanced pre-treatment technologies followed by reverse osmosis desalination membranes have produced excellent quality drinking water from the surface intake. Saline groundwater yield trials started towards the end of 2003. This research supports potential investment in a brackish water desalination plant to meet increasing demand for potable water in and around London.

A major programme of research to better understand the condition and performance relationships for London's extensive but ageing water distribution pipes network has moved from laboratory to full-scale fieldwork. This work has included creating a statistically valid sampling programme to identify, excavate and condition assess some 500 pipe samples for corrosion and residual structural strength. In addition, four complete old streets, pre-1900, have been subjected to a detailed scientific and archaeological excavation, recording ground conditions, type of pipework found and full exhumation of pipework for laboratory condition assessment. This research has been carried out in collaboration with Cranfield, Southampton and Surrey University research teams and other specialists in pipe condition assessment. New techniques for determining residual bend load strength have been developed for cast iron pipe samples, representing potential failure conditions under traffic and soil movement loadings.

The findings show considerable differences in condition and performance of cast iron pipes between older Metropolitan London and other areas. The research supports planning and targeting of investment in water distribution infrastructure.

In its wider research role, the Company has increased engagement with the UK and international academic research community on longer-range issues including rapid microbial detection and monitoring systems for drinking water and improved conversion of bio-solids from sewage sludge to bio-fuels such as methane and hydrogen.



# Thames Water Utilities Limited

## Directors' report for the year ended 31 December 2003 (continued)

### Health and Safety

We are proud of our proactive commitment to effective health and safety risk management and have in place the necessary policies and arrangements that establish our values and standards and monitor their application. Competence in managing health and safety is an essential part of professional management, relying upon co-operative effort and effective communication at all levels in the Company.

Our overall health and safety objectives are to:

- Prevent injury to employees and others affected by our work
- Prevent damage to plant, equipment and buildings
- Control accident potential and ill health hazards through attention to our well established Health and Safety Standards and Procedures
- Ensure co-operation and effective communication at all levels
- Continual improvement in health and safety management

The primary health and safety risk activities that the business manages on a day-to-day basis are:

- Work on or near deep water
- Construction and tunnelling
- Machinery
- Streetworks
- Confined space work
- High voltage electricity
- Occupational health hazards
- Chemicals and gases

The necessary risk assessments, company standards and training programmes are in place to effectively control such risks and are subject to continual review.

During the year, a number of major initiatives have been implemented to progress our health and safety goals.

Key areas have included:

- Improved compliance arrangements for the purposes of maintaining health and safety management in relation to hazardous substances at our sites that are controlled under the requirements of the Control of Major Accident Hazard Regulations. We have continued to work closely with the Environment Agency and the Health and Safety Executive and have met company and statutory requirements in this area.
- Progress has been made in ensuring that we meet our obligations in the new "Duty to Manage Asbestos" under the Control of Asbestos at Work Regulations.
- The Company Drug and Alcohol Policy has now been fully implemented.
- A new system has been introduced to enable effective recording and monitoring of sickness absence, which will enable trends to be analysed in the future.
- Our dedicated Health and Safety Training Centre provided skills training and management development for over 2,500 employees.

# Thames Water Utilities Limited

## Directors' report for the year ended 31 December 2003 (continued)

### Health and Safety Performance

There have been no fatal accidents, dangerous occurrences or prosecutions during the year affecting the Company directly, although contractors working with the Company reported twelve dangerous occurrences. We are working with our contractors to ensure that concerns on the observations of safety precautions by some of their staff are addressed.

We fully complied with an Improvement Notice, which was issued by the Environment Agency at the end of 2002 in relation to information requirements under the Control of Major Accident Hazard Regulations for one of our water treatment works.

A Prohibition Notice served by the Health and Safety Executive relating to access was in place for a short period to facilitate investigations in connection with an accident at the Beckton sludge powered generator. The notice was lifted within two days.

There were 918 lost working days for the year of 2003 resulting from reportable accidents. This equates to an incidence rate, expressed as the number per 1000 employees of 8.75 (2002: 11.01).

### Initiatives for 2004

Looking forward, we are committed to a range of development initiatives, which include:

- Programmed workshops to further develop management skills in risk assessment and self-auditing functions.
- Continually updating our policies and procedures published on our updated intranet system.
- Review and revitalisation of occupational health.

### Directors' Responsibilities

Company law requires the directors to prepare financial statements for each financial period that give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. The directors are required to prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Company will continue in business.

The directors confirm that suitable accounting policies have been used and applied consistently. They also confirm that reasonable and prudent judgements and estimates have been made in preparing the financial statements for the year ended 31 December 2003 and that applicable accounting standards have been followed.

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.

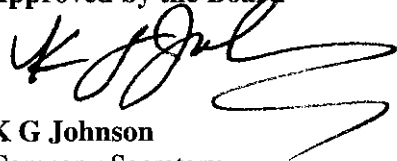
# Thames Water Utilities Limited

## Directors' report for the year ended 31 December 2003 (continued)

### Auditors

A resolution to reappoint PricewaterhouseCoopers LLP as auditors to the Company will be proposed at the annual general meeting.

### Approved by the Board



**K G Johnson**  
Company Secretary

# Thames Water Utilities Limited

## Report of the independent auditors to the members of Thames Water Utilities Limited

We have audited the financial statements, which comprise the profit and loss account, the balance sheet, the cash flow statement and the related notes.

### Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable United Kingdom law and accounting standards 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 United Kingdom Auditing Standards issued by the Auditing Practices Board. This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

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 if, in our opinion, the directors' report is not consistent with the financial statements, if 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 transactions is not disclosed.

We read the other information contained in the annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the chairman's review, corporate governance statements, report on remuneration policy and remuneration and the directors' report.

### Basis of audit opinion

We conducted our audit in accordance with auditing standards 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 judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the 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.

