Company No 2366616

Annual Report & Accounts

2007

United Utilities

We are one of the largest operators of water and wastewater systems in the UK. We provide operations and maintenance and shared services activities to Dŵr Cymru Welsh Water and are helping to deliver capital investment programmes for Scottish Water and Southern Water throughout their operational areas.

We own and operate an electricity network, operate a gas network and provide multi-utility metering and connections services.

-ocus on core skills delivers ɔerformance improvements

- Underlying profit before tax from continuing operations* up 15 9 per cent to £561 4 million
- United Utilities North West segmental operating profit increased by 17 7 per cent to £750 1 million, with underlying profit* up 11 1 per cent to £736 3 million
- £747 9 million capital expenditure in United Utilities North West in the year to improve services to customers including infrastructure renewals expenditure of £101 2 million
- Strategic focus on core skills of managing water, wastewater, electricity and gas networks
- Operational performance improvements delivered for customers
- Customer satisfaction for water and wastewater customers at a three-year high
- First UK water company to announce an action plan to reduce carbon emissions
- Asset owner/operator management reorganisation implemented to generate higher performance
- £10 0 million of annual cost savings expected from management reorganisation

Sale process initiated for United Utilities' electricity distribution assets

- Focus on the much larger water asset base which offers significantly more growth potential
- Expect to return to shareholders the net equity proceeds from the potential sale
- Capital structure and dividend policy to be reviewed at the end of the sale process, recognising the importance of income to our shareholders
- Board's intention is that shareholders will realise total distributions over the remainder of the 2005-10 price control period at least equivalent to the distributions targeted for the same period under the current dividend policy
- Target a credit rating to best mirror regulatory assumptions for United Utilities Water
- Intend to continue to operate electricity assets, consistent with core skills strategy

*** Underlying profit measures are defined and reconciled to the group's income statement on pages 24 and 25**

Contents

The following key performance indicators (KPIs) are the principal measures used by the board to assess the group's performance

	2006/07	2005/06
Financial		
Revenue from continuing operations	**£2,323 0m**	£2,086 0m
Operating profit from continuing operations	**£827 5m**	£729 5m
Underlying operating profit from continuing operations*	**£816 0m**	£752 9m
Profit before taxation from continuing operations	**£676 0m**	£445 1m
Underlying profit before taxation from continuing operations*	**£561 4m**	£484 4m
Total dividends per ordinary share	**44 93p**	43 87p
Basic earnings per share from continuing operations	**57 1p**	37 8p
Basic earnings per share from continuing and discontinued operations	**49 4p**	24 3p
Environment		
Pollution incidents	**9**	23
Carbon management – renewable energy generated	**78 6GWh**	76 6GWh
Water quality – OPI water quality index	**99 84**	99 84
Employees		
Employee satisfaction – employee opinion survey	**69%**	74%
Health and safety – accident incident rate	**498**	548
Health and safety – cumulative accident-related lost time rate	**9,052**	11,564
Customers		
Water – relative efficiency	**Band B**	Band C
Wastewater – relative efficiency	**Band C**	Band D
Security of water supply – rolling annual average leakage	**468 Ml/d**	477 Ml/d
Sewer flooding – number of properties removed from the at-risk register	**152**	237
Electricity – customer minutes lost	**56 68**	51 52
Electricity – customer interruptions	**53 89**	47 50
Overall customer satisfaction – water	**74%**	48%
Overall customer satisfaction – electricity	**69%**	70%
Written complaints	**24,193**	29,842

Notes

Electricity distribution business is treated as a continuing operation in the above results

Underlying profit measures are defined and reconciled to the group's income statement on pages 24 and 25

Business review

Definitions of the key performance indicators

Financial

Revenue from continuing operations
- A definition of revenue is included in accounting policies note (p)

Operating profit from continuing operations
- A definition of operating profit is included in accounting policies note (k)

Underlying operating profit from continuing operations*
- Operating profit from continuing operations excluding restructuring costs and other significant non-recurring items
- The board considers that the removal of the impact of restructuring costs and other significant non-recurring items gives a clearer understanding of the underlying trading performance
- A full reconciliation of this figure to operating profit from continuing operations can be found in the non-GAAP measures section in tables 5 and 6 on page 25

Profit before taxation from continuing operations
- This measure deducts all expenses from revenue including finance expenses and operating expenses, but excludes the taxation charge

Underlying profit before taxation from continuing operations*
- Profit before taxation from continuing operations before share of results of associated company and excluding restructuring costs and other significant non recurring items
- Adjusted to exclude fair value movements on debt and derivative instruments
- The board considers that the removal of the impact of restructuring costs and other significant non recurring items gives a clearer understanding of the underlying performance
- A full reconciliation of this figure to profit before taxation from continuing operations can be found in the non-GAAP measures section in table 7 on page 25

Dividends per ordinary share
- Amount of dividend declared per ordinary share for the year expressed in pence See note 8 to the financial statements for a further analysis of dividends per share

Basic earnings per share
- Basic earnings per share is calculated by dividing profit for the year attributable to equity holders of the company by the weighted average number of shares in issue See note 9 to the financial statements for a further analysis of earnings per share

Environment

Pollution incidents
- Number of category 1 and 2 incidents incurred during the year as defined by the Environment Agency Figures stated are for the years to December 2006 and December 2005

Carbon management
- Number of gigawatt-hours of renewable energy generated by United Utilities North West in the year Figures stated are for the years to December 2006 and December 2005

Water quality
- The Operational Performance Index (OPI) is calculated by the Drinking Water Inspectorate as a means of monitoring water quality It is based on an average of the mean zonal compliance for six water quality parameters (iron, manganese, aluminium, turbidity, E coli, trihalomethanes) as measured at customers' taps Figures stated are for the years to December 2006 and December 2005

Employees

Employee satisfaction – employee opinion survey
- Percentage of employees satisfied with their current job as measured by the annual employee survey

Health and safety – accident incident rate
- This is the number of lost time accidents in the year pro rated to produce a rate per 100 000 employees

Health and safety – cumulative accident related lost time rate
- Cumulative accident-related lost time rate per 100 000 employees

Customers

Relative efficiency
- Operating expenditure relative efficiency band as assessed by Ofwat for the years to December 2006 and December 2005

Security of water supply – rolling annual average leakage (Ml/d)
- Annual rolling leakage – figures given are in megalitres per day for the years to December 2006 and December 2005

Sewer flooding
- Total number of properties removed from the sewer flooding register during the year The register records properties at risk of experiencing one sewer flooding incident in ten years

Customer minutes lost
- A standard measure of network reliability used by Ofgem which is the sum of customer minutes lost for all restoration stages for all incidents divided by the number of connected customers as at 30 September each year

Customer interruptions
- A standard measure of network reliability used by Ofgem This represents the number of interruptions per 100 customers and is calculated as (total customers affected/total customers connected to the network) x 100

Overall customer satisfaction
- The business has an internal overall customer experience assessment mechanism which measures the level of customer satisfaction in relation to the response received from an enquiry It involves a series of interviews with customers Sample interviews are conducted monthly

Written complaints
- Total number of written complaints received by United Utilities North West businesses

We are committed to listening and responding to all our stakeholders

People

The board is pleased to report another good set of financial results We would like to thank our employees for making this possible through their continuing hard work and loyalty

The board was saddened by the death of Gordon Waters in December 2006 Gordon led our Contract Solutions business and worked closely with the Carbon Trust We feel he would have approved of our decision to put carbon management high on our agenda

In March, we completed the sale of Vertex to a consortium led by Oak Hill Capital Partners in line with our strategy of focusing on our core skills Tom Drury left the board as a result, and we wish him well for the future

We have strengthened our team with two recent appointments We welcome Dr Catherine Bell to the board as a non-executive director and Paul Capell as our business development director We say a fond farewell to Sir Peter Middleton, who will retire at the annual general meeting after 13 years as a non-executive director I thank him on behalf of the board for his substantial contribution Nick Salmon will replace Sir Peter as senior independent director

Performance

Revenue from continuing operations rose 11 4 per cent to £2,323 0 million, principally reflecting growth in United Utilities North West Operating profit from continuing operations increased to £827 5 million, up 13 4 per cent on last year

The board is proposing a final dividend in respect of the year ended 31 March 2007 of 30 30 pence per ordinary share This is an increase of 2 4 per cent, consistent with the group's policy of growing dividends in line with inflation Together with the interim dividend of 14 63 pence per ordinary share, the total ordinary dividend relating to the year is 44 93 pence The final dividend of 30 30 pence will be paid to shareholders on 24 August 2007

Where things have gone wrong we have worked hard to address and improve them You will have seen that our regulator, Ofwat, has imposed a penalty of £8 5 million because it concluded that we did not conduct certain internal trading arrangements on an arm's length basis This was a disappointment to us and we have taken all appropriate steps to remedy the matter Our decision to restructure the business, focus on core skills and sharpen our commercial discipline has also helped, it gives greater visibility and accountability to the different parts of our business

Outlook

By focusing on core skills, the business is well placed to meet expectations for the forthcoming financial year With predictable regulated revenue increases ahead, the board expects United Utilities to continue to deliver strong profit growth

We hope you enjoy reading this report and continue to share in our company's success

Dick Evans
Chairman

Our vision is to be a world class operator of utility infrastructure

During the last 12 months we have started a journey towards becoming 'a world class operator of utility infrastructure' through a rigorous focus on our core business We would like to thank all our stakeholders for their support, especially our 9,000 colleagues

We are already seeing some improvement in meeting our leakage performance target set by Ofwat and in higher improved customer satisfaction levels Although we have made a good start, much further progress is needed

When I arrived at United Utilities in February last year, I found a business with many positive attributes an ethos of commitment to service, a large customer base, and services that everybody needs

However, our customer satisfaction levels should have been better and we were not meeting all our regulatory targets I felt these issues sprang from a lack of commercial focus in the business, resulting from a diffused portfolio and a culture without the sharpness that competition provides

A new vision and values

Our first task was to create a clear vision and set of values We sought the full involvement of the business at every level through a series of workshops and other routes and developed our values together We have defined them as 'team, trust, passion and commitment'

Our vision to become world class would be meaningless, however, without a means of measuring our performance against a peer group of world class companies We have implemented a scorecard that provides a high level comparison of our progress against respected international companies in utility and wider corporate industries

It was equally important to create a new streamlined structure that would enable improved performance by focusing on what we do best We are concentrating all our resources on our core competencies in operating water, wastewater, electricity and gas infrastructure Our new structure will help us to share best practice, knowledge and skills across the group

We sold Vertex and brought the call centre customer management services that Vertex provided for us in-house We also have a contract with Accenture to provide back office services We believe these arrangements will deliver a better service to our customers

Changing the structure of an organisation is comparatively straightforward, even for a business as large as United Utilities It is far more challenging to create a culture that allows and motivates people to behave differently

We are placing a greater emphasis on leadership at every level, authentic leadership that inspires people and sets a positive example

The challenge facing us is to retain the valuable ethos of duty and commitment within United Utilities, while commercialising our culture to sharpen performance Part of the solution is to open the entire organisation to the competitive atmosphere that our non-regulated business is used to

Today, internal measurements of customer satisfaction across water, wastewater, billing and collection have risen from a benchmark score of 48 per cent to 74 per cent This follows the introduction of popular new practices such as two-hour appointment windows and Sunday working

Many of these improvements have come through innovative thinking Thermal imaging equipment, for example, is helping us to predict potential plant and equipment failures so we can spot and fix weaknesses before they cause problems

Mobile laser technology is helping to ensure the alignment of our clean water pumps, an investment that is reducing energy use and extending their life

Carbon emissions

United Utilities is the first UK water company to set out an action plan to reduce its carbon emissions The group's electricity consumption has almost doubled since privatisation, as a result of delivering environmental and customer improvements and this plan is actually targeting a reversal in the rising trend of carbon emissions We have developed a cost-effective programme after working closely with the Carbon Trust to maximise our contribution in tackling climate change

Our carbon investment programme is estimated at around £37 million, with an expected three to five-year payback period We are targeting a gross reduction in carbon emissions of around 26 per cent in the medium-term, with approximately eight per cent to come from our internal carbon reduction plans and around 18 per cent via renewable energy supply contracts Harvesting sustainable energy from wastewater treatment processes is a key element in meeting this target and we now have close to a quarter of the UK's sewage gas combined heat and power plants

Planning for the long term

We are initiating a sale process for our electricity distribution assets, with a view to maximising shareholder value Our water business represents over 85 per cent of the group's regulatory asset value and we believe that shareholders' interests are best served by our focusing on the much larger water asset base, which offers significantly more growth potential than our electricity assets

Changes now in place are already giving us greater clarity on our future capital investment programme, which will see us spend approximately £2,300 million improving our infrastructure over the next three years We will bring the costs of customer service in line with industry standards, on the principle that delivering a good, 'right-first-time' service is the most efficient possible solution

Philip Green
Chief executive

Our business today

Restructuring will improve performance and lead to more commercial behaviour

Business description
United Utilities PLC is a public limited company registered in England and Wales Its asset owning operations, comprising United Utilities Water PLC (UUW) and United Utilities Electricity PLC (UUE), hold licences to provide water and wastewater services and electricity distribution services, respectively, to a population of some seven million people in north west England United Utilities Contract Solutions applies the group's expertise in operating utility infrastructure to competitive markets and is now the leading utility outsourcing business in the United Kingdom

History
United Utilities PLC (then known as North West Water Group PLC) was incorporated on 1 April 1989 under the Companies Act 1985 along with its subsidiary United Utilities Water PLC (then known as North West Water Limited) In November 1995, the company acquired UUE (then known as NORWEB plc), the distributor of electricity in north west England and, at that time, a supplier of electricity and gas in the United Kingdom

In August 2000, the company sold the electricity and gas supply business and, as a result, no longer has any significant exposure to the competitive energy generation and supply market In February 2006, the company disposed of its telecommunications business, Your Communications, to THUS Group plc On 26 March 2007, the business process outsourcing business, Vertex, was sold to a consortium of US-based private equity firms led by Oak Hill Capital Partners

Segmental reporting
The group reports through two business segments United Utilities North West and United Utilities Contract Solutions

United Utilities North West
United Utilities North West comprises the regulated monopoly activities of UUW (water and wastewater) and UUE (electricity distribution) These companies own the respective infrastructure network assets representing 87 3 per cent of the group's segmental assets at 31 March 2007 The businesses are capital intensive and are subject to economic, quality and environmental regulation

These businesses generated 90 6 per cent of the group's operating profit from continuing operations in 2006/07, of which approximately three quarters is derived from water and wastewater and approximately one quarter from electricity distribution

United Utilities Contract Solutions
United Utilities Contract Solutions applies the group's infrastructure management expertise to competitive markets by providing a service to clients in managing their infrastructure assets In addition, it owns the group's interest in non-regulated utility assets These activities employ only a limited amount of capital, representing 5 1 per cent of the group's segmental assets at 31 March 2007

Other activities
Other activities include United Utilities Property Solutions (UUPS), the property trading and management business of United Utilities PLC, which owns land and property assets UUPS' operating profit for the year was £18 2 million

Business restructuring
Since the end of the financial year, the company has realigned its structure to improve performance and lead to more commercial behaviour

From 1 April 2007, Utility Solutions will manage the operation of all water and wastewater, electricity and gas networks, whether that is on behalf of United Utilities' own businesses or for external clients The Asset Management and Regulation function will develop and deliver the regulatory price review strategy and will engage with key opinion-formers, ministers, regulators and civil servants Finally, the Business Development function will pursue a growth strategy for the group and deliver its international business's financial targets

As part of this reorganisation, the composition and membership of our executive team has been reviewed and a number of roles have been redefined High quality individuals have been recruited and key internal talent has been retained to ensure that the group has the right blend of skills, experience and resources to help the group to become a world class operator of utility infrastructure Six of our nine executive officers and around one quarter of our senior managers are new to the business The Vertex sale reduced the group's workforce by around a half with minimal impact on profitability

With regard to the new business functions, Charlie Cornish, formerly managing director of United Utilities North West, is managing director of Utility Solutions and an executive board member Clive Elphick, formerly policy director, heads Asset Management and Regulation Paul Capell, who joined the group on 1 May 2007 from Veolia, is managing director of Business Development and an executive board member

Sale of electricity distribution assets
As one of the first stages of realigning the existing businesses into the new structure, a new operating entity, United Utilities Electricity Services Limited, has been established This company will focus on the operation and maintenance of the group's electricity assets, currently owned by United Utilities Electricity The board has taken a decision to initiate a sale process for the electricity distribution assets but intends to retain the asset operator function, consistent with its core skills strategy

United Utilities North West

We are treating and distributing around 1.9 billion litres of water and wastewater per day and distributing some 25,800 GWh of electricity annually

United Utilities North West manages the operation of the licensed water and wastewater network assets owned by United Utilities Water, and the electricity distribution assets owned by United Utilities Electricity, in north west England These businesses involve the removal and treatment of wastewater from, and the treatment and distribution of around 1 9 billion litres of water a day to, 3 2 million homes and businesses, and the annual distribution of approximately 25,800 GWh of electricity to 2 4 million consumer premises

Both businesses enjoy monopoly positions in the north west region and they are therefore subject to regulation in terms of price and performance Figures 1 and 2 below show that both the water and electricity businesses operate in what is essentially the same geographical area

UK water market

The water industry is made up of local and regional monopoly companies operating the water and sewerage networks Figure 1 shows the water and sewerage boundary map of the UK Under current legislation, domestic customers have no ability to change their supplier

The Water Services Regulation Authority (Ofwat) is the economic regulator of the water and sewerage industry in England and Wales

UK electricity market

The electricity industry consists of four components generation, transmission, distribution and supply The majority of electricity distribution services are provided by regional distribution companies, each with its own service area These are broadly based on the former electricity board areas (see figure 2 below) The electricity industry is regulated by the Gas and Electricity Markets Authority, which governs and acts through the Office of Gas and Electricity Markets (Ofgem) In the electricity market, suppliers contract with generators (for wholesale power) and with transmission and distribution network businesses (for delivery services) in order that they can provide energy to final consumers

The activities undertaken by United Utilities North West are

- Capital intensive – At privatisation in 1989, the water and wastewater infrastructure inherited by United Utilities Water was in need of substantial repair and replacement Further improvements have been required in order to comply with applicable UK and European Union environmental and drinking water quality regulations Gross capital expenditure relating to water and wastewater in the year ended 31 March 2007 was £570 3 million (2005/06 £440 9 million) 54 5 per cent related to the water and wastewater network and non-infrastructure maintenance programmes, and 45 5 per cent related to the quality and enhancement programme Capital expenditure for the year ended 31 March 2007 relating to electricity distribution was £177 6 million (2005/06 £141 6 million) 44 2 per cent was load related (enabling new connections to be made to the network and increasing the amount of electricity able to be carried), 48 9 per cent was non-load related (for example, replacing assets due to statutory obligations or replacing faulty or ageing equipment) and 6 9 per cent was non-operational (for example, information technology),
- Subject to economic regulation – In general, these businesses are monopolies and are subject to incentive-based economic regulation which imposes caps on increases in customer prices, rewards efficiency and high standards of customer service and penalises inefficiency and poor standards of customer service The economic regulation of wastewater, water and electricity distribution are described in more detail below, and
- Subject to environmental regulations – During the year ended 31 March 2007, the group spent £33 million (2005/06 £43 5 million) on controlling pollution from certain stormwater overflows (known as Unsatisfactory Intermittent Discharges or UIDs) Key outputs for water included the refurbishment of 810 kilometres of old water mains and the replacement of some 2,415 lead communication pipes Water meters were also installed in 39,503 domestic properties under the free meter option scheme, whereby customers can switch to metered billing free of charge Key outputs from the wastewater capital investment programme include addressing 32 UIDs, the modelling of the sewerage system in the City of Lancaster relating to a further ten UIDs, completing three projects relating to AMP3 at wastewater treatment works, and completing six AMP4 wastewater treatment work outputs Furthermore, flow measuring devices were installed at 29 wastewater treatment works with a view to achieving environmental improvements The environmental regulation of water and wastewater is described on pages 12 to 14 and the environmental regulation of electricity distribution is described on pages 16 and 17

The group cannot increase demand materially for its licensed operations within its licensed area and, as detailed below, the group's licensed businesses are restricted in their ability to increase prices

Key outputs for water included the refurbishment of 810 kilometres of old water mains and the replacement of 2,415 lead communication pipes

Customers, billing and debt collection
United Utilities North West places great importance on the customer relationship activities involved in distributing electricity and supplying water and related products and services to homes and businesses in north west England

- Water and wastewater – United Utilities North West manages the sales, billing, cash collection and debt management activities and systems for 3 2 million domestic and business customers and has responsibility for improving the quality of service and the range of services provided to these customers United Utilities North West's aim is to improve continually upon the existing level of customer satisfaction, and to create value from its customer relationships As the Water Industry Act 1999 prevents licensed water utilities from terminating services to customers for non-payment, the effective management of customer relationships is an important factor in controlling bad debts
- Electricity distribution – United Utilities North West distributes electricity to 2 4 million customers' homes and premises on behalf of the supply companies Customers receive their electricity bill from supply companies who pay United Utilities for use of the electricity distribution network The debt management arrangements afforded to United Utilities North West, through its Distribution Connections and Use of System Agreements ensure that the level of bad debt in the electricity distribution business is minimal

In the UK large-user water market (customers consuming more than 50 megalitres of water per annum), UUW's activities include on-site treatment of water and wastewater at customers' premises (working in conjunction with United Utilities Contract Solutions) and advice on both controlling leakage at customers' premises and the recycling of water

Wastewater collection, treatment and disposal operations
In accordance with its licence, United Utilities Water is responsible for the reception, conveyance, treatment and disposal of domestic wastewater, trade effluent (non-domestic wastewater) and surface water in north west England

Surface water, mainly from groundwater, infiltration and highway drainage, forms a major part of the volume of wastewater that must be treated In some cases, separate sewers are provided for foul water and surface water, so that uncontaminated surface water may be piped directly to a watercourse and re-enter the water cycle

Trade effluent accounts for over 25 per cent of the wastewater load requiring treatment This is equivalent to the wastewater produced by a population of 2 4 million over and above the wastewater generated by the actual domestic population in the region of seven million

United Utilities Water's wastewater treatment works provide a range of treatments These include primary, secondary and tertiary treatment involving a variety of physical, chemical and biological processes These ensure the constituents of wastewater are broken down or removed before discharge Fully treated final effluent is discharged into rivers, estuaries or via sea outfalls The Environment Agency consents to and stringently monitors all these discharges to ensure they comply with all relevant limits

A by-product of the treatment of wastewater is sewage sludge, which is treated further to produce an end product that is suitable for recycling Currently, around three quarters of this end product is recycled to agricultural land as a soil conditioner or used in land reclamation, and one quarter is incinerated However, due to increasing environmental pressures, such as the Water Framework Directive and increasing designation of nitrate vulnerable zones (that is, zones that are subject to restrictions in the amount of nitrogen that can be applied to agricultural land), the amount of end product that can be recycled to agricultural land is likely to decrease quite significantly in the short to medium-term, with a corresponding increase in the expected amount to be incinerated

Water supply operations, treatment and distribution

United Utilities Water obtains water from various sources including reservoirs, rivers and aquifers The majority of its reservoirs are in the uplands of the Lake District and the Pennine Hills, areas with a higher than average rainfall Conversely, the major population centres it serves are in the lowlands of Greater Manchester, Lancashire and Cheshire Merseyside, the other major population centre served by United Utilities Water, receives its water supply principally from the River Dee and Lake Vyrnwy in north Wales A large proportion of water supplied by United Utilities Water flows freely by gravity and does not need to be pumped However, due to the nature of the water catchment areas, being peaty moorlands or coal measure strata, enhanced treatment methods are required to ensure the water satisfies all regulatory and quality standards

All water supplied is treated in order to meet the appropriate standards enforced by the Drinking Water Inspectorate, the government regulator of drinking water in England and Wales The type of treatment varies from disinfection only, for some borehole sources, to more complex processes using coagulation, sedimentation, clarification and filtration and activated carbon absorption for certain waters United Utilities Water monitors water quality by analysing samples regularly for both microbiological and chemical parameters United Utilities Water conducts over half a million tests annually at its water treatment works, service reservoirs and at random from customers' domestic taps Overall water quality remains high with 2006 mean zonal compliance at 99 92 per cent compared with 99 94 per cent in 2005

Treated water is delivered to the end customer through a network of large diameter trunk mains to smaller trunk mains, service reservoirs, water towers and distribution mains

Economic regulation of water and wastewater

The water licence

The UK government awarded Instruments of Appointment ('licences') for the provision of wastewater services and water supply in 1989 These licences continue in force for an indefinite period, subject to potential termination rights as set out below United Utilities Water holds the licence for an area of north west England which comprises 3 2 million homes and businesses

The Water Industry Act 1991 (the 'Act'), as amended by the Water Act 2003 (the 'WA 2003'), provides for the appointment (by way of licensing) of water and sewerage undertakers Economic regulation pursuant to these licences is currently the responsibility of the Water Services Regulation Authority (until 31 March 2006, the Director General of Water Services) The Authority continues to be known as 'Ofwat'

Ofwat also exercises powers under UK competition legislation, most significantly the Competition Act 1998 and the Enterprise Act 2002

The WA 2003 is intended to promote greater water conservation and planning for the future by water companies, revise the framework for water abstraction and impounding and help to build a more transparent regulatory environment

Competition in the water industry

The WA 2003 has extended opportunities for competition in the water industry in England and Wales by introducing a new water supply licensing (WSL) regime From 1 December 2005, water supply licensees have been able to provide both retail supply (i e the supply by a licensee of water purchased from a water undertaker's supply system to an eligible customer) and combined supply (i e the introduction of water into an incumbent water company's existing network for retail by the licensee to an eligible customer) to non-household users with an annual consumption of not less than 50 megalitres per year A water undertaker is obliged to allow a licensed water supplier to use its network for this purpose, subject to payment of a fee and certain conditions and rights of refusal

At the date of this report, seven such licences have been granted, including one granted to a subsidiary of United Utilities PLC, United Utilities Water Sales Limited Ofwat has produced guidance for WSL and published a Customer Transfer Protocol to facilitate the transfer of customers to a new licensee In addition, water companies must draw up an access code which they should review annually The development of WSL is being monitored by an advisory group established by Ofwat Ofwat is of the view that the WSL is not delivering effective competition It intends, in the coming months, to make several changes to the system and to its guidance and intends to introduce a requirement on the water companies to publish draft access agreements Ofwat has also advocated legislative change to amend the 'cost principle' (which means that the licensee must pay most of the associated costs) and the 50 megalitres eligibility threshold (which it considers to be too restrictive)

In line with the new WSL regime, from 1 April 2005 the threshold in the Act for an inset appointment (whereby one licensed undertaker replaces another for a specific non-household user) was also reduced from 100 to 50 megalitres per year To date there have been no inset appointments granted which affect United Utilities Water's area United Utilities Water had already developed and published policies which allow other companies access to its water networks in order to supply customers and to lay new water mains and service pipes These policies have been further developed to facilitate competition in the industry under the WA 2003 and the company welcomes the new competitive developments in this field

Ofwat

The establishment of the Water Services Regulation Authority as a regulatory board also brings Ofwat into line with other regulators which have adopted a board structure Appointments to Ofwat are made by the Secretary of State for Environment, Food and Rural Affairs The chairman will continue to be appointed for a fixed term and may only be removed from his post for incapacity or misbehaviour A new independent Consumer Council for Water (the 'Council') has replaced WaterVoice (previously Ofwat's National Customer Council) and the regional Customer Service Committees The Council is accompanied by nine regional committees for England and one for Wales

Ofwat must comply with its statutory duties as set out in the Act It may receive guidance from the UK government in areas such as social and environmental policy and in the performance in these areas of its statutory functions It also receives views from the government on matters such as the approach to price controls However, Ofwat is not subject to direction about what its judgements should be and is independent of government ministers Ofwat must exercise and perform its powers and duties in the manner that it considers is best calculated to

- protect the interests of consumers wherever appropriate by promoting effective competition between persons engaged in, or in commercial activities connected with, the provision of water and sewerage services,
- secure that the functions of a water undertaker and of a sewerage undertaker are properly carried out in respect of every area of England and Wales,
- secure that relevant undertakers are able (in particular, by securing reasonable returns on their capital) to finance the proper carrying out of their functions, and
- secure that the activities authorised by the licence of a licensed water supplier and any statutory functions imposed on it in consequence of the licence, are properly carried out

Licence restrictions

United Utilities Water's licence contains similar restrictions to those contained in United Utilities Electricity's distribution licence These restrictions include

- a non-discrimination obligation,
- restrictions on the payment of dividends Dividends can only be made in accordance with a written dividend policy of the directors of United Utilities Water which has been accepted by Ofwat as not impairing its ability to finance its business,
- the ring-fencing of financial and management resources of the licensed business, and
- restrictions on dealings with associated companies The consent of Ofwat is required before lending any funds to an associated company and all transactions with associated companies must be on an arm's length basis without cross subsidy

In relation to the last of these licence obligations, in December 2006 United Utilities Water gave an undertaking to Ofwat to change its arrangements for trading with associated companies to ensure that they were at arm's length Ofwat has also decided to impose a penalty on United Utilities Water for breach of this licence obligation The proposed penalty amounted to £8 5 million (0 7 per cent of the company's turnover for its regulated activities) The imposition of financial penalties for breach of licence conditions and other key duties was introduced by the WA 2003 to bring Ofwat's powers into line with those of other regulators Companies may face a penalty of up to ten per cent of relevant regulated turnover for breaching licence conditions, standards of performance or other obligations Ofwat has published a statement of the policy that it intends to apply to the imposition of any penalty and the determination of its amount Such penalties can be appealed to the High Court

Modification and revocation of the licence

Licence conditions can be modified by Ofwat, either with the water undertaker's agreement or following reference to the Competition Commission for a decision on public interest grounds However, reference to the Competition Commission is not required where the changes are necessary or expedient to implement the new WSL regime

The licence may be terminated on 25 years' notice, with more immediate revocation in certain specific circumstances (including, for example, failure to comply with an enforcement order made by Ofwat)

In practice, many regulatory issues arising between licensees and the water regulator are settled without the need to resort to formal proceedings However, where Ofwat is satisfied that a licensee is in breach of the conditions of its licence, it has powers to secure compliance by means of an enforcement order Failure to comply with an enforcement order can lead to enforcement in court, payment of compensation by the licence holder to the 'injured' party and, ultimately, to revocation of the licence Alternatively, where actual or likely contravention of an enforcement order (or of one of a licensee's principal statutory duties under the Act) is so serious as to make it inappropriate for the licensee to continue to hold its licence, Ofwat may, with the Secretary of State's consent, apply to the High Court for the appointment of a special administrator to run the company until arrangements can be made for a new company to carry on the licensed activities A special administrator may also be appointed where the licensee is, or is likely to be, unable to pay its debts

Price control

Ofwat regulates water and wastewater charges by capping the average increase in charges that a company can impose in any year Ofwat conducts a periodic review and sets price caps every five years Ofwat has announced that it intends to maintain this five-year price control but that it will place price limits within a longer-term framework For example, it will ask water companies for a 25-year business plan at the next price control review

This price cap is set by reference to inflation as measured by the retail price index in the UK plus an adjustment factor known as 'K', which is specific to each company and which can vary for each year of the review period The size of a company's K factor (which can be positive, negative or zero) reflects the scale of its capital investment programme, its cost of capital and its operational and environmental obligations, taking into account the scope for it to improve efficiency

'Price cap' regulation as operated in the UK is performance based Companies are incentivised to be efficient, both in terms of their operating costs and in the implementation of their capital expenditure programme The benefit of any efficiency savings achieved through effective management is retained by the companies for a period of five years, after which time the benefit is passed to customers via the subsequent price setting process The cost of any under-performance due to poor management is borne by the companies Companies are also incentivised to provide a high quality of service and penalised if they provide a poor quality of service by means of an adjustment to the K factor at the subsequent price review The last periodic review was completed in December 2004 and covers the period from 1 April 2005 to 31 March 2010 In the last review, Ofwat set the following K factors, being the amount by which prices are allowed to rise above inflation in each of the five financial years commencing on 1 April 2005

2005/06	5 0 per cent
2006/07	6 4 per cent
2007/08	4 4 per cent
2008/09	3 5 per cent
2009/10	3 0 per cent

This equates to a real (i e excluding inflation) average annual price increase over the five-year period of 4 5 per cent Ofwat is currently reviewing its cost base methodology in preparation for the 2009 review

Unexpected costs or savings arising from changes in certain regulatory assumptions during a review period are recorded and agreed by the company and Ofwat This process, known as 'logging up and down', allows prices to be adjusted up or down at the next periodic review to compensate companies or customers respectively for the unexpected change In addition, where the change exceeds the specified materiality thresholds, the company can request, and Ofwat can instigate, a re-setting of its price limit during the five-year period, known as an Interim Determination of K ('IDoK')

All water and sewerage companies' licences now include a 'shipwreck' or 'substantial effect' clause, which allows companies' price limits to be revised when events beyond their control have a significant effect on their costs or revenues This clause is now included in United Utilities Water's licence, allowing adjustment where appropriate for unforeseen events both adverse and favourable

Environmental regulation of water and wastewater

The water and wastewater industry in the UK is subject to substantial domestic and European Union regulation, placing significant statutory obligations on United Utilities Water with regard to, among other factors, the quality of treated water supplied and of wastewater treatment European directives including the Drinking Water Directive, the Bathing Water Directive and the Urban Wastewater Treatment Directive are transposed into UK law by primary and secondary legislation

All water and wastewater companies have a general duty to exercise their powers to conserve and enhance natural beauty and to promote efficient use of water Environmental regulation is the responsibility of the Secretary of State for Environment, Food and Rural Affairs together with

- the Environment Agency ('the Agency'), which is responsible for conserving and redistributing water resources and securing their proper use, including the licensing of water abstraction The Agency also regulates discharges to controlled waters, including discharges from wastewater treatment works,
- the Drinking Water Inspectorate, which enforces drinking water quality standards, and
- Natural England, which is responsible for the protection of designated sites for nature conservation, e g Sites of

Special Scientific Interest. There is a statutory requirement to manage these sites to conserve or improve biodiversity. As a result of new UK government targets, Natural England is seeking improvements to approximately 50 per cent of the sites within United Utilities' ownership.

Regulatory and legislative developments

United Utilities Water expects regulatory regimes in water and wastewater to continue to evolve and become more onerous. Examples of such regulatory and legislative developments include the following:

- amendments to the Water Resources Act 1991 by the WA 2003 and the Water Resources (Abstraction and Impounding) Regulations 2006 make new water abstraction licences time-limited and unused licences more easily able to be revoked or varied without compensation, and create a new statutory right of civil action where water abstraction causes loss or damage. Water undertakers must promote water conservation, and must publish drought plans and water resource plans. The government may require publication of flood plans showing the effect of a reservoir dam failure;
- The Water Framework Directive, transposed into UK law in 2003, which requires the UK government to:
  - establish comprehensive river basin management plans from 2009, revised on a six-year cycle;
  - implement the first set of river basin management plans by December 2015;
  - prevent deterioration in the ecological status of water bodies; and
  - achieve 'good' water status by 2027.

The Directive is likely to require further improvements in discharges from wastewater networks and treatment works;

- the Water Supply (Water Quality) Regulations 2000 and the Water Supply (Water Quality) Regulations 2001 (together the Water Quality Regulations), which transpose into UK legislation the Drinking Water Directive, introduce more stringent lead standards (ten micrograms per litre (10µg/l) from 25 December 2013) which will require improvements to treatment works and distribution systems. United Utilities Water has a programme of installing additional phosphate dosing and pH control assets, and replacing lead communication pipes. Lead pipe replacement is likely to need acceleration during the AMP4 period (1 April 2005 to 31 March 2010); and
- the AMP4 Consumer Acceptability programme also provides part of a ten-year programme for the group to clean and refurbish up to 602 kilometres of large diameter trunk mains and up to 4,689 kilometres of smaller diameter mains, to deal with iron and manganese deposition and corrosion.

Proposed changes to the Water Quality Regulations in 2007 cover emergency bottled water, monitoring by water companies of new abstraction sources, varied monitoring standards, modernised publicity requirements for authorised departures, other information provisions, amended disinfection requirements, altered risk assessment procedures and other matters about supply zones, sources and standards. Both the company and the UK water companies' trade association, Water UK, have responded indicating a need for clarification of the detail of some of these proposals.

The European Union Urban Wastewater Treatment Directive, which was transposed into UK legislation by the Urban Wastewater Treatment Regulations 1994, requires improvements in the treatment of wastewater discharges, in particular, the provision of secondary treatment. United Utilities Water continues to make progress towards achieving this for wastewater treatment works serving areas with a population equivalent of more than 2,000. The Directive also requires measures to be taken to limit pollution from stormwater overflows. Dialogue continues with the regulators on the scope of works needed to meet this obligation and related requirements (for example, see below in relation to recent United Utilities Water 'lead case' appeal decisions).

Infringement proceedings

Infringement proceedings, which began in 2006, by the European Commission against the United Kingdom regarding the implementation of the Urban Wastewater Directive, continue. The European Commission believes that the United Kingdom has not taken all measures needed to reduce the nutrients in wastewater to remedy problems in sensitive areas. Depending upon the outcome of this legal action, some of the Irish Sea could be designated as a sensitive area. This, in turn, could lead to requirements being placed upon United Utilities Water to reduce some nutrient levels in discharges from many of its wastewater treatment facilities which feed into the Irish Sea.

There are, in addition, other ongoing infringement proceedings by the European Commission against the United Kingdom regarding the implementation of the Urban Wastewater Treatment Directive, but these do not directly concern United Utilities Water's appointed area.

Bathing waters

A revised European Union Bathing Water Directive entered into force in March 2006, introducing more stringent microbiological standards at designated bathing waters around the UK coast. United Utilities Water's programme of wastewater network and treatment projects relating to its operational facilities continues to improve the quality of, and meet the required standards for, bathing waters in north west England.

Sewage sludge on agricultural land

Discussion at the European level of a new Waste Framework Directive continues and it is likely that the use of sewage sludge on agricultural land will be excluded. However, revision of the UK regulations may introduce tighter limits for metals in sludge. United Utilities Water's preferred route of disposal for sewage sludge remains spreading on agricultural land, but it is concurrently taking steps to ensure sufficient incineration capacity, with expansion of its Shell Green sludge processing centre near Widnes under way, and the planning process having commenced for a further processing centre near Preston.

Odour

Complaints of odour from wastewater treatment works may be actionable as statutory nuisance under the Environmental Protection Act 1990 The current capital programme includes measures to deal with this issue United Utilities Water complies with the voluntary 'Code of Practice on Odour Nuisance from Sewage Treatment Works' published by the Secretary of State on 12 April 2006

A test case decision of the High Court in January 2006 that certain United Utilities Water's wastewater treatment plant operations should, in addition, be regulated under the Pollution Prevention and Control Regulations, was upheld in the Court of Appeal in May 2006 Depending upon the outcome of an appeal to the House of Lords, this may result in increased costs of compliance with environmental legislation in relation to such operations

Stormwater overflows

Certain 'lead case' appeals made by United Utilities Water have been decided by a Planning Inspector (appointed by the Secretary of State) in January 2007 in relation to the extent of works required under discharge consents for storm water overflows, including for the purposes of compliance with the Urban Wastewater Treatment Regulations The implications of these decisions are currently being considered by Ofwat and the Environment Agency As part of the five-year periodic review of prices, Ofwat takes into consideration the capital investment programme which United Utilities Water needs to achieve in order to comply with environmental legislation

Electricity distribution

United Utilities Electricity owns the distribution network which carries electricity from the National Grid along power lines to consumers' premises on behalf of the electricity supply companies who are United Utilities Electricity's customers

The income derived from the distribution business depends in part on changes in the demand for electricity by consumers in north west England, and also from generators who have been connected to United Utilities Electricity's network under contracts agreed since 1 April 2005 Demand for electricity is affected by such factors as growth and movements in population, social trends, economic and business growth or decline, changes in the mix of energy sources used by consumers, weather conditions and energy efficiency measures

The electricity distribution business is a regulated business in which the average increase in charges, which a company may impose in any year, is capped by the electricity regulator (as described in more detail below) Accordingly, profit derived from the distribution business of United Utilities Electricity also depends upon efficiency, achieved by reducing and controlling costs, and providing high standards of service

Key performance measures for the business relate to quality of supply Electricity supplies were available for 99 99 per cent of the time during the year ended March 2007, sustaining the business's high level of performance in managing the network to maintain constant supplies for consumers

Under the regulatory interruptions incentive scheme, United Utilities Electricity has been set network performance targets for the number and duration of customer supply interruptions This year is the first year for several years where United Utilities Electricity has not comfortably out-performed the regulatory targets, mainly due to a few high impact events on the grid and primary distribution systems, including third party damage to 33,000 volt cables The average number of interruptions per 100 consumers per annum was 53 89, out-performing the regulatory target for the year of 57 1 The average number of minutes for which consumers were without supply was 56 68, again just out-performing the regulatory target for the year of 58 1 minutes

Economic regulation of electricity distribution

Ofgem

The electricity industry in Great Britain is regulated by the Gas and Electricity Markets Authority under the Electricity Act 1989 (the 'Electricity Act'), the Utilities Act 2000 (the 'Utilities Act') and the Energy Act 2004 (the 'Energy Act') The Authority governs and acts through Ofgem The Electricity Act, as amended by the Utilities Act, requires all companies distributing electricity in Great Britain to be licensed, unless they are covered by an exemption Economic regulation pursuant to these licences is the responsibility of Ofgem Ofgem also exercises powers under UK competition legislation, most significantly the Competition Act 1998 and the Enterprise Act 2002

Ofgem is led by a chairman, who is an independent public servant appointed for a fixed term by the Secretary of State for the Department of Trade and Industry The current chairman was appointed from October 2003 for a period of five years

Ofgem must comply with the statutory duties laid down in the Electricity Act as amended by Acts cited above, and others In doing so, Ofgem may receive guidance from the UK government in areas such as social and environmental policy In carrying out its statutory duties, Ofgem is required to exercise judgement, but is not subject to direction as to what those judgements should be and is independent of government ministers The chairman of Ofgem may only be removed from the post for incapacity or misbehaviour

The primary duty of Ofgem is to protect the interests of consumers, wherever appropriate, by promoting effective competition In carrying out this duty, Ofgem is required to have regard amongst other factors, to

- the need to secure that all reasonable demands for electricity are met, and
- the need to secure that licence holders are able to finance their activities

Electricity distribution licence

The UK government awarded electricity distribution licences in 2001 The licences continue in force for an indefinite period, subject to potential termination rights as set out below United Utilities Electricity holds an electricity distribution licence that authorises it to distribute electricity anywhere in Great Britain Under that licence, United Utilities distributes electricity across its distribution system covering an area in north west England comprising 2 4 million consumer premises

United Utilities Electricity's electricity distribution licence contains similar restrictions to those contained in United Utilities Water's water licence These restrictions include

- a non-discrimination obligation,
- restrictions on the payment of dividends The board of directors must provide a certificate of compliance before declaring dividends, affirming they are satisfied that the business is complying with relevant licence obligations including that it has sufficient resources and that the making of the distribution will not cause it to be in material breach of any of the obligations in the future,
- restrictions on dealings with associated companies The consent of Ofgem is required before lending any funds to an associated company and all transactions with associated companies must be on an arm's length basis, without cross subsidy,
- ring-fencing of financial and management resources of the licensed business, and
- restriction on the disposal of any asset forming part of the distribution system

Modification and revocation of the licence

Licence conditions can be modified by Ofgem either with the agreement of the licensee (or, in the case of standard conditions, with the agreement of the requisite proportion of licensees) or following reference to the Competition Commission for a decision on public interest grounds The licence can be terminated on 25 years' notice given by the Secretary of State The licence can also be revoked in certain circumstances, including where the licensee fails to comply with an enforcement order made by Ofgem Breach of a licence condition can attract penalties of up to ten per cent of the licensed company's turnover Ofgem has published a statement of the policy that it intends to apply to the imposition of any penalty and the determination of its amount Any such penalty can be appealed to the High Court

In practice, many regulatory issues arising between licensees and Ofgem are settled without the need to resort to formal proceedings However, where Ofgem is satisfied that a company is in breach of the terms of its licence, it has powers to secure compliance by means of an enforcement order If a company does not comply with the order (as well as potentially giving rise to third party action), compliance can be enforced by the courts and ultimately Ofgem may revoke the licence

The Energy Act introduced a special administration regime, applicable to the holders of electricity distribution licences, similar to that provided for the water sector Ofgem or the Secretary of State can appoint a special administrator to take over the management and operation of the company to secure its financial recovery in the event of actual or threatened insolvency of the licensee

Ofgem has indicated that during 2007 and 2008 it intends to review the electricity distribution licences with a view to improving the clarity of the licence, although it will also consider making more substantive changes

Guaranteed standards

United Utilities Electricity is required to maintain certain standards relating to the quality of supply of electricity in its licence area These standards take the form of guarantees at the individual customer level and are subject to monitoring and compliance audits Failure to meet guaranteed standards of performance will result in a prescribed compensation payment to the customer concerned In addition, Ofgem can impose fines on companies that fail to achieve the guaranteed standards or are in breach of other licence obligations

Price control

Ofgem regulates electricity distribution charges by capping the average charges that a company can impose in any year Ofgem conducts a periodic review and sets price caps every five years This price cap is set by reference to inflation as measured by the retail price index in the UK plus an adjustment factor known as 'X' which is specific to each company and which can vary for each year of the review period The size of a company's X factor (which can be positive, negative or zero) reflects the scale of its capital investment programme, its cost of capital and its operational and environmental obligations, together with scope for it to improve its efficiency The last periodic review was completed at the end of 2004 and covers the period from 1 April 2005 to 31 March 2010 For the 2005-10 review period, United Utilities Electricity was allowed a real (i e excluding inflation) price increase of 8 2 per cent in 2005/06 followed by constant real prices thereafter Ofgem will publish its first scoping letter and timetable for the 2010 price review during 2007

'Price cap' regulation, as operated in the UK, is performance based Companies are incentivised to be efficient, both in terms of their operating costs and in the implementation of their capital expenditure programme The benefit of any efficiency savings achieved through effective management is retained by the companies for a period of up to five years, after which time the benefit is passed to customers via the price setting process The cost of any under-performance due to poor management is borne by the companies

An incentive scheme was introduced by Ofgem in April 2002 which provided greater focus on three specific service areas the number of interruptions to customers' supplies, the length of those interruptions, and the quality of the telephone response to customers Ofgem consulted on its approach to the incentive scheme as part of the price control review and again in 2006, including the form of the scheme, targets and associated costs It has been agreed that the distribution network operators' performance in those areas will continue to be incentivised until the end of the next price control period (2015) Under the scheme, United Utilities Electricity is subject to annual rewards and penalties depending upon its performance against pre-specified targets Both rewards and penalties under the incentive scheme are capped at three per cent of annual revenues