# Thames Water Utilities Limited

## Report of the independent auditors to the members of Thames Water Utilities Limited (Continued)

### Opinion

In our opinion the financial statements give a true and fair view of the state of the Company's affairs at 31 December 2003 and of its profit and cash flows for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

*PricewaterhouseCoopers LLP*

**PricewaterhouseCoopers LLP**  
**Chartered Accountants and Registered Auditors**  
**Reading**  
**24 March 2004**

# Thames Water Utilities Limited

## Profit and loss account for the year ended 31 December 2003

	Note	Year ended Dec 2003 £m	9 month period ended Dec 2002 £m
<b>Turnover</b>	2	<b>1,136.2</b>	831.8
Operating costs	2 & 3	<u>(767.0)</u>	<u>(553.0)</u>
<b>Operating profit</b>		<b>369.2</b>	278.8
Profit on sale of fixed assets	4	14.5	21.3
Net interest	6	<u>(125.1)</u>	<u>(87.5)</u>
<b>Profit on ordinary activities before taxation</b>	2	<b>258.6</b>	212.6
Taxation on profit on ordinary activities	7	<u>(74.6)</u>	<u>(58.0)</u>
<b>Profit for the year / period</b>		<b>184.0</b>	154.6
Dividends	8	<u>(136.1)</u>	<u>(130.9)</u>
<b>Retained profit for the year / period</b>	19 & 20	<u><b>47.9</b></u>	<u>23.7</u>

All amounts above relate to continuing operations.

There is no difference between the profit on ordinary activities before taxation and the profit for the year / period stated above, and their historical cost equivalents.

The Company has no recognised gains and losses other than the profit stated above and therefore no separate statement of recognised gains and losses has been presented.

# Thames Water Utilities Limited

## Balance sheet at 31 December 2003

	Note	Dec 2003 £m	Dec 2002 £m
<b>Fixed assets</b>			
Tangible assets	9	<b>4,924.6</b>	4,626.6
Investments	10	<u>0.1</u>	<u>0.1</u>
		<b>4,924.7</b>	4,626.7
<b>Current assets</b>			
Stocks and work in progress	11	<b>5.8</b>	8.3
Debtors	12	<b>441.9</b>	463.3
Cash at bank and in hand		<u>-</u>	<u>0.8</u>
		<b>447.7</b>	472.4
<b>Creditors: amounts falling due within one year</b>	13	<b>(1,267.6)</b>	(1,054.8)
<b>Net current liabilities</b>		<u>(819.9)</u>	<u>(582.4)</u>
<b>Total assets less current liabilities</b>		<u>4,104.8</u>	<u>4,044.3</u>
<b>Creditors: amounts falling due after more than one year</b>	14	<b>(1,784.7)</b>	(1,824.2)
<b>Provision for liabilities and charges</b>	16	<u>(797.0)</u>	<u>(744.9)</u>
<b>Net assets</b>		<u><b>1,523.1</b></u>	<u>1,475.2</u>
<b>Capital and reserves</b>			
Called up share capital	17	<b>1,029.0</b>	1,029.0
Share premium	18	<b>100.0</b>	100.0
Profit and loss account	19	<u><b>394.1</b></u>	<u>346.2</u>
<b>Equity shareholders' funds</b>	20	<u><b>1,523.1</b></u>	<u>1,475.2</u>

The notes on pages 24 to 45 form part of these financial statements.

The financial statements were approved by the Board of Directors on 24 March 2004 and were signed on its behalf by:



**C Anderson**  
Director

# Thames Water Utilities Limited

## Cash flow statement for the year ended 31 December 2003

	Note	Year ended Dec 2003 £m	9 month period ended Dec 2002 £m
<b>Net cash inflow from operating activities</b>	(a)	<b>740.6</b>	<b>445.8</b>
<b>Returns on investments and servicing of finance</b>			
Interest received		0.7	1.6
Interest paid		(110.8)	(76.5)
Interest in finance lease rentals		<u>(11.7)</u>	<u>(11.7)</u>
<b>Net cash (outflow) from returns on investments and servicing of finance</b>		<b>(121.8)</b>	<b>(86.6)</b>
<b>Taxation</b>		<b>(12.2)</b>	<b>-</b>
<b>Capital expenditure and infrastructure renewals</b>			
Gross cost of purchased fixed assets		(526.9)	(310.8)
Infrastructure renewals expenditure		(67.6)	(54.8)
Receipt of grants and contributions		60.8	42.7
Disposal of fixed assets		<u>15.6</u>	<u>21.3</u>
<b>Net cash (outflow) from investment activities</b>		<b>(518.1)</b>	<b>(301.6)</b>
<b>Equity dividends paid</b>		<b><u>(132.8)</u></b>	<b><u>(128.4)</u></b>
<b>Net cash (outflow) before financing</b>		<b>(44.3)</b>	<b>(70.8)</b>
<b>Financing</b>			
Capital element in finance lease rentals		(5.4)	(5.0)
New loans		446.0	224.7
Repayment of loans		<u>(397.1)</u>	<u>(158.0)</u>
<b>Net cash inflow from financing</b>	(c)	<b><u>43.5</u></b>	<b><u>61.7</u></b>
<b>Decrease in cash</b>	(c)	<b><u>(0.8)</u></b>	<b><u>(9.1)</u></b>



# Thames Water Utilities Limited

## Notes to the cash flow statement for the year ended 31 December 2003

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

	Note	Year ended Dec 2003 £m	9 month period ended Dec 2002 £m
Operating profit		369.2	278.8
Depreciation (infrastructure)	2	68.1	54.8
Depreciation (non-infrastructure)	2	200.6	147.2
Decrease in stocks and work in progress		2.5	0.2
Decrease/(Increase) in debtors and prepaid expenses		24.4	(100.7)
Increase in creditors and accrued expenses		82.5	71.1
Release of deferred income		(6.7)	(5.6)
<b>Net cash inflow from operating activities</b>		<b>740.6</b>	<b>445.8</b>

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

	Note	Year ended Dec 2003 £m	9 month period ended Dec 2002 £m
Decrease in cash in the period		(0.8)	(9.1)
Cash inflow from movement in net debt and financing		(43.5)	(61.7)
Increase in net debt resulting from cashflows		(44.3)	(70.8)
Non-cash increase in net debt		(6.6)	-
Total increase in net debt		(50.9)	(70.8)
Opening net debt		(2,138.1)	(2,067.3)
<b>Closing net debt</b>	(c)	<b>(2,189.0)</b>	<b>(2,138.1)</b>

Non-cash changes comprise the carrying value uplift by RPI, of an RPI index-linked bond. This adjustment is in accordance with FRS 4 'Capital instruments', which requires the carrying value of such index-linked loans to be recalculated at each balance sheet date.