Under the terms of their licences, electricity distribution network operators (DNOs) must produce and implement charging methodologies for both connection to and use of their distribution systems The methodologies are required to set out the principles and methods by which electricity distribution charges will be calculated The methodologies must be approved by Ofgem

Electricity metering services

In 2006/07 Ofgem consulted on licence modifications that are intended to clarify the obligations on DNOs with respect to electricity metering services after the price controls on the provision of new and replacement meters and meter operation services expire on 31 March 2007 The effect of the modifications is to make clear that from 1 April 2007, the regulatory price cap will be retained only for the rental of electricity meters installed prior to 31 March 2007 Other metering services will no longer form part of the definition of a distribution business and DNOs that wish to provide new or replacement meters or meter operation services must do so through a separate subsidiary

Following a review by Ofgem, in 2006 the former bilateral agreements governing the commercial contractual arrangements relating to the connection to and use of distribution networks were replaced by a single multilateral contract, the Distribution Connection and Use of System Agreement, as Ofgem felt that it would improve transparency

Environmental regulation of electricity distribution

Underground cabling

All electricity companies have a general duty under the Electricity Act to have regard to the desirability of environmental preservation and conservation and the protection of Sites of Special Scientific Interest when they formulate proposals for development United Utilities Electricity may be required to carry out an environmental assessment when it intends to lay cables, construct overhead lines or carry out any other development in connection with its licensed activities In response to discussions with environmental organisations in United Utilities Electricity's operating area, and with the backing of Ofgem, the company has embarked on a programme of converting from overhead cables to underground cables in designated areas on aesthetic grounds There is a small allowance of £5 million by Ofgem for such work over the period 2005-10 The first of these schemes was completed recently and five more are now in progress

High voltage cables

United Utilities Electricity, in common with all other UK electricity companies, owns and operates pressure-assisted high voltage cables These operate at voltages of 33,000 volts and 132,000 volts These cables are either filled with nitrogen gas or an insulating liquid United Utilities Electricity operates both types, having 620 kilometres of the latter type of cable Cables of the latter type are pressurised with a light oil type fluid In the main the fluid is biodegradable, although some older cables are pressurised with a variety of fluid that is not

The potential for loss into the environment of the fluid, due to leaks or third party damage, is recognised nationally by all electricity companies and the Agency and is an issue concerning waste disposal and pollution law In order to mitigate the effects of any losses, United Utilities Electricity is party to a national code of practice agreement with the Agency

Over the last six years, the company has worked to minimise losses into the environment and reduced annual loss to around 25m^3 in 2005/06 from a high of 74m^3 in 2001/02 However, 2006/07 has been a particularly disappointing year, with losses of 49m^3 A significant contribution to this figure is damage caused to United Utilities Electricity's 33,000 volts cables by third parties, although there is also a contribution from some particularly poorly performing cables that have been replaced during 2006/07

Microgeneration

The Climate Change and Sustainable Energy Act was adopted in June 2006 with the primary aim of encouraging the production of energy through microgeneration and community energy schemes, improving energy efficiency and alleviating fuel poverty The Act seeks to cut the emission of carbon dioxide in the UK and introduces new powers to modify the conditions of electricity distribution and supply licences to ensure that energy companies pay a fair price for electricity produced from microgeneration

Electric and magnetic fields

The possibility that electric and magnetic fields may cause adverse health effects has been a topic of debate and research for many years Over the last 20 years, major research programmes throughout the world have explored whether electric and magnetic fields (EMF) have an adverse impact on health A large epidemiological study, the UK Childhood Cancer Study, reported in December 1999 that there was "no evidence that exposure to magnetic fields associated with the electricity supply in the UK increases risk for childhood leukaemia, cancers of the nervous system, or any childhood cancer" International bodies such as the World Health Organization (WHO) and the International Agency for Research on Cancer and, in the UK, the Health Protection Agency (HPA) (which has subsumed the former National Radiological Protection Board, or NRPB) continue to investigate this issue and have currently concluded that there is no established causal link between EMFs and ill health In March 2001, the HPA published a review of the state of the science and concluded "for the vast majority of children in the UK there is now considerable evidence that the EMF levels to which they are exposed do not increase the risk of leukaemia or other malignant disease" However, it also noted that the possibility remains that intense and prolonged exposure to magnetic fields can increase the risk of leukaemia in children, but that the epidemiological evidence is currently not strong enough to justify a firm conclusion that such fields cause leukaemia in children

In the spirit of the precautionary approach, in May 2003 the HPA published a consultation document on how to limit exposure to EMFs and, in particular, on whether the UK should adopt the more stringent exposure guidelines of the International Commission on Non-Ionizing Radiation Protection (ICNIRP) In March 2004, the NRPB recommended that the ICNIRP guidelines should be adopted A report published by the Childhood Cancer Research Group in 2005 strengthened the evidence that childhood leukemia rates are slightly higher near power lines, but leaves the question of what causes this more confused than before, stating that "There is no accepted biological mechanism to explain the epidemiological results, indeed, the relation may be due to chance "

The independent Advisory Group on non-ionising Radiation (AGNIR), which reports to the board of the HPA, has issued several reports relating to EMFs, considering their possible link with an increased risk of cancer The most recent AGNIR report on EMFs published in February 2006 concluded that the evidence does not support the hypothesis that exposure to EMFs is associated with an increased risk of breast cancer and that, although it is inconclusive, it does not appear that EMFs affect the hormone melatonin (a reduction in which can lead to breast cancer) The report gave recommendations for further research to be carried out

In spite of the official view of bodies like the HPA and the WHO, there continues to be significant lobbying by pressure groups concerned about the alleged effects of public electricity infrastructure on health In 2005, a cross industry all stakeholder group on the issue was set up in the UK It is known as the Stakeholder Advisory Group on Extra Low Frequency EMFs (SAGE) Although SAGE was initiated by National Grid plc, it has now been taken up by the Department of Health, and will undertake a report to the Department of Health on EMF issues in relation to health The industry is represented on SAGE by the National Grid and by the Energy Networks Association of which United Utilities Electricity is a member

The work of SAGE is not complete, although it is expected that a report will be delivered to the Department of Health during 2007/08 Currently the balance of advice in SAGE seems to support the status quo, although given the breadth of views necessarily aired in the process, other options which could drive significant costs for the industry (such as the maintenance of building-free corridors around power lines) have had their merits reviewed However, it will be for the government to decide on the appropriate response to stakeholder concerns, and United Utilities Electricity does not currently expect any real shift from the status quo to emerge

United Utilities Electricity, in line with other Energy Networks Association (ENA) member companies, carries out its activities in accordance with HPA guidance The ENA is the trade association for electricity companies in the United Kingdom The ENA and its member companies are committed to responsible behaviour in light of the scientific evidence, including considering any appropriate precautionary actions

United Utilities Contract Solutions

Providing services which will benefit 17 million people in the UK and a further seven million internationally

During the financial year, United Utilities Contract Solutions operated through three distinct market-facing business units

- Utility Solutions – developing and operating contracts in the UK applying the group's core infrastructure management skills,
- International – responsible for applying the group's core infrastructure management skills in selected overseas markets, and
- Industrial and Commercial Solutions – providing services to the public sector and commercial market, including multi-utility connections, metering services, water and liquid waste treatment services and facilities management

The structure of the business remained constant throughout the year ended 31 March 2007, aiming to deliver future sales and profit growth by focusing on our target markets As described on page 7, with effect from 1 April 2007 the business has been restructured

The business continued to play a leading role in the delivery of part of Scottish Water's four-year £1 8 billion capital investment programme

Utility Solutions
The Utility Solutions business develops and operates contracts in the UK utility market, servicing over 12 million people It seeks opportunities which will secure long-term operational sources of income while limiting overall financial exposure

During the year, the business has concentrated on profit and service delivery in its four major utility outsourcing contracts 2006/07 was the second full year of operation for two of our major contracts a five-year contract to deliver Southern Water's capital investment programme as part of a consortium, and an operations and maintenance contract with Dŵr Cymru Welsh Water for up to 15 years The latter continues our relationship with Dŵr Cymru following the expiry of the first four-year contract on 31 March 2005 Under the new contract, the business provides water and wastewater services in north Wales and water services in south Wales The business also provides shared services throughout Wales, including education and conservation activities and transport

2006/07 was the first full year of a £1 1 billion eight-year contract to operate, maintain and manage the north of England gas distribution network owned by Northern Gas Networks, a consortium in which Contract Solutions has a 15 per cent stake

The business continues to play a leading role in the delivery of part of Scottish Water's four-year £1 8 billion capital investment programme, the funding for which will be provided by Scottish Water The programme will improve services to 2 2 million homes and businesses across Scotland In addition, during the year, work commenced on the follow-up capital investment programme for the period up to 2010

International
The International business develops and operates contracts in selected overseas utility markets and provides services for over seven million people internationally In Australia, the business focus is on maintaining the current portfolio of contracts and securing long-term investment returns and operational sources of income while managing the overall exposure arising from the contracts Elsewhere, the overseas business focus is on pursuing long-term operations and maintenance opportunities, primarily in the Gulf region, with other existing overseas investments being managed alongside existing UK investments

The business continues to manage its existing portfolio of water and wastewater operations through a number of joint ventures in parts of Scotland, Australia, Poland, Estonia and Bulgaria

Generally, the joint ventures have limited recourse to United Utilities. However, the business has performance bonds and guarantees in place supporting joint venture operations (see 'Performance guarantees' on page 33) and in some cases there are bank letters of credit supporting equity commitments.

The International business is affected by a variety of regulatory regimes and regulatory risks, which are accepted to varying degrees by the client, the concession company and/or the operator. For those contracts where it is the operator, United Utilities is not the licensed entity but may be a direct or indirect investor in the licensed entity.

Industrial and Commercial Solutions
Industrial and Commercial Solutions comprises four distinct businesses.

Connections
The Connections business provides multi-utility connections, connecting domestic, industrial and commercial consumers to the existing utility network infrastructure. In providing this service, the business designs and installs new electricity, water, gas and telecommunications infrastructure. During the year ended 31 March 2007, the business commenced work on a major new £133.0 million seven-year gas connections contract on behalf of Northern Gas Networks, whilst at the same time continuing to focus its sales and marketing effort towards long-term strategic customers and larger projects. This business secured £78.1 million of orders in the year ended 31 March 2007, including £18.0 million out-of-area orders.

Metering
The Metering business provides installation and maintenance services for electricity and gas meters. In the year ended 31 March 2007, the business installed or exchanged 100,000 electricity meters in north west England under a contract with United Utilities Electricity. This contract came to an end during the year with the incumbent electricity supplier deciding to in-source the ongoing activity, resulting in the transfer of some 120 employees to the supplier. In addition, the metering business completed around 600,000 gas and electricity meter installations under a contract with British Gas Trading up to January 2009. Under this contract, both gas and electricity meters are installed by the metering business, with rental income then being received for up to 20 years after installation by a joint venture company (in which the group has a 50 per cent interest), and which owns the meter assets.

Industrial
This business is a provider of specialist water and liquid waste services to industrial customers in the UK, treating approximately 1.1 million tonnes of wastewater a year, as well as providing construction and operations and maintenance services for privately-owned high voltage electrical equipment. The business currently has some 1,500 industrial and commercial clients, including major businesses like Manchester United, Atomic Weapons Establishment, Morrisons, BNFL and Manchester Airport. The business also offers clients a complete multi-utility service, using its expertise to manage on-site water, wastewater and electrical services, allowing clients to concentrate on running their core business.

Facilities management and energy
The Facilities Management business manages properties for clients under contract. The scope of operations includes arranging site services such as reception and cleaning, managing vacant space and office management. The Energy Services business provides energy efficient infrastructure, such as lighting, to customers.

Our people

Leadership is key to business performance and culture

Table 1 People – key contributors to corporate success

Number of employees	2006/07	2005/06
United Utilities North West	**4,831**	4 775
United Utilities Contract Solutions	**3,539**	3,197
Vertex (discontinued operation)	**8,277**	8,203
Your Communications (discontinued operation)	**-**	653
Other activities	**221**	201
Average number of persons employed by the group during the year	**16,868**	17,029

• Substantially all of the group's employees are based in the United Kingdom

Employee involvement
The group seeks to involve employees with open and regular communications about business developments and issues of general interest, both formally and informally

An interim employee opinion survey was conducted in respect of nine key measures Employee satisfaction was 69 per cent compared with 74 per cent last year In future, surveys will be conducted annually in November Greater emphasis will be placed on understanding employees' views and concerns

Leadership
Leadership is key to business performance and culture In accordance with the objective of becoming a high performance organisation, we are providing our senior leaders with the skills to release their own, and develop their team's, potential In addition, our high performance team programme was rolled out to a further 177 teams in United Utilities North West

Industrial relations
Good industrial relations remain a priority for United Utilities across the whole of its business and parts of the group have been recognised in the UK for excellence in this area The group continues to recognise and work in partnership with a range of trade unions across the sectors in which it operates

A statement of principles governs the approach to labour relations across the group

Within United Utilities North West, approximately 60 per cent of employees are members of one of the five recognised trade unions, a figure which has been broadly stable over recent years However, around 99 per cent of employees within United Utilities North West are represented by trade unions for collective bargaining purposes, a process which is underpinned by principles contained within a voluntary collective agreement entitled 'Together in Partnership' Following an independent and comprehensive review and re-evaluation of the agreement, a series of joint initiatives has been put in place to develop this collaborative approach to employee relations further

Within United Utilities Contract Solutions, approximately 57 per cent of employees are now represented by trade unions for collective bargaining purposes Other employees are employed on personal contracts and are not covered by collective bargaining arrangements

A review of union relationships has taken place in a number of business areas and these are being managed at a local level due to the diverse nature of the business and the different contracts operated by the business As a consequence, consultation arrangements have been reviewed in all business areas and effective arrangements are now in place for all employee groups

Good progress has been made in developing relationships with trade unions in these local business areas For example, the 'Working Together Partnership' arrangements in the Welsh Water contract have been reviewed and refreshed In the Northern Gas Networks contract, a two-year pay agreement has been successfully concluded which allows the business now to focus on developing joint working arrangements going forward In the Industrial and Commercial Solutions business, a joint development programme is being rolled-out across the consultation forums, facilitated by the Partnership Institute, aimed at improving their effectiveness

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Health and safety continues to be reviewed at the highest level with monthly reports to the Executive Leadership Team

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- Group-wide health and safety role profile documentation and standard approach to monitoring work related sickness absence

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Group-wide reporting is achieved via a 'key performance indicator' reporting process that measures reactive (lagging) and proactive (leading) indicators

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In 2006, over 1,200 applications were received for 44 apprenticeship roles across the UK A centralised scheme for apprentice recruitment has been introduced in 2007 to improve the application process, with a single webpage link and attendance at career fairs

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The company respects the dignity and rights of every employee and supports them in performing various roles in society The group also challenges prejudice and stereotyping

October 2006 saw the introduction of the new Employment Equality (Age) Regulations Employees across the group were briefed, making them aware of their rights under this new legislation

An equal pay audit was conducted during the year across all the businesses No major disparities in pay between male and female employees were found when comparing like-for-like roles The business is focused on ensuring consistency and integrity of the data held on payroll systems

Employees with disabilities
The company is committed to fulfilling its obligations in accordance with the Disability Discrimination Act 1995 and best practice As an equal opportunities employer, the group gives equal consideration to applicants with disabilities in its employment criteria and will modify equipment and working practices wherever it is safe and practical to do so, both for new employees and for those employees that are disabled during the course of their employment Additionally, the group is committed to providing full support and appropriate training for employees who become disabled during the course of their employment so that they can continue to work in a position appropriate to their experience and abilities

Property assets

The group owns 58,500 hectares of catchment land to protect and improve the quality of raw water supplies

United Utilities Water
United Utilities Water owns and manages assets which include

- 192 raw water impounding reservoirs and associated catchments,
- 1,183 kilometres of raw water aqueducts,
- 108 water treatment works,
- 862 kilometres of treated water large diameter trunk mains,
- 455 service reservoirs and water towers storing treated water,
- 633 pumping stations, and
- 40,080 kilometres of trunk and distribution mains

United Utilities Water owns some 58,500 hectares of catchment land The key reason for owning and managing this land is to protect and improve the quality of raw water supplies, and thus reduce both the risk of non-compliance at our water treatment works and operating costs

In the 2004 Periodic Review, United Utilities Water obtained funds of £10 1 million for an innovative approach to land management entitled the Sustainable Catchment Management Programme (SCaMP) This programme seeks to restore moorland areas so as to meet the government's Public Service Agreement (PSA) targets to bring Sites of Special Scientific Interest into good condition At the same time, it seeks to enter into long-term agreements with tenant farmers to reduce livestock to acceptable levels so that, once restored, the moorland areas will be protected for the future This integrated holistic approach should bring multiple benefits As well as delivering the government's biodiversity targets, it is anticipated that there will be improvements in raw water quality (relating in particular to colour) and potentially reduced risk of downstream flooding

The programme has just completed its second year Plans are in place for the programme to be applied to all the farms owned by United Utilities Water, and the company has been successful in concluding agreements with tenant farmers covering over 85 per cent of the land area in the programme to enable this to happen Subject to the availability of the relevant agri-environment grants such as Higher Level Stewardship, the company is now poised to accelerate the delivery of the programme

United Utilities Water's wastewater operations involve owning and managing assets, which include

- 584 wastewater treatment works,
- 40,323 kilometres of sewers,
- 1,749 pumping stations,
- 371 storage tanks,
- 3,087 combined sewer overflows, and
- 36 sludge treatment facilities

United Utilities Electricity
As at 31 March 2007, United Utilities Electricity's facilities included 13,128 kilometres of overhead lines, 43,149 kilometres of underground cables (operating at 132 kilovolts, 33 kilovolts, 25 kilovolts, 11 kilovolts, 6 6 kilovolts and 400/230 volts), 18,248 ground mounted substations and 17,021 pole mounted transformers

United Utilities Electricity holds wayleaves which entitle it to run lines and cables through and across private land and in some circumstances these can be terminated by the landowner or occupier upon notice pursuant to the Electricity Act However, United Utilities Electricity has statutory rights to seek the compulsory retention of a wayleave if termination is sought by the landowner or occupier United Utilities Electricity does not anticipate that any significant relocation of these facilities will be required, although any relocation of a major portion of these facilities would have a material adverse effect on its business and financial position Ground mounted substations are situated on properties either owned by United Utilities Electricity or held under lease Pole mounted transformers are generally held under wayleave agreements

United Utilities Electricity anticipates that it will be able to negotiate lease renewals on satisfactory terms or relocate equipment so that the non-renewal of any such leases would not have a material adverse effect upon United Utilities Electricity

United Utilities Contract Solutions
At 31 March 2007, United Utilities Contract Solutions' key facilities included leased head office accommodation in Birchwood, Warrington and Industrial & Commercial Solutions' offices at Old Trafford, Manchester In addition to these sites, the business occupies various properties in support of specific contracts, typically within the geographic boundaries of the contracts, both in the UK and overseas These sites consist of offices, depots and operational facilities that are primarily owned or leased by the client It is anticipated that the business will be able to negotiate renewals of any expiring leases, or relocate the relevant facilities, without having a material adverse impact on the business

Other property assets
In addition to the properties described above, the group occupies various other properties consisting primarily of offices, depots, warehouses and workshops These are either owned by the group or leased It is anticipated that the group will

be able to negotiate renewals of any expiring leases, or relocate the relevant facilities, without having a material adverse impact on the group

Lingley Mere Business Park development

In February 2004, the group entered into a 15-year joint venture agreement with AMEC Developments Limited to develop land at Lingley Mere, Warrington Over a period of time, the group will invest up to £20 million in this joint venture, mainly in the form of land

Contaminated land and environmental issues

The contaminated land regime in Part IIA of the Environmental Protection Act 1990 places liability for the clean-up of contaminated land upon any person who caused the contamination or, in some circumstances, who knew of its presence and failed to prevent it If no such person can be found after a reasonable enquiry has been made, liability for clean-up falls upon the current owner or occupier of the land The regime provides for exemptions from liability in certain cases The group is not aware of any liability which it may have under the regime which could have a material adverse impact on its businesses

The group believes that all of its properties are in a reasonable state of repair and are adequate for their purpose The group has a continuing programme of improving, replacing and disposing of property when considered appropriate to meet the needs of its business operations It is not aware of any material environmental issues that would prevent the anticipated utilisation of the above mentioned properties

Some non-operational areas of United Utilities Water's wastewater treatment works, including Irlam, Manchester, may be affected by contamination At present, it is not clear how the liability for the clean-up will be allocated, or the extent of the cost for such work However, this is not expected to have a material impact on the group's results

As at 31 March 2007, the principal water operations facilities were as shown in table 2 below

Table 2 Owned by United Utilities Water PLC

Location	Description	Hectares	Tenure
Bowland Estate, Lancashire	Reservoir/gathering grounds	10,120	Freehold
Haweswater Estate, Cumbria	Reservoir/gathering grounds	9,900	Freehold
Longdendale Estate, Derbyshire	Reservoir/gathering grounds	7,490	Freehold
West Pennine Moors Lancashire	Reservoir/gathering grounds	6,872	Freehold
Thirlmere Estate, Cumbria	Reservoir/gathering grounds	4 850	Freehold
Huntington, Cheshire	Water treatment works	107	Freehold
Prescot, Merseyside	Water treatment works	84	Freehold
Woodgate Hill, Greater Manchester	Water treatment works	40	Freehold

Note One hectare equals 2 47 acres

As at 31 March 2007, the principal wastewater operations facilities were as shown in table 3 below

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Location	Description	Hectares	Tenure
Davyhulme, Greater Manchester	Wastewater treatment works	89	Freehold
Shell Green, Widnes	Sludge processing centre	12	Freehold
Sandon Dock, Liverpool	Wastewater treatment works	8	Leasehold

As at 31 March 2007, the principal offices were as shown in table 4 below

Table 4 Owned by United Utilities Property Solutions Limited

Property	Use	Floor area in sq ft	Utilisation	Tenure
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Property	Use	Floor area in sq ft	Utilisation	Tenure
Lingley Mere, Warrington	Company offices	249,606	100%	Freehold
Winsford	Company offices	18,832	70%	Freehold

Third party owned

Property	Use	Floor area in sq ft	Utilisation	Tenure
Dalton House, Birchwood	Company offices	10,059	100%	Leasehold
Oakland House, Manchester	Company offices	40,732	100%	Leasehold

Our people

Leadership is key to business performance and culture

Table 1 People – key contributors to corporate success

Number of employees	2006/07	2005/06
United Utilities North West	**4,831**	4 775
United Utilities Contract Solutions	**3,539**	3,197
Vertex (discontinued operation)	**8,277**	8,203
Your Communications (discontinued operation)	**-**	653
Other activities	**221**	201
Average number of persons employed by the group during the year	**16,868**	17,029

• Substantially all of the group's employees are based in the United Kingdom

Employee involvement

The group seeks to involve employees with open and regular communications about business developments and issues of general interest, both formally and informally

An interim employee opinion survey was conducted in respect of nine key measures Employee satisfaction was 69 per cent compared with 74 per cent last year In future, surveys will be conducted annually in November Greater emphasis will be placed on understanding employees' views and concerns

Leadership

Leadership is key to business performance and culture In accordance with the objective of becoming a high performance organisation, we are providing our senior leaders with the skills to release their own, and develop their team's, potential In addition, our high performance team programme was rolled out to a further 177 teams in United Utilities North West

Industrial relations

Good industrial relations remain a priority for United Utilities across the whole of its business and parts of the group have been recognised in the UK for excellence in this area The group continues to recognise and work in partnership with a range of trade unions across the sectors in which it operates

A statement of principles governs the approach to labour relations across the group

Within United Utilities North West, approximately 60 per cent of employees are members of one of the five recognised trade unions, a figure which has been broadly stable over recent years However, around 99 per cent of employees within United Utilities North West are represented by trade unions for collective bargaining purposes, a process which is underpinned by principles contained within a voluntary collective agreement entitled 'Together in Partnership' Following an independent and comprehensive review and re-evaluation of the agreement, a series of joint initiatives has been put in place to develop this collaborative approach to employee relations further

Within United Utilities Contract Solutions, approximately 57 per cent of employees are now represented by trade unions for collective bargaining purposes Other employees are employed on personal contracts and are not covered by collective bargaining arrangements

A review of union relationships has taken place in a number of business areas and these are being managed at a local level due to the diverse nature of the business and the different contracts operated by the business As a consequence, consultation arrangements have been reviewed in all business areas and effective arrangements are now in place for all employee groups

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498

accidents per 100,000 employees

Accident incident rate of 498 per 100,000 for the year ended 31 March 2007 (2005/06: 548)

days lost due to accidents

A rate of 9,052 per 100,000 employees for the year ended 31 March 2007 (2005/06: 2,173, a rate of 11,564 per 100,000 employees)

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The group owns 58,500 hectares of catchment land to protect and improve the quality of raw water supplies

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Property	Use	Floor area in sq ft	Utilisation	Tenure
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Oakland House, Manchester	Company offices	40,732	100%	Leasehold

Non-GAAP measures

Providing an increased insight into the underlying performance of the business

The group gives certain additional information in order to provide an insight into the underlying performance of the business An explanation of this information is given below

Underlying operating profit from continuing operations*, and Underlying profit before taxation from continuing operations*

Underlying operating profit from continuing operations* can be derived from the consolidated income statement of the financial statements after adjusting for restructuring costs and other significant non-recurring items and is reconciled to operating profit from continuing operations in tables 5 and 6 on page 25

Underlying profit before taxation from continuing operations* can be derived from the consolidated income statement of the financial statements after adjusting for the group's share of results of its associated company, restructuring costs, other significant non-recurring items, fair value gains and losses on debt and derivative instruments and adding back the interest element relating to swaps and debt under the fair value option This is reconciled to profit before taxation from continuing operations in table 7 on page 25

The board believes that these financial measures align those reported to investors with the measures used by management to evaluate trading performance and allocate resources within the business

Management believes that these additional measures are of relevance in assessing the future direction of the group and the trends in trading performance

Although the board uses these non-GAAP (Generally Accepted Accounting Principles) financial measures to analyse trading performance, operating profit from continuing operations and profit before taxation from continuing operations as shown on the face of the consolidated income statement should also be considered

Segmental underlying operating profit from continuing operations*

Segmental underlying profit from continuing operations* can be derived from note 1 of the financial statements after adjusting for restructuring costs and other significant non-recurring items and is reconciled to the segmental analysis from note 1 of the financial statements in tables 5 and 6

The board considers that the removal of the impact of restructuring costs and other significant non-recurring items is of relevance in assessing the future direction of the segments and the trends in trading performance

Underlying interest payable from continuing operations* and underlying cost of net borrowings from continuing operations*

Underlying interest payable from continuing operations* can be derived from note 5 of the financial statements after adjusting for fair value gains and losses on debt and derivative instruments and adding back the interest element relating to swaps and debt under the fair value option Underlying cost of net borrowings from continuing operations* is then obtained by adjusting further for investment income and net pension interest income, which are derived from note 4 of the financial statements These measures are reconciled to notes 4 and 5 of the financial statements in table 8

Management considers that the removal of the volatility of fair value gains and losses arising on debt and derivative instruments provides a useful comparison of annual performance

*Where these non-GAAP measures are included elsewhere in the annual report (as indicated by the symbol) the above definitions should be referred to

Table 5

2006/07	United Utilities North West £m	United Utilities Contract Solutions £m	Other activities £m	Group £m
Segmental operating profit from continuing operations	**750 1**	**69 1**	**8 3**	**827 5**
Restructuring costs	**5 3**	**0 3**	**5 0**	**10 6**
Other one-off items				
Settlement claims	**(27 6)**	**(3 0)**	**–**	**(30 6)**
Ofwat transfer pricing penalty	**8 5**	**–**	**–**	**8 5**
	(13 8)	**(2 7)**	**5 0**	**(11 5)**
Segmental underlying operating profit from continuing operations	**736 3**	**66 4**	**13 3**	**816 0**

Table 6

2005/06	United Utilities North West £m	United Utilities Contract Solutions £m	Other activities £m	Group £m
Segmental operating profit from continuing operations	637 5	68 5	23 5	729 5
Restructuring costs	0 1	4 7	–	4 8
Other one-off items				
Write-off of IT systems	25 0	–	–	25 0
Profit on disposals	–	(6 4)	–	(6 4)
	25 1	(1 7)	–	23 4
Segmental underlying operating profit from continuing operations	662 6	66 8	23 5	752 9

Table 7

	2006/07 £m	2005/06 £m
Profit before taxation from continuing operations	**676 0**	445 1
Adjustment for share of results of associated company	**(18 7)**	–
Operating profit adjustments (see tables 5 and 6 above)	**(11 5)**	23 4
Fair value (gain)/loss on debt and derivative instruments	**(2.7)**	71 3
Interest on swaps and debt under fair value option	**(81 7)**	(55 4)
Underlying profit before taxation from continuing operations	**561 4**	484 4

Table 8

	2006/07 £m	2005/06 £m
Finance expense from continuing operations	**308 4**	352 9
Fair value gain/(loss) on debt and derivative instruments	**2 7**	(71 3)
Add back interest on swaps and debt under fair value option	**81 7**	55 4
Underlying interest payable from continuing operations	**392 8**	337 0
Investment income	**(138 2)**	(68 5)
Adjustment for net pension interest income	**25 1**	16 5
Underlying cost of net borrowings from continuing operations	**279 7**	285 0

Group results

Tim Weller
Chief financial officer

Performance summary

- > **Underlying profit before tax from continuing operations* up 15 9 per cent to £561.4 million**
- > **Segmental operating profit in United Utilities North West up by 17.7 per cent**
- > **Sale process initiated for United Utilities' electricity distribution assets**
- > **Vertex disposal completed creating a leaner, more focused company**
- > **£10 0 million of annual cost savings expected from management reorganisation**

Financial high	2006/07	2005/06	%
Revenue	**£2,323 0m**	£2,086 0m	11 4
Operating profit	**£827 5m**	£729 5m	13 4
Operating margin	**35 6%**	35 0%	

*Underlying profit measures are defined and reconciled to the group's income statement on pages 24 and 25

Revenue
£2,323.0m
Up 11 4 per cent from 2005/06

Operating profit
£827.5m
Up 13 4 per cent from 2005/06

Overview
United Utilities has again delivered a strong financial performance in the year to 31 March 2007 Underlying profit before tax from continuing operations* increased by 15 9 per cent to £561 4 million and underlying operating profit from continuing operations* was up by 8 4 per cent, to £816 0 million

United Utilities North West (UUNW) has delivered strong growth in the year with operating profit up 17 7 per cent Segmental underlying operating profit from continuing operations* in UUNW has increased by 11 1 per cent This growth primarily reflects the allowed price increases which support the substantial levels of capital investment being made by the company to improve operational standards and services for customers Capital investment in our regulated operations, including £101 2 million of infrastructure renewals expenditure, totalled £747 9 million during the year The board remains confident that regulatory operating and capital expenditure efficiency targets will be met

In United Utilities Contract Solutions, operational performance across the contract portfolio was good Underlying operating profit from continuing operations* was slightly below that of the previous year at £66 4 million Contract Solutions renewed its contract with Scottish Water through Scottish Water Solutions during the year, although new opportunities were limited The order book remains strong with future revenue streams secured

Strategy
The group's strategy is to focus on its core skills of managing water, wastewater, electricity and gas networks to create a world class operator of utility infrastructure This strategic focus has helped deliver operational and service improvements

Sale of electricity assets
The board has taken the decision to initiate a sale process for United Utilities' electricity distribution assets, with a view to maximising shareholder value We believe that shareholders' interests are best served by the group focusing on the much larger water asset base, which offers significantly more growth potential than its electricity assets

We expect to return the net equity proceeds from the proposed sale to shareholders The mechanism for this return will be determined at the time of sale completion

At the conclusion of this sale process, United Utilities intends to review its capital structure and dividend policy so that they will be appropriate for the revised composition of the group, recognising the importance of income to our shareholders

Furthermore, it is our intention that, as part of this capital restructuring, shareholders will realise total distributions over the remainder of the 2005-10 price control period at least equivalent to the distributions targeted for the same period under the current dividend policy, adjusted to take account of the manner in which the net equity proceeds are returned

The review of capital structure will also involve determining a target credit rating that the group believes best mirrors regulatory assumptions for United Utilities Water and we will be consulting with the credit rating agencies on appropriate financial indicators to maintain this rating

As part of the group's asset owner and asset operator management reorganisation initiative, a separate asset operator has been established that carries out capital delivery, operations and maintenance activities for United Utilities' electricity distribution assets We intend to continue operating these assets, consistent with our strategy of focusing on our core skills

Restructuring
The group's management organisation has been restructured around separate asset

operator and asset owner functions, to sharpen commercial focus and help deliver and sustain further performance improvements The business has been separated into an asset owner function, Asset Management and Regulation, and an asset operator function, Utility Solutions, which will be responsible for all of the group's UK utility operations, which were formerly held within UUNW and Contract Solutions

The new structure will help optimise performance by instilling the operational disciplines inherent in commercial trading arrangements and enabling greater sharing of best practice and utilisation of management capital It is expected that the overall management reorganisation initiative will deliver annual savings of around £10 million which are expected to be realised in full from 2008/09

Group financial performance
Revenue from continuing operations increased by 11 4 per cent to £2,323 0 million in 2006/07 compared with £2,086 0 million in 2005/06 These movements reflect growth across all of our businesses

Operating profit from continuing operations increased by 13 4 per cent in 2006/07 to £827 5 million Underlying operating profit from continuing operations* increased 8 4 per cent in 2006/07 to £816 0 million

The finance expense relating to continuing operations for the year was £308 4 million compared with £352 9 million in 2005/06 This expense includes considerable volatility in respect of fair value movements on debt and derivative financial instruments The underlying cost of net borrowings from continuing operations* for the year was £279 7 million compared with the prior year figure of £285 0 million

Profit before tax from continuing operations in 2006/07 increased by 51 9 per cent to £676 0 million Included within profit before tax from continuing operations is £18 7 million in relation to the group's share of the results of its associate, THUS Group plc Adjusting for the impact of this, other non-recurring items and for fair value gains and losses on debt and derivative instruments as shown in table 7, results in an underlying profit before tax from continuing operations* of £561 4 million, an increase of 15 9 per cent from the prior year

Basic earnings per share relating to continuing operations increased by 51 1 per cent to 57 1 pence in 2006/07 (2005/06 37 8 pence)

The total dividend per ordinary share for the year is 44 93 pence, an increase of 2 4 per cent from the prior year

Discontinued operations
On 26 March 2007, the group completed the sale of Vertex, in order to concentrate on the core skills of managing water, wastewater, electricity and gas networks The initial consideration was £217 5 million The total fair value of consideration was £192 9 million, comprising cash of £206 4 million, the repayment of intra-group debt and the assumption by the vendor of certain liabilities of Vertex The group recognised a loss on disposal of £65 1 million and assumed a liability in respect of deferred contingent consideration of £13 5 million, resulting in a total pre-tax loss on disposal of £78 6 million

Taxation
The current UK mainstream corporation tax charge in respect of continuing operations for 2006/07 reflects the high level of accelerated tax allowances arising from the capital investment undertaken by the group

The effective current tax charge relating to continuing operations is 11 5 per cent, compared with a charge of 11 1 per cent in 2005/06 Including deferred tax, there is an effective tax charge of 26 7 per cent, compared with 27 4 per cent in 2005/06

Cashflow
Net cash generated from continuing operating activities increased to £726 9 million, from £715 9 million in 2005/06

A significant level of capital investment continues to be made, mainly as a result of the water and wastewater capital investment programme The 2006/07 capital investment spend of £659 3 million in property, plant and equipment represents a 10 2 per cent increase over 2005/06, reflecting the planned rephasing of the AMP4 capital programme

Cash receipts of £206 4 million from the disposal of subsidiaries arose from the sale of Vertex

As a result of the above, cash and cash equivalents increased by £896 8 million in the year ended 31 March 2007

Borrowings net of cash and short-term deposits decreased by £225 6 million to £3,961 1 million at 31 March 2007 (£4,125 7 million including derivatives) Gearing, measured as borrowings net of cash and short-term deposits divided by total capital employed (being shareholders' equity plus borrowings net of cash and short-term deposits), decreased to 59 2 per cent compared with 61 4 per cent at 31 March 2006

Delisting from the New York Stock Exchange
On 30 May 2007, the company announced its intention to pursue a delisting from the New York Stock Exchange (NYSE) and deregistration under the US Securities Exchange Act of 1934 (the Exchange Act), with the aim of reducing compliance costs Annual savings of around £2 million are expected

The company has American Depositary Shares, evidenced by American Depositary Receipts (ADRs), listed on the NYSE and Securities and Exchange Commission (SEC) registered debt securities These US listings require SEC registration and the ongoing reporting and compliance obligations under both the Exchange Act and the 2002 Sarbanes-Oxley Act incur significant costs Deregistration will provide the company with exemption from meeting these US reporting and compliance requirements

Subsequent to its deregistration, the company intends to maintain its ADR facility with JPMorgan Chase Bank N A as a Level 1 programme This means that the company's ADRs will be traded on the over-the-counter market Accordingly, the company has not arranged for the listing of its ADRs on another national securities exchange

Summary and outlook
The group has again delivered a good set of results, supported by a robust financial performance in UUNW

On completion of the proposed sale of the electricity distribution assets, the board intends to assess and implement a capital structure and dividend policy in light of the revised composition of the group, recognising the importance of income to shareholders

By focusing on core skills, the business is well placed to meet expectations for the forthcoming year

United Utilities North West

Performance summary

> **Segmental revenue increased by 8 9 per cent to £1,636.2 million**
> **Segmental underlying operating profit from continuing operations* up 11.1 per cent to £736 3 million**
> **Capital investment for the year of £747 9 million**
> **Leakage level reduced to 468 megalitres per day**

Financial highlights	2006/07	2005/06	%
Segmental revenue	**£1,636.2m**	£1 502 9m	8 9
Segmental operating profit	**£750.1m**	£637 5m	17 7
Operating margin	**45 8%**	42 4%	

* Underlying profit measures are defined and reconciled to the group s income statement on pages 24 and 25

Segmental revenue
£1,636.2m
Up 8 9 per cent from 2005/06

Segmental operating profit
£750.1m
Up 17 7 per cent from 2005/06

Business objectives and strategy
United Utilities North West (UUNW) aims to be a world class operator of utility infrastructure and part of this goal is targeting an upper quartile position on key operational and service measures in the medium-term

In the group's interim results, announced on 5 December 2006, UUNW outlined a number of key operational and customer service measurements against which it would assess its performance Good progress has been made and the business remains on course to meet its medium-term targets on these measures, which include

- Relative efficiency – United Utilities Water (UUW) has improved its 2005/06 operating expenditure relative efficiency position, as assessed by Ofwat The company is now in band B for the water service and in band C for the wastewater service This represents a one band improvement for each service compared with the previous year, moving the company closer to the efficiency frontiers
- Security of water supply – UUW met the economic level of leakage rolling target of 470 megalitres per day for 2006/07 for the first time in five years In addition, there were no water restrictions in the year
- Pollution – the business has achieved a significant reduction in the number of category one and two pollution incidents in 2006/07, with no water pollution incidents (2005/06 two incidents) and only nine wastewater pollution incidents (2005/06 21 incidents) This performance already meets the medium-term target of reducing these incidents by around 50 per cent and the challenge for the business is to sustain performance at these levels and aim for out-performance against this target
- Sewer flooding – UUW is on track to meet its medium-term target of reducing the number of properties on the sewer flooding register by around 50 per cent This is defined as properties at risk of experiencing at least one sewer flooding incident in ten years Good progress was made in 2006/07 with a reduction of 152 properties, leaving 492 properties on the register
- Customer minutes lost (CMLs) and customer interruptions (CIs) – United Utilities Electricity (UUE) met the 2006/07 regulatory targets for CMLs and CIs set by Ofgem, which is in line with the aim to meet or out-perform the regulatory targets over the 2005-10 period
- Overall customer satisfaction – good progress continues to be made, 74 per cent of UUW's water customers and 69 per cent of UUE's electricity customers who had made an enquiry, were satisfied with the overall service they received This compares with a start point satisfaction level of less than 50 per cent for water and wastewater customers and less than 70 per cent for electricity customers

Financial highlights
Revenue increased by 8 9 per cent to £1,636 2 million in 2006/07, principally as a result of allowed price increases, including inflation, of 8 8 per cent in the water business and 2 6 per cent in the electricity business These price increases support the regulated businesses' substantial capital investment programmes to deliver improvements for customers

Segmental operating profit for the year increased by 17 7 per cent to £750 1 million (2005/06 £637 5 million), which reflects allowed price increases and delivery of efficiencies As expected, infrastructure renewals expenditure was higher in the second half of the year compared with the first six months, in line with the planned rephasing of this programme After adjusting for a number of one-off items, segmental underlying operating profit* increased by 11 1 per cent to £736 3 million

Capital investment in the period, including £101 2 million of infrastructure renewals expenditure, was £747 9 million (2005/06 £582 5 million), of which £570 3 million (2005/06 £440 9 million) related to water and wastewater and £177 6 million (2005/06 £141 6 million) to electricity distribution This represents an increase in expenditure of £165 4 million when compared with the previous year

The rise in capital expenditure is consistent with the planned rephasing of the company's investment programme to help optimise the delivery of outputs Cumulative water capital expenditure remains on track to match regulatory assumptions by 2008 and cumulative wastewater capital expenditure by 2009

The financial performance figures take account of an £8 5 million penalty from Ofwat for historical trading arrangements with associated companies The effect of these trading arrangements had already been excluded from impacting customer bills for the 2005-10 price control period Following review, the company believes it is now fully compliant with the transfer pricing requirements

Business efficiency

Progress on delivering efficiencies has been good and the business remains on course to meet its regulatory efficiency targets The customer transformation programme is progressing well and the new customer billing system is delivering efficiencies, alongside improved cash collection

The business has improved efficiency at its large wastewater treatment plants and the process and optimisation programmes are delivering benefits New work planning and scheduling processes, which make better use of mobile technology, are now embedded in the business and the project and investment management system is helping to optimise the delivery of outputs

Although energy costs in UUW have increased by just over 30 per cent in 2006/07 compared with the previous year, energy costs only represent around six per cent of the total cost base of the business Energy costs in future years are anticipated to be slightly lower than those incurred in 2006/07 UUW continues to benefit from a largely gravity-fed clean water system, which substantially reduces pumping costs In addition, the business is focusing on increasing its renewable energy generation to mitigate costs further

Unsatisfactory intermittent discharges

In the previous price control period (2000-05), around £200 million of funding was provided to deliver a number of obligations, primarily relating to unsatisfactory intermittent discharges (UIDs) of wastewater for that period, which have been carried over into 2005-10 UUW, in its negotiations with the Environment Agency and Ofwat, is seeking to finalise requirements relating to those UID outputs The business expects the bulk of this capital expenditure to be incurred over the next two to three years

At the last water price review, it was also recognised that there was potential for additional investment relating to projects that were not part of United Utilities' 2005-10 regulatory contract, but which may be confirmed as additional obligations during this period by the regulators These potential projects, which primarily relate to UIDs of wastewater, with an estimated maximum value of up to £500 million, continue to be the subject of investigations and studies which are driving discussions with the regulators

A planning inquiry was held in October 2006 which considered three prime case appeals for discharging to inland waters to help establish principles going forward The inspector's findings were published in January 2007 Based on the outcome of the inquiry, United Utilities is currently preparing a submission to Ofwat which, if endorsed by the Department for Environment, Food and Rural Affairs, should allow the related investment programme, estimated to be over £200 million, to be funded through price limits and deliver additional growth in the regulatory asset value (RAV) A further planning inquiry relating to coastal discharges is expected to be held later this financial year The outcome of this inquiry may also result in additional investment and RAV growth

Capital programme

With regard to capital programme outputs, UUW continues to exceed its regulatory and business plan targets During the year, 810 kilometres of water mains were replaced and good progress was made in removing a number of properties from the low pressure and flooding registers The quality of drinking water remains high and mean zonal compliance for 2006 was 99 92 per cent

The delivery of United Utilities' previous investment programme has confirmed the success of its framework contractor approach, which was put in place during AMP3

The delivery strategy for AMP4 (2005-2010) builds on this success with appointed partners helping to deliver its £2 9 billion water and wastewater programme during the regulatory period The group takes a leading role in programme management, increasing its internal resources in engineering and design and placing a greater emphasis on performance management through the alignment of financial targets with partners and benchmarking out-turn results These changes will help the group deliver the capital efficiencies required by Ofwat

UUE places a strong focus on maintaining the integrity, security and safety of its electricity distribution network and outputs remain in line with its five-year delivery plan During the year, the business replaced or refurbished 293 kilometres of overhead lines and replaced 91 kilometres of underground cables It also replaced or refurbished 579 switchgear units and replaced 280 transformers

Price review and customer debt

In its final determination in December 2004, Ofwat allowed UUW an average annual real price increase of 4 5 per cent over the next five years to support environmental and operational improvements for customers Ofgem allowed United Utilities Electricity a real price increase of 8 2 per cent in 2005/06, followed by constant real prices thereafter

United Utilities offers a range of initiatives to help customers who have difficulty paying bills such as the vulnerable customer tariff, an arrears allowance scheme and money advice services UUNW has taken a leading role in the Debt Focus Group of Water UK, an industry-wide body, looking at ways to improve the Department for Work and Pensions' 'Water Direct' scheme It continues to lobby for changes to the benefits system to extend the range of benefits from which deductions can be made and to improve the take-up of such schemes

United Utilities Contract Solutions

Performance summary

- **Segmental revenue increased by 13.4 per cent to £742.2 million**
- **Segmental underlying operating profit from continuing operations* is slightly down at £66.4 million**
- **Total order book standing at more than £4.5 billion**
- **First full year of the £1.1 billion Northern Gas Network contract**

Financial highlights	2006/07	2005/06	%
Segmental revenue	**£742.2m**	£654 5m	13 4
Segmental operating profit	**£69 1m**	£68 5m	0 9
Operating margin	**9 3%**	10 5%	

Underlying profit measures are defined and reconciled to the group s income statement on pages 24 and 25

Segmental revenue
£742.2m
Up 13 4 per cent from 2005/06

Segmental operating profit
£69.1m
Up 0 9 per cent from 2005/06

Business objectives and strategy
United Utilities Contract Solutions applies the core utility skills of United Utilities North West through outsourcing contracts, and is involved in the operation or management of assets representing around 35 per cent of the UK water industry's asset base The business also provides gas services to over six million people and in total now serves a population of around 17 million in the UK UUCS has an order book worth more than £4 5 billion