### (c) Analysis of net debt

	Dec 2002 £m	Cashflow £m	Non-cash £m	Dec 2003 £m
Cash at bank and in hand	0.8	(0.8)	-	-
Debt due within 1 year	(396.9)	(99.3)	-	(496.2)
Debt due after 1 year	(1,496.5)	50.4	(6.6)	(1,452.7)
Finance leases	(245.5)	5.4	-	(240.1)
	<u>(2,138.9)</u>	<u>(43.5)</u>	<u>(6.6)</u>	<u>(2,189.0)</u>
<b>Total</b>	<u>(2,138.1)</u>	<u>(44.3)</u>	<u>(6.6)</u>	<u>(2,189.0)</u>

# Thames Water Utilities Limited

## Notes to the financial statements

### 1 Principal accounting policies

A summary of the more important accounting policies, which have been applied consistently, is set out below.

#### (a) Basis of preparation

The financial statements have been prepared in accordance with the historical cost convention and with applicable Accounting Standards in the United Kingdom and, except for the treatment of certain capital contributions, with the Companies Act 1985. An explanation of the departure from the requirements of the Act is given in note 1(d) below.

The Company has not prepared consolidated group financial statements, as permitted under section 228 of the Companies Act 1985. The Company and its subsidiaries are included in the consolidated accounts of its parent company RWE Thames Water plc, a company registered in the UK.

#### (b) Turnover

Turnover, which excludes value added tax, represents the income receivable in the ordinary course of business, for goods and services provided.

#### (c) Tangible fixed assets

Tangible fixed assets comprise:

##### (i) Infrastructure assets:

Infrastructure assets include mains and sewers, impounding and pumped raw water storage reservoirs and sludge pipelines.

Infrastructure assets comprise a network of systems. Expenditure on infrastructure assets is treated as additions. Expenditure on maintaining the operating capability of the network in accordance with defined standards of service is charged as an operating cost and is classified as depreciation.

##### (ii) Other assets:

Other assets include properties, over ground plant and equipment.

Other assets are included at cost less accumulated depreciation. Freehold and long leasehold land is not depreciated. Assets in the course of construction are not depreciated until they are commissioned. Employee costs incurred in implementing the capital schemes of the company are included within the cost of fixed asset additions.

Other assets are depreciated evenly over their estimated economic lives, which are principally as follows:

Operational structures	40 - 80 years
Other buildings	20 - 60 years
Fixed and mobile plant	8 - 40 years
Vehicles, computers, fixtures and fittings	3 - 10 years

# Thames Water Utilities Limited

## Notes to the financial statements

### (d) Capital contributions

Capital contributions received in respect of infrastructure assets have been deducted from the cost of fixed assets. This is not in accordance with Schedule 4 to the Companies Act 1985 which requires fixed assets to be stated at their purchase price without deduction of contributions, which are accordingly accounted for as deferred income. This departure from the requirement of the Act is, in the opinion of the directors, necessary for the financial statements to give a true and fair view because infrastructure assets do not have a finite life. Accordingly related capital contributions would not be recognised in the profit and loss account. The effect of the departure on the value of tangible fixed assets is disclosed in note 9.

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

### (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 treated as if they had been purchased and the corresponding capital cost is shown as an obligation to the lessor. Leasing payments are treated as consisting of a capital element and finance costs, the capital element reducing the obligation to the lessor and the finance charges being written off to the profit and loss account over the period of the lease in relation to the assets' written down values. The assets are generally depreciated over the shorter of their estimated economic lives and the lease period.

All other leases are regarded as operating leases. Rental costs arising under operating leases are expensed in the year in which they are incurred.

### (f) Investments

Investments held as fixed assets are stated at cost less provisions for impairment in value. Investments held as current assets are stated at the lower of cost and net realisable value.

### (g) Stocks and work in progress

Stocks and work in progress are valued at the lower of cost and net realisable value. Cost includes labour, material, transport and an element of overheads.

### (h) Foreign currencies

All transactions denominated in foreign currencies are translated into sterling at the actual rate of exchange ruling on the date of the transaction. Assets and liabilities in foreign currencies are translated into sterling at rates of exchange ruling at the balance sheet date. All exchange differences arising are dealt with in the profit and loss account.

# Thames Water Utilities Limited

## Notes to the financial statements

### (i) Pension costs

The majority of the Company's employees belong to pension schemes which are funded by both employer's and employees' contributions and which are of the defined benefit type.

The pension cost is assessed in accordance with the advice of an independent, qualified actuary to recognise the expected cost of providing pensions on a systematic and rational basis over the expected remaining service lives of employees. Any difference between the cost charged and the amounts paid by the Company is treated as a prepayment or accrual.

In accordance with the permitted transitional arrangements under FRS 17, 'Retirement Benefits', the costs, accruals and prepayments recorded in the financial statements continue to be reported under the requirements of SSAP 24 'Accounting for Pension Costs'.

Information on the Company's pension arrangements can be found in note 23 to these financial statements, and in the financial statements of the immediate parent company RWE Thames Water plc.

### (j) Research and development

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

### (k) Taxation

The charge for taxation is based on the profit for the year as adjusted for disallowable and non-taxable items.

Tax deferred or accelerated is accounted for in respect of all material timing differences in full, in accordance with the requirements of FRS 19. Provision is made at the rate, which is expected to apply when the liability or asset is expected to crystallise. Future liabilities have not been discounted.

### (l) Related party disclosures

The Company is exempt under the terms of FRS 8 from disclosing related party transactions with entities that are part of the RWE AG group.

### (m) Derivative financial instruments

Interest rate and cross currency swaps are used to manage interest rate profiles and mitigate exchange risks. When matched with primary financial instruments, the net position is measured at the hedge rate and presented within creditors on the balance sheet. Incomes, costs, gains, losses and expenses are recognised within net interest payable in the profit and loss account over the life of the instruments.

# Thames Water Utilities Limited

## Notes to the financial statements

### 2 Segmental analysis by class of business

Turnover, operating profit and net assets derive wholly from activities within the United Kingdom.