Financial highlights
Revenue in Contract Solutions increased by 13 4 per cent to £742 2 million in 2006/07 This partly reflects a 12-month contribution in 2006/07 from the £1 1 billion, eight-year contract with Northern Gas Networks which commenced on 1 June 2005 Revenue also benefited from the planned capital investment profile relating to the Southern Water contract, which provided a strong contribution in the year

Segmental operating profit was broadly flat at £69 1 million in 2006/07, reflecting the increasing maturity of contracts, the successful transformation of the major outsourcing contracts and continued performance improvements in the Connections and Metering business units

Segmental underlying operating profit from continuing operations* for the year decreased slightly to £66 4 million

Business performance
Contract Solutions has grown rapidly since its creation in 2000 with the total order book now standing at more than £4 5 billion

The disciplines of operating within robust contractual frameworks encourages a healthy commercial tension that has helped the business balance risk and reward and ensure that significant focus is placed on improving performance This experience has improved the commercial skillsets of the business and places it in a strong position from which to pursue other infrastructure outsourcing opportunities

The business has a 40 per cent share in the 4D consortium which secured a five-year capital delivery contract with Southern Water worth around £750 million The contract commenced on 1 April 2005 and performance continues to be good Around half of the contract spend had been delivered by the end of 2006/07 and delivery of outputs is in line with Southern Water's expectations This planned investment profile has resulted in a strong contribution from this contract in the year and a natural reduction in contribution is expected in the forthcoming financial year

Contract Solutions holds a £1 5 billion, 15-year contract with Dŵr Cymru Welsh Water to provide operations, maintenance and shared services, which commenced in April 2005 This contract was renewed following the successful delivery of an initial four-year contract with Dŵr Cymru Welsh Water The contract is progressing well and, despite inflationary cost pressures, the profit level has moderately increased compared with the previous year Performance against the contract key performance indicators (KPIs) is good and Contract Solutions has helped Dŵr Cymru Welsh Water achieve the regulatory economic level of leakage rolling target for 2006/07 and sustain an upper quartile position in Ofwat's overall performance assessment league table for the last four years

United Utilities acquired a 15 per cent stake in the CKI-led consortium (Northern Gas Networks) that purchased the north of England gas distribution network from National Grid in early 2005/06 Contract Solutions also won a £1 1 billion, eight-year contract to operate and maintain the network, and manage the capital expenditure programme, on behalf of the consortium, which commenced on 1 June 2005, and performance has been robust

The final proposals for the gas distribution price review were published in December 2006, covering the one-year period 1 April 2007 to 31 March 2008 The proposals were accepted, with an allowed increase in revenue for the one-year period of 8 7 per cent real The next price control will cover the period 1 April 2008 to 31 March 2013 and will be subject to detailed regulatory consultation throughout 2007/08

The Northern Gas Networks contract covers the management of around 36,000 kilometres of gas mains, serving a population of more than six million 2006/07 was the first full year of operations, and saw excellent progress against the client's gas mains replacement programme, with the 520 kilometres target achieved in the year

Earlier in the year, Scottish Water Solutions (SWS), a joint venture company in which Contract Solutions is a key partner, was successful in winning a new £760 million contract with Scottish Water to deliver a substantial part of its 2006-10 capital investment programme

This follows on from a similar contract SWS held with Scottish Water covering the 2002-06 period and a good performance on this initial contract helped in achieving this contract win In addition, there is potential to secure further programme management related work, over the new contract period, with an estimated value of £240 million Contract Solutions' share of this potential combined contract is estimated to be worth around £150 million Performance in relation to the contract KPIs, delivery of outputs and in the area of health and safety is good

Contract Solutions won the first major meter installation contract to be outsourced with British Gas Trading in 2002 and the contract has around one year to run The business is responsible for full meter provision and management services to approximately five million gas and electricity customers in the north of England and Wales It provides a 24 hour, 365 day operation covering meter replacement, emergency response services and customer requested work It also operates a dedicated operational call centre By the end of the contract, it is anticipated that approximately 1 9 million gas meters and 800,000 electricity meters will have been installed The initial value of the contract was £225 million and this was subsequently increased to £276 million The contract continues to progress well

The Contract Solutions' Connections business continued to improve its financial performance during the year following a refocusing in 2005/06 of its sales and marketing effort towards long-term strategic customers and larger projects In August 2006 the business commenced a major new £133 million seven-year gas connections contract with Northern Gas Networks

The five-year contract with the Atomic Weapons Establishment to operate and maintain their water and wastewater assets continues to perform well, with potential for further growth opportunities The contract provides for a potential extension to 20 years and the provision of ancillary services, such as capital maintenance The services do not include handling radioactive or contaminant discharges

In addition, the business applies the group's core skills in related international markets and currently operates concessions in Bulgaria, Estonia, Poland, the Philippines and Australia

Summary and outlook

Contract Solutions holds major utility outsourcing contracts in the United Kingdom with Dŵr Cymru Welsh Water, Southern Water, Scottish Water, and Northern Gas Networks It also has a meter installation contract with British Gas Trading and three Scottish Private Finance Initiative operations The order book remains strong with future revenue streams secured and Contract Solutions remains the leading utility infrastructure outsourcing company in the UK water sector Performance across the contract portfolio is in line with management expectations

Liquidity and capital resources

The group's primary source of liquidity is cash generated from its ongoing business operations As reflected in the consolidated cashflow statement on page 73, in the year ended 31 March 2007, net cash generated from the group's continuing operating activities was £726 9 million, compared with £715 9 million in 2005/06 The water regulator and the electricity regulator have established price increase limits to 2010 which will provide certainty for a major element of the group's revenues from ongoing operations, providing both a stable and a predictable source of funds

Treasury policy

The group's treasury function operates within policies approved by the board, it does not act as a profit centre and does not undertake any speculative trading activity Long-term borrowings are structured or hedged to match earnings, which are largely in sterling, indexed to inflation and subject to regulatory price reviews every five years Index-linked debt is the preferred method of funding Over the last two years, the group has made significant progress in raising this type of funding, holding £1 36 billion of index-linked debt at the year end The longer-dated nature of this funding provides a good match to the group's long life infrastructure assets Exposure to interest rate movements for the following 12 months, where necessary, are eliminated at the start of each financial year using short-term hedges The credit quality of counterparties and individual aggregate exposures are reviewed annually

Debt financing

Moody's Investor Service rates the credit of United Utilities PLC as A3 on a long-term basis with a stable outlook and P-2 on a short-term basis Equivalent ratings published by Standard and Poor's Rating Services were BBB+ long-term with a stable outlook and A-2 short-term during the year On 2 April 2007, Standard and Poor upgraded its rating to A- long-term with a stable outlook and A-1 short-term

Details of borrowings and net cash and cash equivalents are provided in notes 16, 17 and 18 to the consolidated financial statements

Short-term liquidity

Short-term liquidity requirements are met from the group's normal operating cashflow Further liquidity is provided by cash and short-term deposit balances, the company's US$1 5 billion euro-commercial paper programme, supported by committed bank facilities and committed but undrawn long-term credit facilities

Long-term liquidity

The group has effective access to the international debt capital markets through its €7 billion medium-term note programme which provides for the periodic issuance by United Utilities, United Utilities Water and United Utilities Electricity of debt instruments on terms and conditions determined at the time that the instruments are issued

The programme does not represent a funding commitment, with funding only becoming committed when debt securities have been successfully issued The currencies in which borrowings are held are disclosed in note 18 to the consolidated financial statements

Interest rate management

The group manages interest rate exposure by seeking to match financing costs as closely as possible with the revenues generated by its assets The group's exposure to interest rate fluctuations is periodically managed in the medium-term through the use of interest rate swaps and the use of financial futures contracts traded on the London International Financial Futures and Options Exchange The average interest rate for 2006/07 was 6 55 per cent, compared with 6 84 per cent in 2005/06 excluding fair value adjustments

Quantitative and qualitative disclosures about market risk

Risk management

The principal financial market risks faced by the group are the risks of interest rate movements and foreign currency movements

Interest rate and foreign currency management

The group uses a combination of interest rate swaps, futures and funding instruments to hedge exposure to interest rate volatility The company's use of derivative instruments relates directly to underlying indebtedness No speculative transactions are undertaken The proportion of borrowings at effective fixed rates of interest for a period greater than one year is set in conjunction with the level of floating rate borrowings and projected regulatory revenues that are exposed to inflationary adjustments (index-linked) In addition, the company aims to manage its short-term budgetary commitments by ensuring that the majority of floating rate interest is fixed for periods of less than one year through the use of exchange traded financial futures The group has limited exposure to foreign currency exchange rate movements Interest rate management and funding policies are set by the board

Quantitative disclosure of market risk

The analysis in note 18 to the consolidated financial statements details the sensitivity of the market value of the group's financial instruments to selected changes in market rates and prices The range of changes chosen reflects the group's view of changes that are reasonably possible over a one-year period Market values are quoted values, or, where these are not available, those values are obtained by discounting cashflows at market rates and prices The market values for interest rate risk are calculated by using a standard zero coupon discounted cashflow pricing model For long-term borrowings, a favourable change in market value results in a decline in the value of borrowings For other financial instruments, a favourable change in market value results in an increase in market value

Contractual obligations

Financial guarantees are given by United Utilities in support of borrowings by subsidiary companies, where the underlying obligation is already reflected in the disclosure of long-term debt Financial guarantees of £703 7 million relate to borrowings by United Utilities Water and United Utilities Electricity from the European Investment Bank (EIB)

The capital commitments of the group as at 31 March 2007 were £370 7 million, for which the group has contractual commitments for property, plant and equipment The group also has obligations under its licence to comply with the capital programmes as specified by the regulators The purchase obligations of the group as at 31 March 2007 total £48 0 million and primarily relate to services for which the group has purchase orders or contractual commitments

Off-balance sheet arrangements

Joint ventures

The group enters into joint ventures with consortium partners The financial and legal structure of joint ventures is designed to limit the group's exposure to the extent of the equity investment and loans provided by the group, with no further recourse should the joint venture default All joint venture arrangements have been incorporated into the group's results on a proportionate consolidation accounting basis The joint venture normally enters into the main contract with the customer, for example, by taking on ownership of the assets subject to the contract The consortium partners may then enter into subcontracts with the joint venture for the provision of services appropriate to their expertise This enables the group to take on only those risks that fall within its normal commercial expertise, such as infrastructure management, whilst other parties will provide their skills to the joint venture and take on their risks accordingly, for example, design and construction However, the performance of any joint venture will affect the group's financial performance to the extent of its interest in such a joint venture

Performance guarantees

As part of the commercial operations of the group, performance guarantees are sometimes required by clients These guarantees may be called where the standards of service set out within the relevant contract are not fulfilled, and other possible remedies under the contract are not successful Total guarantees as at 31 March 2007, where a financial limit has been specified, were £134 1 million

A guarantee which has unlimited liability is supported by an indemnification agreement from a third party external to the United Utilities group This indemnification agreement follows the disposal of certain operations to a third party, and contains no limit on the value of indemnity available Therefore any payments under this guarantee may be fully recoverable from the third party

In certain circumstances, the group has issued guarantees and performance bonds to support its contribution to the performance of partnership companies In some instances, the partnership company is responsible for arranging the issue of the guarantee and the partners are required to provide an indemnity to the issuing financial institution for a share of that guarantee, usually in proportion to the respective shareholdings in the partnership company Where this is the case, recovery of any amounts paid under the guarantee will be in proportion to the indemnities provided Therefore, the full value of the guarantee arranged by the group would only become payable if the total project guarantee were to be payable in full

Alternatively, the partners may be required to arrange the issue of separate guarantees directly to the client, normally contributing to the total guarantee requirement in proportion to the shareholding in the partnership company In most cases, these arrangements are supported by cross-indemnities from the partners so that the partners must pay a proportionate share of any claim under any of the individual guarantees issued Therefore, the full value of the guarantee arranged by the group will only become payable if the total project guarantee is called in full Guarantees issued by the group directly to the client, supporting the performance of partnership companies, totalled £100 0 million at 31 March 2007 This includes guarantees of up to £51 3 million, which are supported by cash held in escrow to secure the cross-indemnity from partners

The value of indemnities issued to financial institutions by the group, in order to support the issue of a guarantee by the financial institution on behalf of the partnership company, totalled £13 6 million at 31 March 2007

Guarantees totalling £13 9 million relate to the disposal of certain operations and reflect the capped value of indemnities issued to the purchaser for pre-completion events It is anticipated that, in the event of a claim, the group may be able to recover funds from its insurers, although this will depend upon the circumstances of the incident giving rise to the claim under the indemnity

An additional guarantee for £5 4 million relates to the disposal of other operations and reflects guaranteed obligations under a property lease Under the sale and purchase agreement the buyer is obliged to put in place a replacement guarantee and in parallel provide an indemnity to United Utilities Therefore any payments under these guarantees may be fully recoverable from the buyer The carrying value of the guarantees discussed above has been £nil for the past two fiscal years

Inflation

Inflation affects revenue, operating expense and finance expense However, the impact of inflation has not had a material effect on the group's operating results during the year

Summary

The board has reviewed its business plan and considers that the group has sufficient liquidity to meet the anticipated financial commitments for the next 12 months In total, at 31 March 2007, unutilised committed facilities of £1,172 2 million expiring in more than one year, together with cash and short-term deposits of £2,403 3 million and undrawn funding from EIB of £50 0 million, provide substantial pre-funding for the group

Corporate responsibility

The board believes that being responsible in the way it conducts its operations makes sound business sense

Active management of its key environmental, social and economic impacts helps the group work in a way that is ethical and balances the needs of all of its stakeholders It enables the group to reduce risk, identify business opportunities, provide stability in its markets, protect resources, make savings, improve performance and build trust and understanding

Code of ethics
The group has adopted a set of business principles It will continue to develop them in line with best practice A free copy of the business principles booklet is available upon request from the company secretary, United Utilities PLC, Haweswater House, Lingley Mere Business Park, Lingley Green Avenue, Great Sankey, Warrington, WA5 3LP, England or may be viewed on our website at www unitedutilities com

Our approach
The business principles guide the way the group manages its activities and its relationships with stakeholders and set the context for the group's approach to corporate responsibility

The group's corporate responsibility policies are considered as part of the business planning process and corporate responsibility performance is a personal objective for each member of the executive leadership team (ELT) Members of the ELT meet regularly to discuss the key social and environmental issues and have determined a process which identifies and prioritises our impacts and opportunities

An important part of this process is stakeholder consultation, which provides an understanding of the interests and priorities of the different groups of people who are affected by the group's activities More information on the group's stakeholder approach, identification of key impact areas and detailed information, performance data and discussion can be found in the stakeholder report, or on our website at www unitedutilities com

Formal management systems cover many of the group's impact areas, including environment, health and safety and quality Where appropriate, we seek formal certification of these systems Most of the group's operations are covered by the ISO 140W accreditation for environmental management Benchmarking exercises help us to track performance, drive continual improvement and establish best practice

Environment
Our operations can have significant environmental impacts Our key focus areas are to improve compliance standards at our water and wastewater treatment works whilst at the same time reduce the amount of energy we use We aim to minimise our environmental impacts in terms of pollution incidents and manage the demand on the water and wastewater networks

Regulation
In north west England, we met our compliance standards at wastewater treatment works serving 98 99 per cent of the population, a reduction from last year due to failures at three of our wastewater treatment works Pollution incidents have fallen to 152 from 165 last year The most serious, category one and two pollution incidents, reduced to nine from 23 last year Convictions increased, with 11 prosecutions relating to wastewater resulting in fines of £137,300 in 2006, compared with £47,500 in 2005

Last year, the annual report by the Drinking Water Inspectorate showed that the overall quality of drinking water in the north west had improved for the 12th year in succession In 2006, drinking water compliance at customers' taps was 99 91 per cent (2005 99 90 per cent)

Regional bacteriological compliance at wastewater treatment works has improved significantly, with the number of infringements reducing from 81 in 2003 to seven in 2006 This improvement was achieved through the implementation of operational best practice, improved plant maintenance, sampling changes and capital investment

Climate change
United Utilities is a major user of energy, using around 0 3 per cent of the UK's electricity supply, mainly to transport and treat water In 2006/07 we used 1,121GWh of electricity

From our assets and activities, we emit several greenhouse gases including carbon dioxide, methane and nitrous oxide In 2005/06, these emissions were the equivalent to 0 49 million tonnes of carbon dioxide A further 1 66 million tonnes were emitted by operations that we manage but do not own Largely produced by losses from electricity distribution and by direct methane emissions from the gas network, these bring our overall carbon dioxide equivalent to a total of 2 15 million tonnes

In 2006, we set up a carbon management forum to bring greater focus to our emissions management The forum commissioned a six-month programme with the Carbon Trust to establish our carbon footprint and devise a mitigation plan

We are the first UK water company to set out a £37 million action plan that will reduce our carbon dioxide emissions by a total of eight per cent on 2005/06 figures by 2012 The reduction is the equivalent of taking more than 9,000 cars off the road We aim to reverse our trend of rising emissions and will buy almost a quarter of our energy from renewable sources for the next three years This will cut our emissions by a further 17 6 per cent, although this offsetting is not included in our overall target

We are taking steps to improve energy efficiency and introduce more sustainable sources of energy In north west England we have 17 combined heat and power (CHP) plants fuelled by methane produced from wastewater treatment with plans to increase the number of CHP units to 23

Leakage

In north west England, we have halved water leakage since 1995 and out-performed the rolling average target of 470 Ml per day for 2006/07 by achieving 468 Ml per day, meeting our agreed target with Ofwat The sustained programme of investment in renewing ageing mains, supported by new technologies to help us detect leaks, should continue to reduce leakage for the year ahead

We are spending £361 million on managing, maintaining and upgrading the water network and fixing leaks between 2005 and 2010 We are also working with the Environment Agency on a water efficiency campaign entitled 'Don't waste it, we all need it' This involves advertising on local radio and features in the regional press to encourage everyone to consider how they currently use water and look for ways to use it wisely

Waste management

The majority of our sludge is recycled to agricultural land or used for restoration and reclamation However, the land bank available for sludge is reducing as tighter regulations come into force We are therefore pursuing a mixed strategy which will involve recycling to land and thermal destruction with energy recovery where possible This is to ensure that we can avoid landfill as a disposal route should the land bank reduce still further In all, 68 per cent of wastewater sludge is now recycled to agricultural land, six per cent is used in restoration and reclamation and the remainder is incinerated

Land and rural issues

Leighton Moss nature reserve, near Carnforth, is the first place in north west England to benefit from a project to relay cables underground for purely aesthetic reasons This scheme forms part of United Utilities' £640 million investment programme to improve the electricity distribution system in north west England between 2005 and 2010 The complete programme of work includes areas in the Lake District National Park and Forest of Bowland, all of which will be completed by 2010

Workplace

We are committed to training and developing our employees and we seek to involve them with open and regular communications about business developments For further information see page 20

Health and safety

We seek continual improvement in our health and safety performance For further information on health and safety see page 20

Business continuity

Business continuity in United Utilities is monitored and controlled by the Business Continuity Steering Group The group reports to the ELT Escalation paths exist from both line management and a 'Virtual Watch' team that monitors potential threats

During 2006/07, the Business Continuity Policy was updated and crisis management capabilities and facilities enhanced Initiatives included pandemic planning consistent with central government advice

Investigations on communications resilience included early planning for implementation of '21st Century' data networks United Utilities remains an active participant in UK emergency preparedness, chairing the Regional Utilities Resilience Forum, representing all utilities on the Regional Resilience Forum and participating in the Regional Civil Contingencies Committee
for north west England

Community impact

We support community activity, investing company resources in partnerships and projects where we can share benefits with local communities

Our support includes financial assistance as well as employee time and in-kind help In 2006/07, we invested £3 1 million, around 0 5 per cent of our pre-tax profits

Our businesses have relationships with a wide range of community stakeholders, and most of our community investment is made through these links We have revised our employee initiatives by offering community grants to employees who volunteer more than 80 hours a year of their own time

Internationally, we continue to support programmes of local community involvement, with particular emphasis on water projects, young people and social welfare projects For example, as part of our Sofiyska Voda contract in Bulgaria each year we host a water festival to educate children on water as a precious resource

We also work in partnership on specific projects with Groundwork UK, WaterAid and the Royal Society for the Protection of Birds

Risk factors

Cautionary statement regarding forward-looking statements
Certain statements included or incorporated by reference within the annual report may constitute 'forward-looking statements' Forward-looking statements are based on expectations, forecasts and assumptions by our management and involve a number of risks, uncertainties, and other factors that could cause actual results to differ materially from those stated

The board considers the following risks to be the principal ones that might affect the group's performance and results but cautions that the risks listed in this section do not address all the factors that could cause results to differ materially

There may be additional risks that the group does not currently know of, or that are deemed immaterial based on either information currently available or the group's current assessment of the risk The group's business, financial condition or results of operations could be materially affected by any of these risks, resulting in a decline in the trading price of the group's ordinary shares The group operates an internal control system to evaluate and manage risks as described in the section 'Internal control' on page 49

All the information supplied in the chairman's and chief executive's statements on pages 4 to 6 and the business review on pages 7 to 38 form part of the directors' report as incorporated by reference Any liability for the information is restricted to the extent prescribed by the Companies Act 2006

Revenue of the group's regulated businesses is substantially influenced by regulators, which could adversely affect profitability
The revenue and profitability of the group's water, wastewater and electricity distribution businesses (the regulated businesses) are substantially influenced by price limits established every five years by the respective regulators Price reviews for the regulated businesses covering the five-year period commencing on 1 April 2005 were determined by the electricity regulator in November 2004 and by the water regulator in December 2004 The group has accepted both of these determinations and has not exercised its right to appeal against adverse price determinations to the Competition Commission

An adverse price determination may occur as a result of a number of factors, including an inadequate allowed cost of capital or unrealistic regulatory assumptions concerning operating expenses, required capital expenditure and revenue forecasts

Scope to re-open these price controls within the charging period is limited In the case of the water and wastewater business, there are provisions for Interim Determinations of K ('IDoK') and the application of the 'shipwreck clause'

There is no equivalent provision that allows for the re-opening of electricity distribution price limits However, specific re-opening provisions have been made, with effect from 1 April 2005, in relation to uncertain costs associated with specified provisions of the Electricity Safety, Quality and Continuity Regulations 2002 (or amending/replacement regulations), the New Roads and Street Works Act 1991 and the Traffic Management Act 2004

Failure to deliver the capital investment programmes could adversely affect profitability
United Utilities' regulated businesses require significant capital expenditure for additions to, or replacement of, plant and equipment for their water, wastewater and electricity distribution facilities and networks The price limits set by the respective regulators take into account the level of capital expenditure expected to be incurred during the relevant five-year price review period and the associated funding costs

Historically, the group has financed the expenditure from cashflows from operations and from debt financing There can be no assurance that cashflows from operations will not decline, or that additional debt financing or other sources of capital will be available to meet these requirements

If the group is unable to deliver the capital programme at expected expenditure levels, is unable to secure the expected capital efficiencies associated with the capital programme, the programme falls behind schedule for other reasons, or adverse legacy effects of earlier capital investment emerge, the group's profitability may suffer The regulators may factor such failure into future price reviews In addition, the group's ability to meet regulatory and environmental performance standards could be adversely affected by such failure, which may result in fines or other sanctions

The group is currently in discussions with Ofwat and the Environment Agency in relation to the scope of works required in order to complete that part of its capital programme for the last charging period (i e 2000-05) which related to limiting pollution from stormwater overflows These are referred to by the Environment Agency as 'Unsatisfactory Intermittent Discharges' ('UIDs')