#### Operating results

	Water supply	Sewerage services	Other trading activities	Year ended Dec 2003	9 month period ended Dec 2002
	£m	£m	£m	£m	£m
<b>Total turnover year ended Dec 2003</b>	<u>478.1</u>	<u>625.0</u>	<u>33.1</u>	<u>1,136.2</u>	
Total turnover 9 month period ended Dec 2002	<u>348.6</u>	<u>450.2</u>	<u>33.0</u>		<u>831.8</u>
<b>Operating Costs</b>					
Operating costs before depreciation	(254.0)	(220.6)	(23.7)	(498.3)	(351.0)
Depreciation - other	(93.7)	(106.5)	(0.4)	(200.6)	(147.1)
Depreciation - infrastructure	<u>(46.7)</u>	<u>(21.4)</u>	<u>-</u>	<u>(68.1)</u>	<u>(54.9)</u>
<b>Total operating costs year ended Dec 2003</b>	<u>(394.4)</u>	<u>(348.5)</u>	<u>(24.1)</u>	<u>(767.0)</u>	
Total operating costs 9 month period ended Dec 2002	<u>(275.8)</u>	<u>(251.9)</u>	<u>(25.3)</u>		<u>(553.0)</u>
<b>Operating profit year ended Dec 2003</b>	<u>83.7</u>	<u>276.5</u>	<u>9.0</u>	<u>369.2</u>	
Operating profit 9 month period ended Dec 2002	<u>72.8</u>	<u>198.3</u>	<u>7.7</u>		<u>278.8</u>
Profit on sale of fixed assets	1.8	12.7	-	14.5	21.3
Net interest	<u>(61.7)</u>	<u>(63.6)</u>	<u>0.2</u>	<u>(125.1)</u>	<u>(87.5)</u>
<b>Profit on ordinary activities before taxation year ended Dec 2003</b>	<u>23.8</u>	<u>225.6</u>	<u>9.2</u>	<u>258.6</u>	
Profit on ordinary activities before taxation 9 month period ended Dec 2002	<u>30.2</u>	<u>174.4</u>	<u>8.0</u>		<u>212.6</u>
<b>Net Assets</b>					
				<b>Year ended Dec 2003</b>	<b>9 month period ended Dec 2002</b>
				<b>£m</b>	<b>£m</b>
Water supply				<u>1,823.8</u>	1,772.8
Sewerage services				<u>1,875.6</u>	1,830.5
Other trading activities				<u>12.7</u>	10.8
Net operating assets				<u>3,712.1</u>	3,614.1
Net interest bearing liabilities				<u>(2,189.0)</u>	<u>(2,138.9)</u>
				<u>1,523.1</u>	<u>1,475.2</u>

# Thames Water Utilities Limited

## Notes to the financial statements

### 3 Operating costs

Analysis of operating costs by type of expense:

	Note	Year ended Dec 2003 £m	9 month period ended Dec 2002 £m
Manpower costs	5	157.4	111.3
Other external charges		309.8	225.5
Materials and consumables		22.8	16.5
Other operating charges		36.3	20.2
Depreciation:			
- owned asset (infrastructure)		68.1	54.8
- owned assets (non-infrastructure)		191.5	139.4
- assets held under finance leases		9.1	7.8
Rentals under operating leases:			
- hire of plant and machinery		2.0	3.1
- other		7.7	6.1
Auditors' remuneration:			
- for statutory audit work		0.3	0.2
- for regulatory audit work		0.1	-
Research and development		6.1	4.6
		<u>811.2</u>	<u>589.5</u>
Own work capitalised		<u>(44.2)</u>	<u>(36.5)</u>
		<u>767.0</u>	<u>553.0</u>

The auditors received remuneration of £21,776 in respect of non-audit work (2002: £25,500).

### 4 Profit on sale of fixed assets

	Year ended Dec 2003 £m	9 month period ended Dec 2002 £m
Profit on disposal of fixed assets	<u>14.5</u>	<u>21.3</u>
Taxation attributable, included in the charge for the year / period	<u>0.6</u>	<u>1.1</u>

# Thames Water Utilities Limited

## Notes to the financial statements

### 5 Information regarding directors and employees

Aggregate directors remuneration:

	Year ended Dec 2003 £000	9 month period ended Dec 2002 £000
Salary	595	410
Bonus	228	48
Other benefits	50	28
Total aggregate emoluments	<u>873</u>	<u>486</u>

Retirement benefits are accruing to 3 directors (2002: 3) under a defined benefit scheme.

Aggregate remuneration of each of the executive directors:

	Year ended Dec 2003 £000	9 month period ended Dec 2002 £000
T J V Jones	224	147
C Anderson	200	110
J R Sexton	244	141
W U Böttcher	111	-
G W Maxwell	-	25
Total aggregate emoluments	<u>779</u>	<u>423</u>

Aggregate remuneration of each of the independent non-executive directors:

	Year ended Dec 2003 £000	9 month period ended Dec 2002 £000
C Bowe	38	25
P T Warry	28	19
S Slipman	28	19
Total aggregate emoluments	<u>94</u>	<u>63</u>

#### Highest paid director

The highest paid director was J R Sexton. In addition to the aggregate emoluments disclosed above, J R Sexton had accrued pension benefits of £87,881 at 31 December 2003 (31 December 2002: £64,376).

# Thames Water Utilities Limited

## Notes to the financial statements

### Non-executive Chairman

The above details of directors' remuneration do not include W J Alexander, who was remunerated by RWE Thames Water plc in respect of his services to the Division as a whole. Details of his remuneration are disclosed in the financial statements of RWE Thames Water plc.

### Other non-executive directors

S C Walker is remunerated by RWE Thames Water plc in respect of his services to the Division as a whole, as RWE Thames Water Division Investment Director. S C Walker is not remunerated in respect of his role as a non-executive director of the Company, accordingly, his remuneration is not disclosed in the aggregate disclosures above.

### Managing Director RWE Thames Water Europe

W U Böttcher is remunerated by RWE Thames Water plc in respect of his services to the Division as a whole. The remuneration disclosed above, represents the appropriate proportion of his remuneration in respect of services to the Company. Details of his remuneration in respect of services to other areas of the Division are disclosed in the financial statements of RWE Thames Water plc.

### Transactions with directors and officers

There are no transactions or arrangements, which are required to be disclosed under the provisions of the Companies Act 1985.

### Employee information

The average number of persons employed by the Company, including executive directors, analysed by class of business was:

	Year ended Dec 2003 Number	9 month period ended Dec 2002 Number
Water supply	2,543	2,663
Sewerage services	<u>2,262</u>	<u>2,473</u>
Total	<u>4,805</u>	<u>5,136</u>

Employment costs including executive directors' remuneration were:

	Year ended Dec 2003 £m	9 month period ended Dec 2002 £m
Salaries and wages	136.2	104.7
Social security costs	11.7	8.8
Pension costs (note 23)	<u>13.0</u>	<u>-</u>
Total	160.9	113.5
Employment costs included within research and development costs	<u>(3.5)</u>	<u>(2.2)</u>
Net employment costs	<u>157.4</u>	<u>111.3</u>



# Thames Water Utilities Limited

## Notes to the financial statements

### 6 Interest

	Year ended Dec 2003 £m	9 month period ended Dec 2002 £m
Bank loans, overdrafts and other loans:		
- group loans	(80.8)	(51.9)
- bank loans	(36.4)	(24.7)
- other loans	(1.5)	(5.0)
Finance charges in respect of finance leases	<u>(9.9)</u>	<u>(8.2)</u>
Interest payable and similar charges	(128.6)	(89.8)
Interest receivable	<u>3.5</u>	<u>2.3</u>
Net interest	<u>(125.1)</u>	<u>(87.5)</u>

### 7 Taxation

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

		Year ended Dec 2003 £m	9 month period ended Dec 2002 £m
Current year:			
Amounts payable in respect of corporation tax for the period		22.1	-
Amounts payable in respect of group relief		-	2.7
Adjustments in respect of previous periods		<u>0.4</u>	<u>2.8</u>
Total current tax	7(b)	<u>22.5</u>	<u>5.5</u>
Deferred tax:			
Origination and reversal of timing differences	16	52.1	55.2
Adjustments in respect of previous periods		<u>-</u>	<u>(2.7)</u>
Total deferred tax		<u>52.1</u>	<u>52.5</u>
Taxation on profit on ordinary activities		<u>74.6</u>	<u>58.0</u>

# Thames Water Utilities Limited

## Notes to the financial statements

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

The tax charge for the year is lower than the standard rate of corporation tax in the UK (30%). The differences are explained below:

	Year ended Dec 2003 £m	9 month period ended Dec 2002 £m
Profit on ordinary activities before tax	<u>258.6</u>	<u>212.6</u>
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 30% (2002: 30%)	77.6	63.8
Effects of:		
Income not taxable (primarily intra-group disposals of property)	(3.0)	(5.8)
Capital allowances for period in excess of depreciation	(37.7)	(38.1)
Utilisation of tax losses	(14.8)	(17.2)
Adjustments to tax charge in respect of previous periods	<u>0.4</u>	<u>2.8</u>
Current tax charge for the year / period	<u>22.5</u>	<u>5.5</u>

### 8 Dividends

	Year ended Dec 2003 £m	9 month period ended Dec 2002 £m
Interim paid: 4.3p (2002: 4.2p) per ordinary share	44.7	42.8
Second interim proposed: 8.9p (2002: Nil) per ordinary share	91.4	-
Final proposed: Nil (2002: 8.6p) per ordinary share	<u>-</u>	<u>88.1</u>
	<u>136.1</u>	<u>130.9</u>

# Thames Water Utilities Limited

## Notes to the financial statements

### 9 Tangible fixed assets

	Land & buildings £m	Plant and equipment £m	Infrastructure assets £m	Total £m
<b>Cost</b>				
At 1 January 2003	1,796.1	2,414.2	2,601.4	6,811.7
Additions	132.2	239.2	234.3	605.7
Disposals	(1.1)	(38.5)	-	(39.6)
<b>At 31 December 2003</b>	<b>1,927.2</b>	<b>2,614.9</b>	<b>2,835.7</b>	<b>7,377.8</b>
<b>Capital contributions</b>				
At 1 January 2003	-	-	340.5	340.5
Additions	-	-	37.9	37.9
<b>At 31 December 2003</b>	<b>-</b>	<b>-</b>	<b>378.4</b>	<b>378.4</b>
<b>Depreciation</b>				
At 1 January 2003	425.6	905.5	513.5	1,844.6
Provided during the year	29.8	170.8	68.1	268.7
Disposals	(0.2)	(38.3)	-	(38.5)
<b>At 31 December 2003</b>	<b>455.2</b>	<b>1,038.0</b>	<b>581.6</b>	<b>2,074.8</b>
<b>Net Book Value</b>				
At 31 December 2003	<b>1,472.0</b>	<b>1,576.9</b>	<b>1,875.7</b>	<b>4,924.6</b>
At 31 December 2002	1,370.5	1,508.7	1,747.4	4,626.6

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

	Dec 2003 £m	Dec 2002 £m
Freehold land and buildings	1,447.7	1,345.6
Leasehold - over 50 years	8.8	9.0
- under 50 years	15.5	15.9
	<b>1,472.0</b>	<b>1,370.5</b>

Depreciation has not been charged on freehold and leasehold land stated in the accounts at cost of £30.6m (2002: £8.7m).

Tangible fixed assets at 31 December 2003 include assets in the course of construction of £678.6m (2002: £638.8m).

# Thames Water Utilities Limited

## Notes to the financial statements

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

	Cost		Net book value	
	Dec 2003 £m	Dec 2002 £m	Dec 2003 £m	Dec 2002 £m
Plant and equipment	<u>272.5</u>	<u>272.5</u>	<u>196.1</u>	<u>205.2</u>

### 10 Fixed asset investments

	Dec 2003 £m	Dec 2002 £m
Cost of shares in subsidiaries	<u>0.1</u>	<u>0.1</u>

At 31 December 2003 the Company held more than 10% of the allotted share capital of the following undertakings:

Name of undertaking	Nominal value and class of shares held	Proportion of nominal value of issued shares held	Activity
Gemwel Limited	£1 Ordinary	50%	Water and Sewerage Services
Thames Water Drainage Services Limited	£1 Ordinary	100%	Sewerage Management
Thames Water Procurement Limited	£1 Ordinary	100%	Procurement
Thames Water Utilities Finance plc	£1 Ordinary	100%	Finance Company
NPC Realisations Ltd (Formerly New Power Company Limited)	£1 Ordinary	100%	Wholesale of Green Electricity

All of the above companies were incorporated and are registered in Great Britain.