This means that some of these works are being delayed until the required scope is determined Once the cost of the scope of works is finally determined, it may be more than the amounts that have been allowed for by Ofwat in the 1999 and 2004 price reviews In such cases the company will seek to process the resulting changes through Ofwat's protocol for dealing with changes to the regulatory contract (the 'change protocol')

In respect of those UIDs which were the subject of the company's 2003 interim determination, Ofwat has stated that additional costs of completing these works will be recoverable through future price reviews provided that they meet Ofwat's conditions for recovery under the change protocol In respect of the UIDs which were not dealt with in the 2003 interim determination, Ofwat has given a similar confirmation in relation to those which the company considers present the greatest risk of significantly exceeding the costs assumed in the 1999 price review The group cannot be certain, however, that all these additional costs will be recoverable on this basis and will not adversely affect its profitability or financial position

Failure to deliver operational performance or cost savings implicit in the regulatory reviews could adversely affect profitability
Operating cost savings to be achieved during the current five-year regulatory period are implicit in the regulatory reviews To assist the achievement of these operating cost savings, a business change programme is underway If the operating cost savings were not achieved,

or the business change programme was not delivered, then the group's profitability would suffer Similarly, if operational performance was to deteriorate, this may be reflected by less favourable outcomes from future price reviews and the group's profitability would suffer

Environmental regulations could increase the group's costs and adversely affect profitability

Various government environmental protection and health and safety laws and regulations govern the water, wastewater and electricity distribution businesses These laws and regulations establish, amongst other things, standards for drinking water, discharges into the environment and the quality of electricity supply, which affect the group's operations

In addition, the group is required to obtain various environmental permissions from regulatory agencies for its operations The group endeavours to comply with all regulatory standards However, historically the group has not been in total compliance and cannot guarantee in the future that it will be in total compliance at all times with these laws and regulations Should the group fail to comply, it would face fines imposed by the courts or otherwise face sanction by the regulators

Environmental laws and regulations are complex and change frequently These laws, and their enforcement, have tended to become more stringent over time Whilst management believes it has taken into account the future capital and operating expenditures necessary to achieve and maintain compliance with current and known future changes in laws and regulations, it is possible that new or stricter standards could be imposed, or current interpretation of existing legislation could be amended, which will increase the group's operating costs by requiring changes or modifications to the assets in order to comply with environmental laws and regulations

Although these costs may be recoverable in part through the regulatory process of setting appropriate future price limits, there can be no assurance of this Therefore, the group cannot guarantee that the costs of complying with, or discharging its liabilities under, current and future environmental and health and safety laws will not adversely affect its profitability or financial position

Service interruptions or contamination of water supplies could adversely affect profitability

In addition to the capital investment programmes, United Utilities' regulated businesses control and operate water, wastewater and electricity networks and undertake maintenance of the associated assets with the objective of providing a continuous service

Historically, there have been interruptions to the supply of services One example is the severe storm in January 2005 which damaged the electricity network supply to 250,000 customers in Cumbria and Lancashire However, the majority of interruptions relate to minor issues that are rectified promptly

During 2006/07, there were an unusually high number of interruptions in total, which led to a few long duration interruptions and a number of interruptions affecting a large number of customers However there were no instances combining long duration and high numbers affected Nevertheless, the failure of a key asset could cause a more significant interruption to the supply of services (in terms of duration or number of customers affected), which may have an adverse effect on the group's operating results or financial position

Water supplies may be subject to contamination, including contamination from the development of naturally occurring compounds and pollution from man-made sources or third parties' actions In the event that water supply is contaminated and the group is unable to substitute water supply from an uncontaminated water source, or to treat adequately the contaminated water source, the regulated business is required to provide a statutory minimum alternative water supply quantity within a stipulated period until piped supplies can be restored The group could also be held liable for human exposure to hazardous substances in its water supplies or other environmental damage

Although the group has continued to refine its contingency planning process, it is only possible to be reasonably, but not absolutely, certain that such measures will be effective in managing large-scale incidents to the satisfaction of its customers, regulators and the wider stakeholder community Consequently, it is possible there may be an adverse effect on the group's operating results or financial position

It is possible that some of the costs associated with service interruptions or contaminations may be partly recoverable through the shipwreck clause or future price reviews The group maintains insurance policies in relation to legal liabilities likely to be associated with these risks, although there can be no assurance that all costs of any such claims would be covered or that coverage will continue to be available in the future

Non-recovery of customer debt could adversely affect profitability

United Utilities North West manages the billing, cash collection and debt management activities for 3 2 million domestic and business wastewater and water customers The Water Industry Act 1991 (as amended by the Water Industry Act 1999) prohibits the disconnection of a water supply for non-payment and the limiting of a supply with the intention of enforcing payment for certain premises including domestic dwellings

Non-recovery of debt is therefore a risk to the group and may cause the group's profitability to suffer However, allowance is made by the water regulator in the price limits at each price review for a proportion of debt deemed to be irrecoverable In addition, the group can also request a re-setting of its price limits through an IDoK during a review period when costs or savings arising from changes in certain regulatory assumptions (including as to the level of non-recoverable debt) are material, although there can be no guarantee that an IDoK application will be successful Although new and existing strategies continue to be implemented to reduce cash collection risks, including targeted summonsing, there can be no assurance that the group will not suffer losses from the group's inability to recover its debts fully

Rapid growth in the infrastructure management sector exposes the group to execution risk, conversely, slow growth could adversely affect profitability

The infrastructure management business, United Utilities Contract Solutions, is expanding into new markets The delivery of contracts, both existing and future, will be achieved by exploiting the group's core infrastructure management skills Overstretching these skills could lead to a loss of customers which, in turn, may cause profitability to suffer Slower than expected expansion could also impact profitability

Pension scheme obligations may require the group to make additional contributions to the schemes which would reduce profitability
The group participates in a number of pension schemes, principally in the UK The principal schemes are funded defined benefit schemes and the assets of the schemes are held in trust funds independent of group finances

The group increased contribution rates to the United Utilities Pension Scheme and the United Utilities Group of the Electricity Supply Pension Scheme in 2003/04 and the results of the full actuarial valuation resulted in further increases being required to the United Utilities Pension Scheme and the United Utilities Group of the Electricity Supply Pension Scheme from 1 April 2005

A one-off lump sum contribution of £319 5 million was made on 31 March 2005 This contribution was calculated to equal the capitalised value of the group's funding obligations to the schemes for the next five years (based on the actuarial valuation as at 31 March 2004) and represents advance payment of employer contributions which would have been made to the schemes during that period

The schemes had a combined surplus of £62 2 million as at 31 March 2007, compared with a surplus of £19 3 million at 31 March 2006

However, the group continues to monitor the funding of the schemes and cannot guarantee that during the next three years further contributions will not be required to eliminate shortfalls in the schemes This may adversely affect the financial position of the group

Should long-term investment returns be lower than the rate assumed by the actuaries in their pension scheme valuations, or interest rates reduce further leading to a deficit, the profitability of the group may be further adversely affected and the group may be required to increase its contributions to eliminate an under-funding Currently, anticipated future pensions contributions and a proportion of existing pension scheme deficits are recoverable through the price limits established by the regulators

Operating risk
Managing the group's businesses is dependent upon the ability to process a large number of transactions efficiently and accurately Operational risk and losses can result from fraud, employee errors, supply chain disruption, failure to document transactions properly or to obtain proper internal authorisation, failure to comply with regulatory requirements and business principles, resource shortages, failure or under-performance of business processes or equipment, natural disasters, the failure of internal or external systems, or the actions or inactions of third parties

Although the group has implemented risk controls and loss mitigation actions, and substantial resources are devoted to developing efficient procedures and to staff training, it is only possible to be reasonably, but not absolutely, certain that such procedures will be effective in controlling each of the operational risks faced by the group

Litigation
NOSS Consortium ('NOSS'), of which North West Water International Limited ('NWWIL'), a wholly owned subsidiary of the company, is a member and the sole remaining active participant, is party to arbitration proceedings in Thailand in relation to a design and construction contract dated 1 November 1993 between NOSS and the Bangkok Metropolitan Administration ('BMA') to build a wastewater treatment plant and network in central Bangkok

Following disagreements with the engineer and a dispute with the BMA, NOSS rescinded the contract and in November 1997 served a notice under Section 387 of the Thai Civil and Commercial Code on the BMA In March 1998, NOSS terminated the contract and served notice of arbitration NOSS has total claims against the BMA of approximately 6 billion Thai baht (approximately £83 million)

The BMA has counter-claimed for approximately 3 2 billion Thai baht (approximately £44 million) Arbitrators have been appointed by each party, but the arbitration process has stalled following the arbitrators' failure to agree on the appointment of a third arbitrator NOSS will continue to monitor the situation, but presently no hearings are scheduled

Save as stated above, neither the company nor any member of its group is, or has been, involved in any legal or arbitration proceedings nor, as far as the directors are aware, are any such proceedings pending or threatened by or against any member of the group which may have, or have had within the previous 12 months, a significant effect on the group's financial position

The group is engaged in litigation in the ordinary course of its operations, such as contract disputes, disputes over easements/wayleaves and other similar property matters, bill collections, personal injury claims and workers' compensation claims The company does not believe that such litigation, either individually or in aggregate, is material The company maintains insurance and, to the extent that the amounts in dispute may not be covered by such insurance, maintains provisions in those situations where management deems it appropriate in accordance with International Financial Reporting Standards (IFRS)

Governance

1 2 3 4 5 6 7 8 9 10 11 12

Board of directors

1 **Tim Weller**
Chief financial officer

2 **Charlie Cornish**
Managing director
Utility Solutions

3 **Nick Salmon**
Non-executive director

4 **Sir Peter Middleton**
Deputy chairman
non-executive director

5 **Sir Richard Evans**
Chairman

6 **Philip Green**
Chief executive officer

7 **David Jones CBE**
Non-executive director

8 **Andrew Pinder CBE**
Non-executive director

9 **Paul Heiden**
Non-executive director

10 **Norman Broadhurst**
Non-executive director

11 **Dr Catherine Bell**
Non-executive director

12 **Paul Capell**
Managing director,
Business Development

The business of the company is managed by the board of directors There are no family relationships between any of the directors or senior managers There are no arrangements or understandings with major shareholders, customers, suppliers or others pursuant to which any of the persons referred to below was selected as a director or member of senior management

Executive directors

Philip Green (age 54) – Chief executive officer

Philip Green was appointed as a director on 20 February 2006 In his most recent role before he joined the company, he led the container shipping company Royal P&O Nedlloyd through its successful listing in 2004 and subsequent agreed acquisition by AP Moller-Maersk A/S, delivering significant value for shareholders On 10 May 2007, he joined the board of Lloyds TSB Bank plc as a non-executive director He has also been a main board director and chief operating officer at the global information company Reuters Group PLC, and chief operating officer at DHL for Europe and Africa He is a member of the London Business School Advisory Board and a trustee of the Philharmonia Trust

Tim Weller (age 43) – Chief financial officer

Tim Weller joined the board as the chief financial officer on 1 August 2006 He was previously group finance director at RWE Thames Water plc and prior to that group finance director of Innogy Holdings plc from 2002 to 2004 He has been a partner at KPMG and director of financial control with the Granada group of companies and a non-executive director of Stanley Leisure Plc

Charlie Cornish (age 47) – Managing director, Utility Solutions

Charlie Cornish is responsible for the delivery of all utility contracts in the business, both to the group's regulated businesses and to external clients He joined the group in January 2004 and was formally appointed to the board on 27 January 2004 After graduating from Strathclyde University, he worked for British Aerospace, Plessey Telecommunications and Associated British Foods and also served as an executive director of NHS Trusts In 1998, he joined the West of Scotland Water Authority as human resources director and was involved with major change programmes He went on to become its customer services director and later chief executive He joined Thames Water in 2002 as global business performance director, working across Europe, Asia-Pacific and the Americas, eventually becoming chief operating officer with Thames Water UK and Ireland with responsibility for service delivery, including operations and capital programmes He is chairman of Young Enterprise North West and was appointed to the board of Water UK in March 2006 He is a director of The Mersey Partnership, an organisation promoting the Liverpool City region

Paul Capell (age 50) – Managing director, Business Development
Paul Capell joined United Utilities on 1 May 2007 He was previously a senior executive responsible for developing major industrial project capability at Veolia Water Solutions and Technologies and chairman of VWS Westgarth Prior to that he was divisional managing director of the global contracting business Weir Techna In 2005 he led the sale of the water and wastewater businesses of Weir Techna to Veolia Paul Capell is a Fellow of the Institute of Mechanical Engineers and a chartered engineer

Non-executive directors
Sir Richard Evans (age 64) – Chairman
Sir Richard Evans was appointed a non-executive director on 1 September 1997 and chairman in January 2001 In October 2006, he was appointed chairman of Samruk, the Kazakhstan state holding company He started his career in the Military Aircraft Division of British Aircraft Corporation (BAC), joining the board of British Aerospace plc as marketing director in January 1987 In 1990 he became its chief executive He was also a director of the Airbus company He was appointed chairman of British Aerospace plc (now BAE Systems plc) in May 1998, a post from which he retired in July 2004 after more than 30 years with the company and its predecessors He was also a non-executive director of NatWest plc from 1998 to 2000

Dr Catherine Bell (age 56) – Non-executive director
Dr Catherine Bell was appointed a non-executive director on 19 March 2007 She is a former civil servant and was Acting Permanent Secretary at the Department for Trade and Industry from March to October 2005 Prior to that, she was the director general of the Corporate Services Group and the Competition and Markets Group overseeing employment law, competition and consumer policy, company law and corporate governance, and was previously the head of Competition and Utility Regulation She is currently a non-executive director of the Civil Aviation Authority, Ensus Limited and Swiss Reinsurance GB plc

Norman Broadhurst (age 65) – Chairman of the audit committee
Norman Broadhurst was appointed a non-executive director on 1 April 1999 and is chairman of the audit committee He is currently chairman of Chloride Group plc, Freightliner Ltd and Cattles plc He is also a non-executive director of Old Mutual plc On 22 May 2006, he retired as a non-executive director from the board of Tomkins plc He was group finance director of Railtrack plc from 1994 to 2000 and a non-executive director of Taylor Woodrow Plc from March 2000 to November 2003

David Jones CBE (age 65) – Chairman of the remuneration committee
David Jones CBE was appointed as a non-executive director on 3 January 2005 He is currently chairman of UK Coal PLC and is also chairman of Teesside Power Ltd He was the group chief executive of The National Grid Company plc from 1994 to 2001, taking National Grid to the stock market and leading it successfully through an extensive business transformation programme Prior to that, he was chief executive of South Wales Electricity, having previously held senior engineering, commercial and management posts on the South Western and Midlands Electricity Boards

Paul Heiden (age 50) – Non-executive director
Paul Heiden was appointed as a non-executive director on 5 October 2005 He has been the chief executive of FKI plc since 2003 From 1992, he held various senior management positions at Rolls-Royce plc prior to joining the board in 1997 as director of Industrial Businesses and being appointed group finance director in 1999 After qualifying as a chartered accountant at Peat Marwick Mitchell & Co, he worked in senior finance roles at Hanson PLC and Mercury Communications He was a non-executive director of Bunzl plc from 1998 to 2005 and was a non-executive director of Filtrona plc from 2005 to 2006

Sir Peter Middleton (age 73) – Deputy chairman and senior independent non-executive director
Sir Peter Middleton joined the board as a non-executive director in January 1994 He is chairman of Camelot Group plc, the operator of the National Lottery, chairman of the Barclays Group Asia Pacific Advisory Committee, chairman of the Centre for Effective Dispute Resolution, UK chairman of Marsh & McLennan companies, chairman of Marsh Ltd, chairman of Creative Sheffield, chancellor of the University of Sheffield and on the board of the US listed Russian company Mobile TeleSystems (MTS) OJSC He is also a member of the advisory boards of Marsh McLennan companies, Three Delta, Financial Dynamics and Sistema and senior advisor to Fenchurch Advisory Partners After National Service, he joined HM Treasury where he had a long and distinguished career spanning 30 years, ultimately ascending to become Permanent Secretary from 1983 to 1991 Sir Peter joined Barclays in 1991 as group deputy chairman and as executive chairman of BZW, became chairman of Barclays Capital following the reorganisation of BZW in October 1997 and was group chief executive from November 1998 until October 1999 He became group chairman of Barclays Bank PLC in April 1999 and retired in August 2004 He is a past chairman of the British Bankers' Association, and a former board member of the National Institute of Economic and Social Research

Andrew Pinder CBE (age 60) – Non-executive director
Andrew Pinder was appointed a non-executive director on 1 September 2001 As the e-Envoy to the UK government from 2000 to 2004, he was responsible to the Prime Minister for the delivery of internet access to all British citizens and businesses He is currently a senior executive of Entrust, a US-based security specialist, on whose board he sat from 2004 to 2006, and the senior independent non-executive director of Spring Group plc

He is also a member of the Intel Global Advisory Board In January 2006, he became chairman of Becta (British Educational Communications and Technology Agency), an agency of the Department for Education and Skills, which looks after information technology in schools and further education Before his appointment as e-Envoy, he was a partner in a venture capital firm and carried out a number of management consultancy assignments for the British government Previous executive leadership roles also include positions as the head of European operations and technology at Citibank, director of operations and technology at Prudential Corporation and as director of information technology at the Office of Inland Revenue

Nick Salmon (age 54) – Non-executive director
Nick Salmon was appointed as a non-executive director on 4 April 2005 He has been the chief executive of Cookson Group plc since 2004 From 2001 to 2004, he was executive vice president of Alstom S A , the global energy and transport infrastructure group From 1997 to 2001 he was executive vice president of ABB Alstom Power and was chief executive of Babcock International Group PLC from 1993 to 1997 Prior to joining Babcock, he held senior management positions at GEC and GEC Alsthom in the UK and France, and previously spent 11 years with China Light & Power Company Limited in Hong Kong

Nick Salmon will become the senior independent non-executive director when Sir Peter Middleton retires at the annual general meeting in July 2007

The executive leadership team
Philip Green, Chief executive officer
Martin Bradbury, Chief information officer
Paul Capell, Managing director, Business Development
Alison Clarke, Human resources director
Charlie Cornish, Managing director, Utility Solutions
Clive Elphick, Managing director, Asset Management and Regulation
Gaynor Kenyon, Communications director
Tim Weller, Chief financial officer

The chief executive is responsible for executive management of the group and is assisted by the Executive Leadership Team (ELT) The ELT meets on a formal basis at least 12 times per year The ELT consists of the executive directors, details of whom are given above, together with the following senior officers

Martin Bradbury (age 51) – Chief information officer
Martin Bradbury was appointed to the new role of chief information officer on 11 May 2007 and will focus on developing the structure of the function and transformation to the new organisation structure He was formerly chief operating officer for Scottish Water Solutions, a public-private partnership to upgrade Scotland's water infrastructure He is a former trustee of WaterAid and a past chairman of Business in the Arts North West He took over as managing director of Contract Solutions following the death of Gordon Waters in December 2006, up to 30 April 2007

Alison Clarke (age 40) – Human resources director
Alison Clarke joined the group on 21 May 2007 She was previously group international human resources director for global retailer AS Watson in Hong Kong She has been human resources director at Hilton UK and at Whitbread Restaurants and has also worked for Ford Motor Company and Thames Water

Clive Elphick (age 50) – Managing director, Asset Management and Regulation
Clive Elphick was appointed as managing director of Asset Management and Regulation on 8 March 2007 He is responsible for developing and delivering the group's asset management and price review strategy and for leading the group's regulatory relationships He is also a non-executive director of the Department for Culture, Media and Sport and of the Northern Ireland Authority for Utility Regulation and is vice chair of the CBI in the north west of England Clive Elphick has been an associate at Deloitte & Touche and has also worked at ICI and his experience includes a part-time secondment to the Cabinet Office

Gaynor Kenyon (age 46) – Communications director
Gaynor Kenyon was appointed communications director on 22 May 2006 Gaynor joined the company from Scottish Power and has 18 years' experience in the energy industry, having previously been at Manweb until 1995 Initially leading Scottish Power's communications in the Manweb region, for the last three years she was the company's UK Government and Community Affairs Director In this role, Gaynor was responsible for Scottish Power's political strategy in the Scottish Parliament, Welsh Assembly and Westminster and for the group's US and UK corporate responsibility strategy

Directors' report

Principal activities
The company is the holding company of a group which owns and operates electricity distribution, water and wastewater assets and also manages infrastructure and business processes for its own and other businesses

A fuller description of business activities is contained within the business review on pages 2 to 38 The principal subsidiary undertakings, associate and joint ventures of the company are shown in note 13 to the consolidated financial statements

Business review
The chairman's and chief executive's statements on pages 4 to 6 and the business review on pages 7 to 38 report on the group's activities during the year and on likely future developments A summary of key performance indicators can be found on page 2 The directors, in preparing the business review, have not sought to comply with the ASB's 2006 Reporting Statement on operating and financial reviews All the information supplied in the chairman's and chief executive's statements on pages 4 to 6 and the business review on pages 7 to 38 form part of the directors' report as incorporated by reference Any liability for the information is restricted to the extent prescribed by the Companies Act 2006

The dividend for shareholders
The directors are recommending a final dividend of 30 30 pence for each ordinary share for the year ended 31 March 2007, resulting in a total for the year of 44 93 pence for each ordinary share Subject to shareholders approving this recommendation at the annual general meeting, the dividend will be paid on 24 August 2007 to shareholders on the register at the close of business on 29 June 2007 United Utilities Employee Share Trust Limited has waived its rights to dividends in respect of its holding of 53,601 ordinary shares

The business for the annual general meeting
Details of the resolutions to be proposed at the 2007 annual general meeting are set out in the notice calling the meeting There is also a full explanation of the resolutions in the leaflet containing the notice, enclosed with this report In addition to the matters normally dealt with at the annual general meeting, resolutions will be put to shareholders to

- increase the authorised share capital of the company,
- amend the articles of association of the company, and
- adopt the rules of the United Utilities PLC 2007 Matching Share Award Plan

Full details of these resolutions can be found in the notice of meeting and the explanatory notes thereto

Employees
The company's policies on employee involvement and on persons with disabilities are contained within the business review on pages 20 and 21 The board encourages employees to own shares in the company Details of employee share schemes are in the remuneration report on page 68

Financial instruments
The risk management objectives and policies of the company can be found in note 18 to the financial statements on page 98 and on pages 32 and 33

Directors and senior management
The names of the present directors and their biographical details are given on pages 40 to 42 The following also served during the year Tom Drury, managing director of Vertex, who resigned his directorship on 27 March 2007 following the sale of Vertex to a consortium headed by Oak Hill Capital Partners, Jane Newell, non-executive director and Simon Batey, group finance director, who both stood down at the annual general meeting on 28 July 2006, and Gordon Waters, managing director of United Utilities Contract Solutions, who died on 24 December 2006

Dr Catherine Bell was appointed as an additional non-executive director on 19 March 2007 and Paul Capell was appointed as managing director of Business Development on 1 May 2007

Reappointment of directors
Under the articles of association, a director appointed by the board to fill a casual vacancy must retire at the annual general meeting of the company next following such appointment Tim Weller was appointed by the board on 1 August 2006, Dr Catherine Bell was appointed on 19 March 2007 and Paul Capell on 1 May 2007 Each of these directors is retiring and offering himself or herself for reappointment at the 2007 annual general meeting