At 31 December 2003 and 31 December 2002 the net asset values of Thames Water Drainage Services Limited and Thames Water Utilities Finance plc were £2 and £50,000 respectively. No profits or losses have been made in either of the periods concerned.

Thames Water Procurement Limited had a deficit on reserves of £1,525,000 at 31 December 2003 (31 December 2002: £1,526,000). Profit for the year ended 31 December 2003: £1,000 (9 months ended 2002: £1,000).

Gemwel Limited has a statutory accounting reference date of 31 March. At 31 March 2003 there was a deficit on reserves of £75,000 (31 March 2002: £232,000). Profit for the year ended 31 March 2003: £157,000 (2002: £46,000).

During the year the Company acquired a further 50% of the share capital of New Power Company Limited for the sum of £1. Subsequently New Power Company Limited changed its name to NPC Realisations Limited. At 31 December 2003 NPC Realisations Limited had a deficit on reserves of £3.5m (31 December 2002: £3.5m).

# Thames Water Utilities Limited

## Notes to the financial statements

Since 31 December 2003 the Company has begun taking steps to liquidate NPC Realisations Limited on a solvent basis. The cost to Thames Water Utilities Limited of liquidating NPC Realisations Limited is not significant and has been fully provided for in the financial statements of the Company as at 31 December 2003.

### 11 Stocks and work in progress

	Dec 2003 £m	Dec 2002 £m
Raw materials and consumables	<u>5.8</u>	<u>8.3</u>

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

	Dec 2003 £m	Dec 2002 £m
Trade debtors	172.9	192.5
Amounts owed by group undertakings	46.6	57.6
Other debtors	19.2	18.7
Insurance claims receivable	48.1	41.8
Prepayments and accrued income	<u>155.1</u>	<u>152.7</u>
	<u>441.9</u>	<u>463.3</u>

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

	Dec 2003 £m	Dec 2002 £m
Bank loans	45.2	44.2
Bank overdrafts	21.4	-
Other loans	-	32.5
Obligations under finance leases	6.6	5.4
Trade creditors:		
- Operating	87.6	43.6
- Capital	125.7	114.5
Amounts owed to group undertakings	482.0	379.6
Insurance claims payable	48.1	41.8
Amounts payable in respect of corporation tax	9.8	-
Amounts payable in respect of group relief	7.0	6.5
Other taxation and social security payable	4.4	4.3
Accruals and deferred income	338.4	294.3
Proposed dividend	<u>91.4</u>	<u>88.1</u>
Total	<u>1,267.6</u>	<u>1,054.8</u>

Amounts owed to group undertakings includes interest bearing loans, which are described in more detail in note 14.

# Thames Water Utilities Limited

## Notes to the financial statements

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

	Dec 2003 £m	Dec 2002 £m
Bank loans	418.6	466.3
Obligations under finance leases	233.5	240.1
Amounts owed to group undertakings (see below)	1,034.1	1,030.2
Accruals and deferred income	<u>98.5</u>	<u>87.6</u>
Total	<u>1,784.7</u>	<u>1,824.2</u>

#### Amounts owed to group undertakings are:

	Dec 2003 £m	Dec 2002 £m
Inter company loans:		
- Within one year	429.6	320.2
- After more than one year	<u>1,034.1</u>	<u>1,030.2</u>
	1,463.7	1,350.4
Non-loan amounts due within one year	<u>52.4</u>	<u>59.4</u>
	<u>1,516.1</u>	<u>1,409.8</u>

Loan amounts owed to group undertakings, are comprised of:

- £225.0m (December 2002: £225.0m) owed to RWE Finance BV, a subsidiary of RWE AG, the ultimate parent undertaking, in respect of a fixed rate loan, due for repayment in 2021.
- £424.6m (December 2002: £223.9m) due to RWE Thames Water plc, the immediate parent undertaking, in respect of a floating rate loan wholly repayable within one year.
- £814.1m (December 2002: £901.5m) owed to Thames Water Utilities Finance plc, a subsidiary undertaking, of which £5.0m (December 2002: £96.3m) is included within creditors due within one year and £809.1m (December 2002: £805.2m) within creditors due after more than one year.

The loan from Thames Water Utilities Finance plc relates to Guaranteed Bonds that it has in issue, the net proceeds of which have been loaned to Thames Water Utilities Ltd under the same commercial terms. Thames Water Utilities Ltd has guaranteed the principal and interest payments of the subsidiary undertaking due under the terms of the bonds.

#### Other loans and finance leases, as disclosed in more detail in note 15, are:

	Dec 2003 £m	Dec 2002 £m
Inter company loans (as above)	1,463.7	1,350.4
Other loans:		
- Within one year	-	32.5
Finance leases:		
- Within one year	6.6	5.4
- After more than one year	<u>233.5</u>	<u>240.1</u>
	<u>1,703.8</u>	<u>1,628.4</u>

# Thames Water Utilities Limited

## Notes to the financial statements

### 15 Financial instruments

FRS 13 requires the disclosure of the funding and treasury policy together with further details on financial assets and liabilities.

#### Funding and treasury policy

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

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

The Company's treasury operations are managed centrally by a small specialist team within the RWE Thames Water Division and are managed as a cost, not a profit centre; no material open or speculative positions are taken.

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

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

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

#### Financial liabilities

	Total at floating rates		Total at fixed rates		Total at book value		Fixed rate liabilities			
							Weighted average interest rate		Weighted average period until maturity for which rate is fixed	
	Dec 2003	Dec 2002	Dec 2003	Dec 2002	Dec 2003	Dec 2002	Dec 2003	Dec 2002	Dec 2003	Dec 2002
	£m	£m	£m	£m	£m	£m	%	%	Years	Years
Bank loans & overdraft										
- £ Sterling	69.2	130.0	416.0	380.5	485.2	510.5	7.4	7.1	5.7	5.5
Other loans & finance leases										
- £ Sterling	846.3	742.5	857.5	885.9	1,703.8	1,628.4	6.2	6.1	21.2	21.5
Total	915.5	872.5	1,273.5	1,266.4	2,189.0	2,138.9	6.6	6.4	16.1	16.7

The Company's interest rate swaps convert £56.0m (2002: £69.7m) of floating rate borrowing to fixed rate and £26.6m (2002: £25.9m) of fixed rate borrowing to floating rate. Cross currency swaps hedge currency risk on £97.4m (2002: £106.4m) of foreign currency borrowing through conversion to Sterling.

Short term lending bears interest at rates linked to LIBOR.

# Thames Water Utilities Limited

## Notes to the financial statements

### Financial assets

	Total at floating rates		Total at fixed rates		Total at book value	
	Dec	Dec	Dec	Dec	Dec	Dec
	2003 £m	2002 £m	2003 £m	2002 £m	2003 £m	2002 £m
Cash at bank/hand						
- Sterling	-	0.8	-	-	-	0.8
Total	-	0.8	-	-	-	0.8

Base rate is the benchmark rate for all cash at bank.

### Currency risk

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

### Fair values

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

	Book value	Book value	Fair value	Fair value
	Dec	Dec	Dec	Dec
	2003 £m	2002 £m	2003 £m	2002 £m
<b>Primary financial instruments</b>				
Financial assets				
- Cash at bank/hand	-	0.8	-	0.8
Financial liabilities				
- Bank loans	(466.5)	(510.5)	(497.6)	(539.9)
- Overdrafts	(21.4)		(21.4)	
- Other loans & finance leases	(1,703.7)	(1,628.4)	(1,810.9)	(1,830.3)
<b>Derivative financial instruments</b>				
- Interest rate swaps	2.6	-	4.0	1.9
- Cross currency swaps	-	-	8.3	13.0
Total	<u>(2,189.0)</u>	<u>(2,138.1)</u>	<u>(2,317.6)</u>	<u>(2,354.5)</u>

Primary financial instruments include bonds, which are traded on a public market. Fair values for these have been calculated using the 31 December 2003 quoted prices. Mark to market techniques (discounting expected cashflows at prevailing interest and exchange rates) are employed in computing fair values for the remaining fixed rate borrowing and all derivative financial instruments. Floating rate liabilities have fair values, which approximate to book value.

Book values of primary financial instruments are shown gross of the effect of any hedging instrument. Therefore, the effect of revaluing foreign currency borrowing at closing rates is included in the fair valuation.



# Thames Water Utilities Limited

## Notes to the financial statements

### Maturities

	Dec 2003 £m	Dec 2002 £m
Bank loans and overdrafts		
- Within one year	66.6	44.2
- Between one and two years	17.0	45.2
- Between two and five years	106.3	91.1
- After more than five years	<u>295.3</u>	<u>330.0</u>
	<u>485.2</u>	<u>510.5</u>
Other loans and finance leases		
- Within one year	436.2	358.1
- Between one and two years	8.1	11.9
- Between two and five years	69.3	42.8
- After more than five years	<u>1,190.2</u>	<u>1,215.6</u>
	<u>1,703.8</u>	<u>1,628.4</u>
<b>Total borrowing</b>	<u><b>2,189.0</b></u>	<u><b>2,138.9</b></u>

- Loans are repayable between 2003 and 2032.
- Loans wholly repayable after more than five years are:

	Dec 2003 £m	Dec 2002 £m
Bank Loans	295.3	325.0
Other Loans	<u>998.8</u>	<u>1,011.9</u>
	<u><b>1,294.1</b></u>	<u><b>1,336.9</b></u>

- Other loans include:
  - £330m 6.75% MTN Eurobonds due 2028.
  - £200m 6.50% MTN Eurobonds due 2032.
  - £175m 3.375% index-linked bond due 2021.
  - £225m 6.60% inter company loan from parent undertaking due 2021.
- Loans repayable by instalments after more than five years hence are:

	Dec 2003 £m	Dec 2002 £m
Bank loans	-	5.0
Finance leases	<u>191.4</u>	<u>203.7</u>
	<u><b>191.4</b></u>	<u><b>208.7</b></u>

- The ranges of interest rates on outstanding bank loans are 2.3% to 11.5% (2002: 5.4% to 11.5%) and other loans and finance leases, are 1.7% to 6.8% (2002: 1.7% to 6.8%).

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

# Thames Water Utilities Limited

## Notes to the financial statements

### Borrowing facilities

The Company has committed borrowing facilities with a range of financial institutions totalling £150m (2002: £220m), expiring as below. At 31 December 2003 and 31 December 2002, no funds have been borrowed.

	Dec 2003 £m	Dec 2002 £m
<b>Expiring:</b>		
Within one year	<u>150.0</u>	<u>220.0</u>

Thames Water Utilities Finance plc also has a US\$ 4 billion (December 2002: US\$ 4 billion) uncommitted Euro-Medium Term Note programme, which provides the Company with access to the capital markets in a range of currencies and maturities. At 31 December 2003, outstanding debt obligations of Thames Water Utilities Finance plc were £814.0m (December 2002: £907.6m), with a weighted average term of 22.7 years (December 2002: 20.2 years) at a weighted averaged rate of 6.05% (December 2002: 5.68%).

### 16 Provision for liabilities and charges

Provision for liabilities and charges consist entirely of a provision for deferred taxation, there are no amounts of deferred tax unprovided (2002: £nil).

#### The movement in the provision was as follows:

	Note	Dec 2003 £m
Provision brought forward at 1 January 2003		744.9
Deferred tax charge:		
- Current year	7(a)	<u>52.1</u>
Provision carried forward at 31 December 2003		<u>797.0</u>

#### An analysis of amounts provided at current tax rates is as follows:

	Dec 2003 £m	Dec 2002 £m
Accelerated capital allowances	804.5	754.6
Tax losses carried forward	-	(5.6)
Other timing differences	<u>(7.5)</u>	<u>(4.1)</u>
	<u>797.0</u>	<u>744.9</u>

# Thames Water Utilities Limited

## Notes to the financial statements

### 17 Share capital

	Dec 2003 £m	Dec 2002 £m
<b>Authorised</b>		
1,029,050,000 (2002: 1,029,050,000) ordinary shares of £1 each	<u>1,029.0</u>	<u>1,029.0</u>
<b>Allotted, called up and fully paid</b>		
1,029,050,000 (2002: 1,029,050,000) ordinary shares of £1 each	<u>1,029.0</u>	<u>1,029.0</u>