In addition, the articles of association provide that if, at the start of business on the date of the notice convening that annual general meeting, a director has served for a continuous period of nine years he must retire and may offer himself for reappointment Sir Richard Evans and Sir Peter Middleton will both have completed over nine years' service at the date of notice Sir Richard Evans is therefore retiring and is offering himself for reappointment at the 2007 annual general meeting Sir Peter Middleton is standing down and will not seek reappointment at the annual general meeting

The articles of association also state that a director must retire at the third annual general meeting following his or her last appointment Charlie Cornish was last appointed at the annual general meeting held in 2004 and is therefore retiring and is offering himself for reappointment at the 2007 annual general meeting

Under the articles of association, one third of the directors (excluding those seeking reappointment on other grounds) must retire by rotation at each annual general meeting Andrew Pinder, the director determined by lot as required under the articles, was appointed at the annual general meeting in 2005 and retires and offers himself for reappointment

Executive leadership team
The names of the present members of the executive leadership team (ELT) and their biographical details are given on page 42 The members of the ELT together with the directors are regarded as 'persons discharging managerial responsibility' under the UK Listing Authority's Disclosure Rules

The following also served as executive leadership team members during the year

Ian Priestner, communications director, who left the company on 30 April 2006, Simon Batey, group finance director, who resigned on 28 July 2006, Gordon Waters, managing director of Contract Solutions, who died on 24 December 2006, Tom Drury, managing director of Vertex, who resigned his directorship on 27 March 2007, Tim Rayner, general counsel, who left the company on 31 March 2007, and Linda Booth, human resources director, who will be leaving the company on 31July 2007

Paul Capell was appointed as managing director of Business Development on 1 May 2007 Martin Bradbury took up the role of chief information officer with effect from 11 May 2007, and Alison Clarke was appointed as human resources director on 21 May 2007

Directors' and officers' insurance
The company maintains an appropriate level of directors' and officers' insurance whereby directors are indemnified against liabilities to third parties to the extent permitted by the Companies Act 1985 (as amended)

Directors' interests in shares
The directors and their immediate families had the following beneficial interests as at 31 March 2007 and as at 4 June 2007 in the company's ordinary shares and options to subscribe for shares None of the directors or ELT members hold more than one per cent of the ordinary share capital of the company Except as described below, none of the directors had any interest in any share capital of any other group company or in any debenture of any group company

Interests in ordinary shares
The individual interests of the directors in ordinary shares are shown in table 9

Table 9

	At 1 April 2006 or date of appointment if later	At 31 March 2007	At 4 June 2007
Sir Richard Evans	381	**381**	381
Philip Green	100,000	**100,527**	100,565
Dr Catherine Bell*	–	–	–
Norman Broadhurst	530	**530**	530
Paul Capell*	n/a	**n/a**	–
Charlie Cornish	321	**10,383**	10,421
Paul Heiden	1,852	**1,852**	1,852
David Jones	–	–	–
Sir Peter Middleton	7,115	**7,115**	7,115
Andrew Pinder	6,222	**6,222**	6,222
Nick Salmon	–	**1,300**	1,300
Tim Weller*	39,000	**39,020**	39,256

Notes
- Each executive director is a member of the class of discretionary beneficiaries of the United Utilities Employee Share Trust and is therefore treated as having an interest in the 53 601 ordinary shares held by United Utilities Employee Share Trust Limited as trustee of the United Utilities Employee Share Trust at 31 March 2007 As at 4 June 2007 United Utilities Employee Share Trust Limited continued to hold 53,601 ordinary shares
- Tim Weller was appointed as a director on 1 August 2006
- Dr Catherine Bell was appointed as a non-executive director on 19 March 2007
- Paul Capell was appointed as a director on 1 May 2007

Interests in share options
The individual interests of the directors in share options are shown in table 10 Full detail of these arrangements can be found in the remuneration report on pages 63 to 66

Table 10

	At 1 April 2006 or date of appointment if later	At 31 March 2007	At 4 June 2007
Philip Green*	–	**106,371**	106 371
Charlie Cornish*	–	**50,022**	50 022
Tim Weller*	–	**41,484**	41 484

Notes.
- Non executive directors do not participate in the company's share option plans
- Philip Green – options granted on 16 January 2007 under the terms of a long term incentive scheme in which Mr Green is the sole participant The original number of options awarded (100 000) is increased on each dividend payment date after 1 April 2006 accordingly a further 4 398 and 1 973 ordinary shares have been added to the award in respect of dividends already paid on 25 August 2006 and 12 February 2007 Provided Mr Green maintains his holding of 100 000 ordinary shares and remains in employment with the company throughout the next five years these options together with additional shares from notional reinvestment of dividends will be capable of exercise by Mr Green at nil cost at the end of the five-year period after the conclusion of the next regulatory reviews
- Charlie Cornish – options granted on 16 March 2007 under the terms of a long-term incentive scheme under which Mr Cornish is the sole participant The original number of options awarded (47 027) is increased on each dividend payment date after 1 April 2006 accordingly a further 2 068 and 927 ordinary shares have been added to the award in respect of dividends already paid on 25 August 2006 and 12 February 2007 The options will be capable of exercise by Mr Cornish at nil cost subject to the satisfaction of certain performance targets by 31 December 2010 at the latest
- Tim Weller – options granted on 14 February 2007 under the terms of a long-term incentive scheme in which Mr Weller is the sole participant The original number of options awarded (39 000) is increased on each dividend payment date following Mr Weller's joining date of 1 July 2006 Accordingly a further 1 715 and 769 ordinary shares have been added to the award in respect of dividends already paid on 25 August 2006 and 12 February 2007 Provided Mr Weller maintains his holding of 39 000 ordinary shares and remains in employment with the company throughout the next five years these options together
with additional shares from notional reinvestment of dividends, will be capable of exercise by Mr Weller at nil cost at the end of the five-year period after the conclusion of the next regulatory reviews

Contingent interests in the performance share plan
Details of directors' contingent interests in the performance share plan can be found in the remuneration report in table 24 on pages 59 and 60

Indemnities
Throughout the year and as at the date of this report, the articles of association contained provisions for the benefit of directors, officers and employees of the group and its subsidiary and associated companies indemnifying them out of the assets of the company to the full extent allowed by law against liabilities incurred by them in the course of carrying out their duties

Following recent changes in company law, the board will propose at the forthcoming annual general meeting that shareholders approve an amendment to the articles to make clear provision for the directors to participate in the approval of such indemnity arrangements, notwithstanding the fact that they may benefit from those arrangements Any such indemnities would be implemented in compliance with the applicable limitations provided by company law The changes to the articles do not permit the provision of an indemnity in favour of auditors, which reflects market practice

Business review
Governance
Financial statements
Information for shareholders

Purchase of own shares
At the annual general meeting held on 28 July 2006, the company was authorised by shareholders to purchase, in the market, up to 87,557,542 of its own ordinary shares of £1 each No shares were purchased pursuant to this authority during the year This authority is normally renewable annually and approval will be sought from shareholders at the 2007 annual general meeting to renew the authority for one year

Political and charitable donations
Charitable donations by the group in the year amounted to £3,080,070 (2005/06 £1,324,308) The group's policy is not to make any donations for political purposes However, the Political Parties, Elections and Referendums Act 2000 requires certain types of expenditure on political events to be pre-approved by shareholders At the 2005 annual general meeting, an authority was taken to cover such expenditure Pursuant to that authority, in the year, the company incurred costs of £nil (2005/06 £22,499) as part of the process of talking to government at all levels Resolutions to renew this authority for the company and its principal subsidiaries will be put to the 2008 annual general meeting

Substantial shareholders and related party transactions
The company is not directly or indirectly owned or controlled by another corporation or by an individual or government and there are no arrangements the operation of which may, at a subsequent date, result in a change in control of the company

At 4 June 2007, the directors were aware of the following notifiable beneficial interests of greater than three per cent in the company's issued ordinary share capital

Table 11

Company	Date notified	No of shares	%
Pictet ASSET Management S A	20/03/2007	57,889,156	6 597

Holders of all ordinary shares, including those held through American Depository Shares, have the same voting rights

Other than with respect to employment agreements and compensation arrangements, there is no material indebtedness owed to, or by, and there have been no material transactions between, the company and management during the company's two most recent financial years, nor are there presently proposed to be any such indebtedness or any material transactions, or any transactions that are unusual in their nature or conditions to which the company or any of its subsidiaries was or is a party and in which any director or executive officer, or five per cent shareholder, or any relative or spouse thereof or any associate of the company or any enterprise that directly or indirectly controls, is controlled by or is under common control with the company, had or is to have a direct or indirect material interest

For details of related party transactions see note 27 to the consolidated financial statements on page 116

Approach to technology development
The company is committed to using innovative, cost-effective and practical solutions for providing high quality services It recognises the importance of ensuring that it properly focuses its investment in the development of technology, that it has the right skills to apply technology to achieve sustainable competitive advantage and that it continues to be alert to emerging technological opportunities

Fulfilling social and environmental responsibilities
As described in the corporate responsibility review on pages 34 and 35, the company seeks to manage its total impact on society as a responsible corporate citizen Full details are set out in the company's separate stakeholder report, which is an important part of the company's integrated approach to reporting on overall performance, together with the annual report and the website

Creditor payment policy and practice
Neither the company nor the group follow any specific external code or standard on payment practice Their policy is normally to pay suppliers according to terms of business agreed with them on entering into binding contracts and to keep to the payment terms providing the relevant goods or services have been supplied in accordance with the contracts The group and the company had 23 days (2005/06 45 days) and 99 days (2005/06 100 days) respectively of purchases outstanding at the end of the financial year

Events after the balance sheet date
Details of events after the balance sheet date are included in note 30 to the consolidated financial statements on page 118

Information given to auditors
Each of the persons who is a director at the date of approval of this report confirms that

(1) so far as the director is aware, there is no relevant audit information of which the company's auditors are unaware, and

(2) the director has taken all the steps that he/she ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the company's auditors are aware of that information

This confirmation is given and should be interpreted in accordance with the provisions of s234ZA of the Companies Act 1985

Independent auditors
The board is proposing to reappoint Deloitte & Touche LLP as auditors at the forthcoming annual general meeting

Approved by the board on 4 June 2007 and signed on its behalf by

Paul Davies
Secretary

Corporate governance report

The Combined Code

United Utilities PLC is subject to the Combined Code on Corporate Governance 2003 (the 'Combined Code') Throughout the year, the board has complied fully with the revised provisions of Section 1 of the Combined Code This report, together with the remuneration report on pages 52 to 68, gives details of how the principles of the Combined Code have been applied

The board of directors

The board is scheduled to meet ten times each year with additional meetings called if required Additionally, the board met during the year specifically to consider and develop the company's strategy and long-term plan The board has a formal schedule of matters reserved to it, which ensures that it takes all major strategy, policy and investment decisions affecting the group In addition, it is responsible for business planning and risk management and for the development of group policies in such areas as health and safety, directors' and senior managers' remuneration and on social, environmental and ethical issues Attendance by individual directors at scheduled meetings of the board and its committees during the year ended 31 March 2007 is shown in table 12 and full biographical details of the directors can be found on pages 40 to 42

The group's governance structure ensures that all decisions are made by the most appropriate people in such a way that the decision making process itself does not unnecessarily delay progress The board has formally delegated specific responsibilities to board committees, including the audit (see page 49), remuneration (see page 53), nomination (see 'Appointments to the board' below), approvals and treasury committees All board committees are provided with sufficient resources to undertake their duties

The approvals committee considers and approves expenditure and investment proposals within limits delegated by the board Its members are the executive directors and the company secretary The treasury committee considers and approves borrowing, leasing, bonding and other banking facilities within limits set by the board Its members are the chairman and the executive directors together with, for more significant or complex transactions, one other non-executive director

The directors of subsidiary companies are legally responsible for those business entities They are tasked with the delivery of the targets set within the budgets approved by the group board and for the implementation of group strategy and policy across their businesses United Utilities Water PLC, for example, is a substantial business in its own right and its board includes two independent non-executive directors (Phillida Entwistle and Deborah Morton)

The chairman holds meetings with the non-executive directors without the executive directors present Led by the senior independent director, the non-executive directors meet without the chairman present at least annually to appraise the chairman's performance Directors have a right to ensure that any concerns they have which cannot be resolved, about the running of the company or a proposed action, are recorded in the board minutes In addition, upon resignation a non-executive director is asked to provide a written statement addressed to the chairman, for circulation to the board, if they have any such concerns

The company maintains an appropriate level of directors' and officers' insurance

Chairman and chief executive

Separate individuals have been appointed to the positions of chairman and chief executive The board has agreed clearly defined responsibilities for the roles and has adopted a set of guiding principles to govern the relationship between them The chairman is primarily responsible for the working of the board and for ensuring that the non-executive directors are fully engaged in their role and that they provide an effective contribution to the board and the management of the company The chairman and non-executive directors meet informally before scheduled board meetings The chief executive is responsible for running the group's business and for implementing board strategy and policy

Board balance and independence

The board aims to maintain a balance of executive and non-executive directors and, at the date of adoption of this statement, comprises the non-executive chairman, four executive directors and seven non-executive directors determined by the board to be independent in accordance with the Combined Code The Combined Code does not regard the chairman as being independent in view of his unique role in corporate governance, although Sir Richard Evans was independent upon first appointment

Taking into account the provisions of the Combined Code, the board has determined that all of the non-executive directors are independent and free from any business or other relationship which could compromise their independent judgement In particular, the board has determined that Sir Peter Middleton remains independent, notwithstanding that he has served on the board for more than nine years In making this determination, the board took into account Sir Peter's breadth of experience, his financial independence and his other business interests It also confirmed its view that Norman Broadhurst is independent notwithstanding a close family tie with one of the company's advisers, his daughter being a tax partner in Deloitte & Touche's Birmingham office, because Deloitte & Touche have confirmed in writing to the company that she had not, and would not, be involved with the United Utilities account in any way

Senior independent director

Sir Peter Middleton has been appointed as senior independent director The senior independent director is available to shareholders if they have concerns which contact through the normal channels has failed to resolve or for which such contact is inappropriate The terms of reference for the senior independent director are available on the company's website and include the authority to call a meeting of the non-executive directors if, in his opinion, it is necessary, to lead a meeting of the non-executive directors without the chairman present at least annually to appraise the chairman's performance, and to attend sufficient meetings with a range of major shareholders to listen to their views in order to help develop a balanced understanding of their issues and concerns

Appointments to the board

The board has constituted a nomination committee which meets at least once each year and otherwise as required The committee considers and makes recommendations to the board on the composition, balance and membership of the board

Table 12 Attendance by individual directors at scheduled meetings of the board in the year ended 31 March 2007

	Board		Audit		Nomination		Remuneration	
	Possible	Actual	Possible	Actual	Possible	Actual	Possible	Actual
Philip Green	10	10	n/a	n/a	2	2	n/a	n/a
Simon Batey	4	4	n/a	n/a	n/a	n/a	n/a	n/a
Charlie Cornish	10	10	n/a	n/a	n/a	n/a	n/a	n/a
Tom Drury	10	10	n/a	n/a	n/a	n/a	n/a	n/a
Gordon Waters	7	7	n/a	n/a	n/a	n/a	n/a	n/a
Tim Weller	6	6	n/a	n/a	n/a	n/a	n/a	n/a
Sir Richard Evans	10	10	n/a	n/a	2	2	n/a	n/a
Dr Catherine Bell	1	1	0	0	n/a	n/a	n/a	n/a
Norman Broadhurst	10	10	5	5	2	2	4	4
Paul Heiden	10	8	5	5	1	0	4	4
David Jones	10	10	5	5	2	2	6	6
Sir Peter Middleton	10	7	5	3	2	1	4	3
Jane Newell	4	4	2	1	1	1	3	3
Andrew Pinder	10	9	1	0	2	1	6	5
Nick Salmon	10	10	3	2	2	2	6	6

Notes

- Simon Batey and Jane Newell retired on 28 July 2006
- Tim Weller was appointed as a director on 1 August 2006
- Gordon Waters died on 24 December 2006
- Tom Drury resigned his directorship on 27 March 2007 following the disposal of Vertex
- Dr Catherine Bell was appointed as a non-executive director on 19 March 2007

Its members are the non-executive directors, including the chairman (who is also chairman of the committee, although the chairman will not chair the committee when the committee deals with the appointment of a successor to the chairmanship) together with the chief executive As such, the majority of the members of the committee are non-executive directors determined by the board to be independent in accordance with the Combined Code The nomination committee's terms of reference are available to shareholders on request and are also available on the company's website The nomination committee evaluates the balance of skills, knowledge and experience on the board and, in the light of this evaluation, prepares a description of the roles and capabilities required for a particular appointment

The nomination committee leads the process for board appointments and makes recommendations to the board about filling vacancies on the board, appointing additional persons to the board and the re-election by shareholders of any director under the retirement by rotation provisions in the company's articles of association The committee considers and makes recommendations to the board from time to time on the board's composition and balance During the year, the committee prepared a description of the roles and capabilities required for the appointment of an executive and a non-executive director, engaged the services of Whitehead Mann and made recommendations to the board as part of the final selection process which led to the appointments of Tim Weller as chief financial officer and Dr Catherine Bell as a non-executive director

The letters of appointment of non-executive directors are made available for inspection and are available on the company's website They set out the expected time commitment and non-executive directors undertake that they will have sufficient time to meet what is expected of them Non-executive directors' other significant commitments are disclosed to the board before appointment, with the board being notified of any subsequent changes

The board's policy is that no full-time executive director should take on more than one non-executive directorship of a FTSE 100 company or the chairmanship of such a company

Information and professional development

The chairman is responsible for ensuring directors receive comprehensive information on a regular basis to enable them to perform their duties properly

Board papers are normally distributed five or so days in advance of scheduled board meetings to enable directors to obtain a thorough understanding of the matters to be discussed, and seek clarification if required

The board has established a governance framework which encourages all directors to bring an independent judgement to bear on issues of strategy, performance and resources, including key appointments and standards of conduct

New directors receive appropriate induction on joining the board, typically including meeting with members of the senior management team and visits to operational sites Major shareholders are invited to meet with new non-executive directors As part of this, major shareholders will have the opportunity to meet Dr Catherine Bell, as a new non-executive director, at the annual general meeting in July

All directors have access to the advice and services of the company secretary, who is responsible to the board for ensuring that board procedures are complied with The appointment and removal of the company secretary are matters for the board as a whole

The board has adopted a protocol under which directors have access, through the company secretary, to independent professional advice at the company's expense where they judge it necessary to discharge their responsibilities as directors. All board committees are provided with sufficient resources to undertake their duties.

Performance evaluation

During the year, the board conducted an evaluation of its own performance and that of its committees and individual directors. The process involved the completion by each director of a confidential questionnaire in a form consistent with last year's and which was modelled on the Chairmen's Guide to the Board Performance Review published by the Chairmen's Forum and is consistent with guidance published by the Institute of Chartered Secretaries and Administrators. Each director was required to score the board's performance on 64 issues, such as contribution to strategy, risk management, financial and operational reporting, board committees, matters reserved for the board, communication, company and board advisers, relations with the group's regulators and board procedures.

In addition, the members of the audit, nomination and remuneration committees completed additional confidential questionnaires about the functioning of those committees, as did those managers and advisers who deal with those committees frequently. For example, in the case of the audit committee, the auditors and the group audit manager each completed confidential questionnaires about the audit committee.

The company secretary analysed the completed questionnaires and summarised the findings in a report for the chairman, which highlighted and prioritised the key areas of feedback and provided a comparison with the previous year's evaluation. The chairman subsequently conducted one-to-one discussions with each of the board members based on the summary report, after which the chairman reported back to the whole board on the evaluation process. The board has developed a plan to improve succession planning, the management of external financial advisers and the quality and frequency of board reports on regulatory and political issues.

The responses to the questionnaires demonstrated a high degree of consistency and the evaluation process affirmed the board's confidence in the group's system of corporate governance.

The chief executive conducts annual appraisals with executive directors and has regular one-to-one discussions about their performance with them, as does the chairman with the chief executive.

Reappointment of directors

The board initially appoints all new directors, upon the recommendation of the nomination committee and following an appropriate recruitment process. Following the appointment of a new director, he or she is required to retire and seek appointment at the next annual general meeting. The company's articles of association include provisions requiring one third of all directors to retire and seek reappointment at each annual general meeting, and ensuring that no director serves for more than three years without retiring and being proposed for reappointment at an annual general meeting. Biographical details of directors being submitted for appointment or reappointment are set out in the notes accompanying the relevant notice of meeting.

Non-executive directors are appointed for specified terms subject to reappointment under the company's articles of association and to Companies Acts' provisions relating to the removal of a director. The board explains to shareholders, in the papers accompanying a resolution to elect a non-executive director, why they believe that that non-executive director should be elected. The chairman will confirm to shareholders when proposing reappointment that, following formal performance evaluation, the individual's performance continues to be effective and that they demonstrate commitment to the role. Any term beyond six years for a non-executive director will be subject to particularly rigorous review, and will take into account the need for progressive refreshing of the board. Any non-executive director serving longer than nine years will be subject to annual reappointment.

Financial reporting

In presenting the annual and interim financial statements and similar significant publications, the directors aim to present a balanced and understandable assessment of the group's position and prospects. The company produces a UK compliant annual report in June each year. Shareholders who elect to receive a summary financial statement will also receive a stakeholder report which summarises the most important features of the group's activity during the year.

The directors have adopted the going concern basis in preparing these financial statements. This is based upon a review of the group's budget for 2007/08, the five-year business plan and investment programme, together with the cash and committed borrowing facilities available to the group. The board also took into account potential contingent liabilities and other risk factors as interpreted by the 'Guidance on Going Concern and Financial Reporting for Directors of Listed Companies registered in the United Kingdom', published in November 1994.

Statement of directors' responsibilities

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

Company law requires the directors to prepare financial statements for each financial year. The directors are required by the IAS Regulation to prepare the group financial statements under International Financial Reporting Standards (IFRSs) as adopted by the European Union and have also elected to prepare the parent company financial statements in accordance with IFRSs as adopted by the European Union. The financial statements are also required by law to be properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation.