### 18 Share premium reserve

	Dec 2003 £m	Dec 2002 £m
Premium of 25p on issue of 400 million £1 ordinary shares	<u>100.0</u>	<u>100.0</u>

### 19 Profit and loss account

	£m
At 1 January 2003	346.2
Profit for the year	<u>47.9</u>
At 31 December 2003	<u>394.1</u>

### 20 Reconciliation of movements in shareholders' funds

	Dec 2003 £m	Dec 2002 £m
Profit for the financial year / period	184.0	154.6
Dividends	<u>(136.1)</u>	<u>(130.9)</u>
Net movement in shareholders' funds	47.9	23.7
Shareholders' funds at 1 January / 1 April	<u>1,475.2</u>	<u>1,451.5</u>
Shareholders' funds at 31 December	<u>1,523.1</u>	<u>1,475.2</u>

# Thames Water Utilities Limited

## Notes to the financial statements

### 21 Capital commitments

	Dec 2003 £m	Dec 2002 £m
Contracted for but not provided	<u>269.1</u>	<u>271.2</u>

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

### 22 Operating leases

At 31 December 2003 the Company was committed to making the following payments during the next year in respect of non-cancellable operating leases:

	Dec 2003		Dec 2002	
	Land and buildings £m	Other £m	Land and buildings £m	Other £m
<b>Leases which expire:</b>				
Within one year	0.4	0.4	-	0.5
Between one and two years	-	0.4	0.4	0.2
Between two and five years	0.2	-	0.2	-
After more than five years	<u>5.7</u>	<u>-</u>	<u>5.7</u>	<u>-</u>
	<u>6.3</u>	<u>0.8</u>	<u>6.3</u>	<u>0.7</u>

### 23 Pension schemes

Pension arrangements for the majority of the Company's employees are of the defined benefit type, funded through pension schemes covering employees within the RWE Thames Water Group, whose assets are held separately from those of the Group in independently administered funds. In addition, there are unfunded defined benefits provided for directors and senior employees affected by the cap on earnings, which cannot be provided through approved arrangements.

The Company's pension arrangements are of the group multi-employer scheme nature, such that the Company's pension schemes assets and liabilities cannot be separately identified on a reasonable and consistent basis, from those of the RWE Thames Water Group. Accordingly, the Company has made the appropriate FRS 17 transitional disclosures, required of a company with group multi-employer pension schemes. It is not anticipated that full adoption of FRS 17 will become mandatory for accounting periods ending before 1<sup>st</sup> January 2005, until then the transitional arrangements will apply.

# Thames Water Utilities Limited

## Notes to the financial statements

### SSAP 24

Details of the actuarial position of the Group pension schemes are given in the financial statements of RWE Thames Water plc, for the year ended 31 December 2003. The key assumptions for the UK schemes are set out below:

Method	Projected unit method for schemes open to new Attained age method for closed scheme.
Interest rate	5.8% pa
Earnings increases	3.7% pa
Pension increases	2.7% pa
Asset valuation	Market value
Regular cost	£18.4m
Variation cost	(£2.6m)
Interest cost	(£0.8m)

The latest full actuarial valuation was undertaken at 31 December 2001. Scheme assets at that date amounted to £947m and this represents 123% of the value of benefits accrued to members as at 31 December 2001.

An interim valuation was undertaken at 31 August 2003. Scheme assets at that date amounted to £863m and this represents 100% of the value of benefits accrued to members as at 31 August 2003.

During the year the Company made company contributions of £7.9m (9 month period ended 2002: £4.0m) into the Company's pension schemes for the benefit of members.

The total ongoing pension cost for the Company during the year ended 31 December 2003 was £13.0m (9 month period ended December 2002: £nil). The pension cost is assessed in accordance with advice received from Hewitt, Bacon and Woodrow, the independent and professionally qualified consulting actuaries to the schemes. The SSAP 24 pension cost has increased following the interim valuation undertaken at 31 August 2003, which indicated a reduced pension surplus.

The regular cost of benefits amounted to £16.7m (2002: £15.7m) and the actuarial surplus resulted in a variation amounting to a reduction in the pension cost of £3.7m (2002: £15.7m).

At 31 December 2003 a prepayment in respect of the funded schemes amounting to £6.4m was included in debtors. At 31 December 2002, £11.5m was included in debtors.

In addition to the ongoing cost of the UK Pension arrangements, the Company operates discretionary arrangements under which it augments benefits on retirement. These augmentations are funded by way of additional employer contributions to the schemes. In the year ended 31 December 2003 payments amounted to £0.6m (9 month period ended Dec 2002: £0.6m).

### FRS 17

Information on the Group schemes is disclosed in accordance with FRS 17 in the RWE Thames Water plc Group accounts, prepared for year ended 31 December 2003.

# Thames Water Utilities Limited

## Notes to the financial statements

The latest full actuarial valuation was undertaken as at December 2001. At this date, the Group schemes were in surplus to the extent of £143.3m. An Interim valuation was undertaken at 31 August 2003.

The next full actuarial valuation will be as at 31 December 2004.

The December 2001 valuation has been updated at 31 December 2003 by Hewitt, Bacon and Woodrow (the independent and professionally qualified consulting actuaries to the schemes), using revised assumptions that are consistent with the requirements of FRS 17 and shown in the table below. At this date, the Group schemes were in deficit to the extent of £35.2m (2002: £63.1m).

The main financial assumptions for the UK schemes used for FRS 17 purposes are shown in the following table:

Price inflation	2.8%
Salary increases	3.8%
Pension increases	2.7%
Discount rate for scheme liabilities	5.40%

RWE Thames Water Group has taken advice from Hewitt, Bacon and Woodrow in respect of the *funding position of the group pension schemes*. The FRS 17 deficit does not have a direct impact on funding. With consideration of the funding position of the schemes, the company contribution rate has been increased where necessary in accordance with Hewitt, Bacon and Woodrow recommendations.

### **24 Ultimate parent company and controlling party**

The ultimate parent company and controlling party is RWE AG, a company incorporated in Germany.

Copies of the consolidated financial statements of the immediate parent company, RWE Thames Water plc may be obtained from The Company Secretary, RWE Thames Water plc, 14 Cavendish Place, London W1M 0NU.

Copies of the ultimate parent company's accounts may be obtained from RWE Aktiengesellschaft, Opernplatz 1, D-45128 Essen, Germany.