International Accounting Standard 1 requires that financial statements present fairly for each financial year the company's financial position, financial performance and cashflows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards

Board's 'Framework for the preparation and presentation of financial statements' In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable IFRSs However, directors are also required to

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

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 1985 They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions

Internal control

The board is responsible for the group's system of internal controls and for reviewing its effectiveness Throughout the year under review and up to the date of this report, the board has operated procedures meeting the requirements of the Combined Code relating to internal control as set out in the September 1999 guidance 'Internal Control Guidance for Directors on the Combined Code' published by the Institute of Chartered Accountants in England and Wales Each year the board reviews all controls, including financial, operational and compliance controls and risk management procedures The internal control system is designed to manage, rather than to eliminate, the risk of failure to achieve the company's business objectives and can only provide reasonable, and not absolute, assurance against material misstatement or loss

The key features of the internal control system are

- a control environment with clearly defined organisation structures operating within a framework of policies and procedures covering every aspect of the business,
- comprehensive business planning, risk assessment and financial reporting procedures, including the annual preparation of detailed operational budgets for the year ahead and projections for subsequent years,
- a monthly board review of financial and non-financial performance to assess progress towards objectives,
- monthly meetings prior to each board meeting of the executive leadership team, a forum in which the executive directors, the managing directors of the group's businesses, the group functional directors and the company secretary exchange information and discuss strategic and operational issues which are of group-wide importance,
- regular monitoring of risks and control systems throughout the year by the operating businesses, supported by the use of risks and issues databases,
- a self-certification process whereby the operating businesses are required to confirm that the system of internal control is operating effectively,
- an internal audit function to provide independent scrutiny of internal control systems and risk management procedures,
- a quarterly review of group-wide risks by the executive leadership team, a forum in which the executive directors, the group functional directors and the company secretary scrutinise key risks, mitigating actions and controls,
- an annual risk assessment exercise involving self-assessment by management of all business risks in terms of impact, likelihood and control strength and an objective challenge of that assessment by the internal audit team,
- health and safety performance reviews carried out by our in-house safety professionals in addition to the normal health and safety risk assessment and management processes carried out within each of the operating businesses,
- centralised treasury operations operating within defined limits and subject to regular reporting requirements and internal audit reviews, and
- established procedures, set out in a group internal control manual, for planning, approving and monitoring major capital expenditure, major projects and the development of new business which includes short and long-term budgets, risk evaluation, detailed appraisal and review procedures, defined authority levels and post-investment performance reviews

The audit committee and the auditors

The audit committee's members are Norman Broadhurst (chairman), Dr Catherine Bell, Paul Heiden, David Jones and Sir Peter Middleton They are all non-executive directors who are determined in accordance with UK corporate governance rules to be independent The board is satisfied that Norman Broadhurst has recent and relevant financial experience The committee met five times in the year to 31 March 2007 The terms of reference of the audit committee are available to shareholders on request and are also available on the company's website

The committee has primary responsibility for making a recommendation to the board, for consideration by shareholders in general meeting, of resolutions on the appointment, reappointment and removal of the external auditor The committee also keeps under review the scope, results and effectiveness of the audit, and the independence and objectivity of the auditor The committee has established policies and procedures to pre-approve the engagement of the auditor to provide any audit or non-audit services and keeps the nature and extent of non-audit services under review

The board has decided that if it does not accept the audit committee's recommendation in respect of the position of the external auditor, it should include in the annual report, and in any papers recommending appointment or reappointment, a statement from the audit committee explaining the recommendation and should set out reasons why the board has taken a different position

The audit committee reviews the half-year and annual financial statements and any formal announcements relating to financial performance before submission to the board, reviews periodically the scope, remit and effectiveness of the internal audit function and the effectiveness of the group's internal control system

The audit committee reviews, at least annually, arrangements by which staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters The board has a disclosure policy which provides a confidential mailbox for employees who want to report any concerns which they may have The committee's objective is to ensure that arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow-up action

Fees

Audit and audit-related services are pre-approved annually by the audit committee Audit-related services generally are highly correlated with the role of independent auditors Such services include assurance on non-statutory information, assurance work carried out in connection with reporting to a statutory regulator, analysis and interpretation of accounting principles and their application, support for debt issues and similar transactions, and other services that have a bearing on the group's financial statements on which the external auditors provide their opinion

Non-audit services are allowed under the procurement of audit and non-audit services' policy and do not affect the independence of the external auditors, but do require the pre-approval of the audit committee prior to the engagement Specific approval may be delegated to a designated member of the audit committee, with such approvals to be reported at the next audit committee meeting In granting such approval, the designated member of the audit committee is required to consider the cumulative proportion of fees paid for such work compared with the statutory audit fees In the financial year 2006/07, all services were pre-approved by the audit committee

The group also maintains a list of prohibited services that cannot be provided by the group's auditors as they are considered by statute or in the group's opinion to be incompatible with the role of the independent auditor

The fees paid or payable to the auditors in the year under review are set out in table 13

Table 13 Fees to Deloitte & Touche LLP

Year ended 31 March	**2007 £'000**	2006 £ 000
Audit services		
Statutory audit	**1,179**	912
Audit related regulatory reporting[1]	**2,463**	687
Further assurance services		
Compliance services[2]	**850**	850
Advisory services[3]	**100**	15
Total	**4,592**	2,464

Notes

(1) Audit related regulatory reporting fees are fees billed for work on regulatory returns and assurance work reasonably related to the statutory audit including due diligence and assurance work work associated with raising debt and equity finance and securities filing work

(2) Compliance services fees mainly relate to transaction support

(3) Advisory services fees are fees incurred for tax compliance tax advice and related tax work

In addition to the above fees relating to joint ventures of the group were paid to Deloitte & Touche LLP in 2007 totalling £41 900 (2005/06 £52 400)

Dialogue with institutional shareholders

There is a programme of investor meetings and presentations which take place throughout the year, both in the UK and overseas During the year, the board met or offered to meet with 87 different funds, representing 38 per cent of the company's issued share capital This, together with regular announcements of significant events affecting the group and frequent updates on current trading, emphasises the board's commitment to keeping the company's equity and debt investors informed of developments affecting the group The board regards this programme as important continually to improve investors' awareness of the business and for the board to maintain an understanding of investors' priorities

All members of the board, and in particular the non-executive directors, are informed of the views of major shareholders about their company through an annual survey of shareholder opinion produced for the company by Makinson Cowell Non-executive directors have the opportunity to attend meetings with major shareholders and would attend them if requested by major shareholders

Constructive use of the annual general meeting

The board encourages shareholders to exercise their right to vote at the annual general meeting The notice calling the meeting and related papers are sent to shareholders at least 20 working days before the meeting

At annual general meetings, voting on all resolutions takes place by means of a poll which ensures that all shareholders' votes are taken into account, whether lodged in person at the meeting, or by proxy The poll vote is scrutinised by Lloyds TSB Registrars and the results are released to the Stock Exchange and posted on the company's website the next business day Separate resolutions are proposed on each substantially separate issue and the company always proposes a resolution at the annual general meeting relating to the report and accounts For each resolution, proxy appointment forms provide shareholders with the option to direct their proxy to vote either for or against the resolution or to withhold their vote The proxy form and any announcement of the results of a vote will make it clear that a 'vote withheld' is not a vote in law and will not be counted in the calculation of the proportion of votes for and against the resolution Presentations are made on the progress and performance of the business prior to the formal business of the meeting

Shareholders are encouraged to participate through a question and answer session and individual directors or, where appropriate, the chairman of the relevant committee, respond to those questions directly Normally, the chairmen of the audit, nomination and remuneration committees will be available at the annual general meeting to answer questions relevant to the work of those committees All directors normally attend the annual general meeting

The interim report, the annual report, the stakeholder report and summary financial statement remain the primary means the board has of communicating during the year with all of the company's shareholders However, the board recognises the importance of the internet as a means of communicating widely, quickly and cost-effectively A lot of information about the company is available on its website Financial news releases are made available on the site at the same time as being released through other news channels and anyone with an email address can register free of charge to receive an email alert upon the posting of each new release

Approach to reward

The group aims to ensure that its remuneration arrangements attract and keep people of the right calibre in order to achieve corporate success and to enhance shareholder value Its overall approach is to attract, develop, motivate and keep talented people at all levels, pay competitive salaries and benefits to its staff and encourage its staff to hold shares in the company When pay levels are set, account is taken of the work that an employee does and what is paid in other companies for that work The company seeks to reward its people fairly and give them the opportunity to increase earnings by linking pay to achieving business and individual performance targets

Aggregate remuneration

During the year, the aggregate remuneration paid to all directors was £5,536,159 (2005/06 £4,376,580) This includes salaries, annual bonuses earned and accrued in the year ended 31 March 2007 but paid after the year end, the value of long-term incentives earned for the period ended 31 March 2006 and paid during the year and benefits in kind

Non-executive directors (including the chairman)

A committee of the board decides the remuneration of the non-executive directors (other than the chairman) Its members are the chairman (Sir Richard Evans) and the executive directors, Philip Green, Simon Batey (to 28 July 2006), Charlie Cornish, Tom Drury (to 27 March 2007), Gordon Waters (to 24 December 2006) and Tim Weller (from 1 August 2006) The committee may take independent advice It is also advised by the group's human resources director The committee met once during the year to review the fees paid to non-executive directors The remuneration committee decides the remuneration of the chairman

Terms of appointment

Non-executive directors' appointments are for an initial period of three years They are subject to reappointment at the first annual general meeting after their initial appointment and at an annual general meeting at least every three years thereafter if they are to be reappointed After nine years in office a non-executive director is required to seek reappointment each year at the annual general meeting They do not have contracts of service In the event of early termination, for whatever reason, they are not entitled to compensation

Non-executive directors' letters of appointment can be inspected at the company's registered office and on the company's website at www unitedutilities com The letters set out the expected time commitment and non-executives agree to devote sufficient time to meet what is expected of them Table 14 summarises the terms of appointment for each non-executive director

Policy statement on non-executive directors' remuneration

The company's policy is to pay annual fees that reflect the responsibilities placed upon the non-executive directors Fees are reviewed each year when account is taken of the level of fees paid in companies of similar size and complexity There are separate annual fees for the chairman, deputy chairman and the other non-executive directors Additional fees are paid to the chairmen of the audit committee (Norman Broadhurst) and remuneration committee (David Jones) Non-executive directors do not participate in any annual bonus or incentive plan, the pension scheme, healthcare arrangements, the company's long-term incentive plans or employee share schemes The company repays the reasonable expenses non-executive directors incur in carrying out their duties as directors

Non-executive directors' remuneration

Non-executive directors' fees were increased on 1 September 2006 The base fee is £50,000 a year (2005 £47,250) The annual fee paid to Sir Peter Middleton, deputy chairman, is £90,000 (2005 £84,000) The additional fees paid to the chairmen of the audit and remuneration committees are £10,000 a year

The chairman's fee increased to £220,000 a year (2005 £210,000) The next review of non-executive directors' fees will be in September 2007 Non-executive directors' remuneration for the year ended 31 March 2007 is set out in table 15

Table 14 Non-executive directors' terms of appointment

	Date first appointed to board	Date of last appointment AGM in	Reappoint no later than AGM in	Notice period	Compensation upon early termination
Sir Richard Evans	01 09 1997	2004	2007	None	None
Sir Peter Middleton	01 01 1994	2006	2007	None	None
Dr Catherine Bell	19 03 2007	n/a	2007	None	None
Norman Broadhurst	01 04 1999	2005	2008	None	None
Paul Heiden	05 10 2005	2006	2009	None	None
David Jones	03 01 2005	2005	2008	None	None
Jane Newell	01 09 1996	2003	n/a	None	None
Andrew Pinder	01 09 2001	2005	2008	None	None
Nick Salmon	04 04 2005	2005	2008	None	None

Notes.

- Jane Newell resigned from the board at the AGM on 28 July 2006
- Sir Peter Middleton will not be standing for re-election at the 2007 AGM

Table 15 Non-executive directors' fees (audited information)

	Total fees 2007 £'000	2006 £'000
Sir Richard Evans	**215 8**	205 0
Dr Catherine Bell	**1 7**	–
Norman Broadhurst	**58 9**	56 3
Paul Heiden	**48 9**	23 1
David Jones	**57 8**	51 4
Sir Peter Middleton	**87 5**	82 3
Jane Newell	**15 4**	46 3
Andrew Pinder	**48 9**	93 8
Nick Salmon	**48 9**	45 9
John Seed	**–**	17 2
Total	**583 8**	621 3

Notes.

- Nick Salmon was appointed to the board on 4 April 2005
- Paul Heiden was appointed to the board on 5 October 2005
- Dr Catherine Bell was appointed to the board on 19 March 2007
- John Seed resigned from the board on 29 July 2005
- Jane Newell resigned from the board on 28 July 2006
- Between August 2004 and March 2006 Andrew Pinder received additional fees in his capacity as a non executive director of Vertex Data Science Limited During the year to 31 March 2006 fees of £47,500 became due These are included in the 2006 figures above He resigned as a director of Vertex Data Science Limited on 31 March 2006

Executive directors

The remuneration committee

The remuneration committee makes recommendations to the board on the group's framework of executive remuneration and its cost It approves, on the board's behalf, the general recruitment terms, remuneration benefits, employment conditions and severance terms for executive management It decides the specific recruitment terms, remuneration benefits, employment conditions, pension rights, compensation payments and severance terms for the executive board directors and other directors who form the executive leadership team

The committee's members are David Jones, Andrew Pinder and Nick Salmon All are non-executive directors determined by the board to be independent in accordance with the Combined Code The committee's members have no personal financial interest in the company other than as shareholders and the fees paid to them as non-executive directors They have no conflicts of interest arising from cross-directorships and are not involved in the day to day running of the group's businesses Jane Newell was a member of the committee until 28 July 2006 Norman Broadhurst, Paul Heiden and Sir Peter Middleton were members until 31 October 2006 Sir Richard Evans attends meetings but is not a member of the committee The committee's terms of reference are available to shareholders on request and are on the company's website at www unitedutilities com

The committee has retained New Bridge Street Consultants LLP to advise it on executive remuneration They also advise the company on the remuneration of a limited number of senior executive managers whose specific terms of employment do not fall within the remit of the remuneration committee This is to ensure consistency in the application of the board's policies on executive remuneration and the general terms of employment approved by the remuneration committee Mercer Human Resource Consulting advise the committee on pensions matters They are also the actuaries to one of the company's pension schemes (United Utilities Pension Scheme) and advise the company on matters relating to its operation Eversheds LLP provide legal advice on the operation of the group's share incentive and share option plans, including drafting the rules and advising on their interpretation and may advise on individual termination arrangements They also provide general legal advice to the group

The committee is assisted by the chief executive, who is consulted on proposals relating to the remuneration of the other executive directors and senior executives and by the group's human resources director They and the company secretary, attend meetings except when the committee discusses matters relating to their own remuneration The committee can and does also seek advice directly from other specialist staff within the group

The committee follows the principles of good governance and the code of best practice It met six times in the year ended 31 March 2007 Individual attendance at the meetings is stated in the corporate governance report in table 12 on page 47 During the year, matters considered by the committee included

- the 2006 salary review for executive directors and other senior executives,
- awards payable under the 2005/06 annual bonus plan and the measures and targets for the 2006/07 plan,
- the size of and performance conditions to apply to the 2006/07 grant of awards under the performance share plan and its equivalent for overseas participants, the international plan, monitoring ongoing performance against the conditions applying to previous grants and the vesting of the 2003/04 awards,
- pension provision for executives,
- monitoring of executive shareholdings against target,
- the terms of appointment and departure of executive directors and other senior executives,
- revisions to share plans to take account of age discrimination legislation, and
- the form and content of the remuneration report in light of developments in stakeholder views and evolving best practice on disclosure

The committee also reviewed the incentive arrangements for executive directors and members of the executive leadership team Details of revised annual bonus arrangements, proposed changes to be made in 2007/08 to the level of performance share plan awards for executive directors and the total shareholder return performance measure and the proposed introduction of a matching share award plan are given later in this report The proposed introduction of a matching share award plan is subject to shareholder approval at the annual general meeting on 27 July 2007 During the year matched investment awards were made to Philip Green and Tim Weller and a special long-term incentive award was granted to Charlie Cornish Details of the awards made to Tim Weller and Charlie Cornish are given later in this report Philip Green's award was made on the basis disclosed in last year's report

The board accepted the committee's recommendations without amendment The chairman of the board ensures the company talks to its major shareholders, when appropriate, about matters relating to remuneration

Policy statement on executive directors' remuneration

The board's policy for executive directors' and senior executives' remuneration is to

- pay a basic salary which compares with other companies of comparable size and complexity,
- use short and long-term incentives to encourage executives to out-perform key targets, thereby linking their rewards to the interests of shareholders and other stakeholders and giving them the opportunity to increase their earnings,
- encourage executives to hold shares in the company, and
- overall, reward executives fairly and responsibly for their contribution to the group's short and long-term performance and avoid paying more than is necessary for achieving this objective

In deciding the executive directors' total remuneration package and individual elements of it, the remuneration committee assesses both the performance of the individual and the company as well as the range of pay in similar companies In making these comparisons it considers the results carefully The company aims to pay within a range of the mid-market rate over time but may pay higher salaries and total remuneration for out-performing individuals (or to attract or retain executives of the right calibre) and where the company itself out-performs The company also takes account of a range of other factors, including the general increases in base salaries taking place within the company Below mid-market pay may result from under-performance by an individual and/or the company or where an individual is new to the role

Fixed rewards include basic salary, a car allowance or company car and fuel for private mileage, life, medical and permanent health insurance and pension benefits Variable rewards take the form of an annual bonus and a long-term incentive (the performance share plan) The plans are designed to establish a clear link between pay and performance by encouraging and rewarding out-performance in both the short and long-term They are based on business and individual performance, linking executives' rewards directly to the interests of shareholders and other stakeholders Annual and long-term awards are non-pensionable

The committee aims to achieve an appropriate balance between fixed and variable rewards It recognises that the group operates in both a regulated and non-regulated environment and therefore needs to ensure that the structure of executive remuneration reflects the practices of the markets in which its executives operate and stakeholder expectations of how the group should be run The board reviews its policy in the light of emerging best practice

During 2006/07, the committee reviewed the operation of the group's incentive arrangements in the light of evolving market practice and to ensure that rewards remained competitive and aligned to stakeholder interests It considered that changes were needed to annual and long-term incentives to make a greater proportion of the reward package performance related, bringing it more in line with market practice to facilitate the recruitment and retention of key executives With effect from 2007/08 the annual bonus maximum for executive directors will be 100 per cent of salary (increased from 75 per cent) and performance share plan awards will be up to 100 per cent of salary (previously 80 per cent)

It is the board's policy that shareholders will be invited to approve all new long-term incentive schemes (as defined in the Listing Rules) and significant changes to existing schemes, save in the circumstances permitted by the Listing Rules Information on and a resolution seeking shareholder approval to the introduction of a matching share award plan are included in the shareholders' circular and notice for this year's annual general meeting and there is a brief summary of its principal terms contained in pages 61 to 62 of this report The plan's rules will be available for inspection by shareholders Under the plan, participants will be able to invest, initially, up to 50 per cent of the annual bonus paid in respect of the previous financial year in company shares which will be matched by the company The vesting of the matched shares will depend upon the achievement of corporate performance targets over a three-year period

The group operates a defined contribution pension scheme which newly appointed directors (and senior executives) can join Three former executive directors were members of the defined benefit section of the pension scheme which is now closed to new entrants

Chart 1 sets out the impact of the board's policy on an executive director's annual total reward It shows both the current and the revised or proposed arrangements, effective from 2007/08, assuming shareholder approval is obtained where necessary It is expressed in terms of the maximum reward opportunity The changes will increase the proportion of the maximum reward opportunity that is 'at risk' from about 56 per cent in 2006/07 to 69 per cent from 2008/09

Chart 1 Executive directors' annual total reward

Notes

- The shading represents the value of each element of the reward package relative to base pay (base pay = 100)
- Pension refers to the defined contribution section of the pension scheme with a company contribution of 25 per cent of basic pay
- The maximum values apply only where maximum annual bonus is achieved and the performance share plan and matching share award plan have paid out fully
- The values for the performance share plan and matching share award plan assume a dividend reinvestment value of six per cent a year for each of the three years of the performance period and in the case of the matching share award plan that a director has invested to the extent initially allowed i e 50 per cent of annual bonus paid for the previous year

The company expects executive directors and other senior executives to acquire and hold shares at least to the value of their basic salary within five years of appointment

Detailed policy in relation to executive directors' remuneration is set out below

Executive directors' remuneration 2006/07

Executive directors' emoluments and the value of the long-term incentive vesting during 2006/07 are set out in table 16

Table 16 Executive directors' emoluments and long-term incentive payments (audited information)

	Gross salary		Annual bonus		Other benefits		Total emoluments		Long term incentive vesting during the year ended 31 March	
	2007 £'000	2006 £ 000	2007 £'000	2006 £ 000	2007 £'000	2006 £ 000	2007 £'000	2006 £ 000	2007 £'000	2006 £ 000
John Roberts	–	525 0	–	229 7	–	36 8	–	791 5	217 2	465 1
Philip Green	686 7	74 3	488 2	–	28 4	2 4	1,203 3	76 7	–	–
Simon Batey	120 7	360 8	78 4	179 5	336 1	18 4	535 2	558 7	148 2	310 1
Charlie Cornish	340 0	273 3	241 7	142 0	17 5	25 4	599 2	440 7	107 5	–
Tom Drury	312 0	277 5	131 7	103 9	667 5	14 5	1,111 2	395 9	–	–
Gordon Waters	235 3	306 3	166 7	143 5	26 3	28 8	428 3	478 6	110 5	237 7
Tim Weller	266 7	–	185 1	–	40 1	–	491 9	–	–	–
Total	1,961 4	1,817 2	1,291 8	798 6	1,115 9	126 3	4,369 1	2,742 1	583 4	1,012 9

Notes.

- Philip Green was appointed to the board on 20 February 2006
- Tim Weller was appointed to the board on 1 August 2006 His other benefits include £30 435 in relation to reimbursement of relocation costs
- Tom Drury was appointed to the board on 9 May 2005 resigned from the board on 27 March 2007 and left the company on 31 March 2007 His other benefits include payments totalling £319 300 in relation to the disposal of Vertex Data Science Limited and £329 712 made in connection with his loss of office
- Simon Batey resigned from the board on 28 July 2006 and left the company on 31 July 2006 His other benefits include payments totalling £331 003 made in connection with his loss of office
- Gordon Waters died on 24 December 2006 An ex-gratia payment was made to his widow with a net value of £9 410 after offsetting amounts due to Gordon
- The value of the long-term incentive plan vesting during the year ended 31 March 2007 is based on the share price when the awards under the 2003/04 performance share plan were exercised The awards relate to the three-year performance period which ended on 31 March 2006
- Other benefits include the taxable value of the car or car allowance private fuel and medical insurance

A – Salary

The remuneration committee reviews salaries each year taking account of group and personal performance It commissions independent assessments of market rates based on the practice of other utility companies and companies of a similar size and complexity and takes account of the levels of pay awards elsewhere in the group In this way it aims to establish whether an increase should apply and, if so, what it should be It also considers whether there should be any departures from the norm, for example, to ensure that salaries are competitive and consistent with the application of board policy on executive remuneration

The following changes were made to the annual salaries of executive directors during the year

Table 17 Executive directors' salaries

	Salary at 31 March 2007 £ 000	Salary at 31 March 2006 £ 000	Date of change
Philip Green	695 0	675 0	1 Sept 2006
Simon Batey	–	371 0	–
Charlie Cornish	340 0	290 0	1 April 2006
Tom Drury	319 3	310 0	1 Sept 2006
Gordon Waters	–	315 0	–
Tim Weller	400 0	–	1 July 2006

Notes.

- Gordon Waters salary was increased to £330,750 on 1 September 2006 He died on 24 December 2006

B – Annual bonus

The annual bonus is designed to motivate executive directors and other senior executives to achieve the group's key financial, operational and strategic objectives Directors are rewarded according to the company's financial and operational performance for the year and the achievement of individual targets Targets are set each year The operational and individual targets may include performance against key stakeholder measures and personal objectives Annual bonus awards are normally paid in cash

(a) 2007/08

The remuneration committee has decided that, for the 2007/08 annual bonus plan, the maximum bonus will be 100 per cent of salary for executive directors and 60 per cent for other members of the executive leadership team For executive directors (except Paul Capell), group financial measures will account for bonus payments worth up to 50 per cent of salary For Paul Capell, group financial measures will account for 30 per cent The measures will be group profit before restructuring costs, other non-recurring items, investment income and finance expense (PBEIT) and profit before restructuring costs, other non-recurring items and taxation (PBET) (weighted equally)

For each of the financial measures, one quarter of the maximum award allocated to that measure becomes payable once the threshold target is met Awards increase in value on a straight-line basis until half of the maximum award is payable for achieving an intermediate target between the threshold and stretch targets Awards continue to increase in value on a straight-line basis between the intermediate and stretch targets, at which point the maximum award is payable The stretch targets are demanding and achievement represents results which exceed expectations

Executive directors' annual bonus payment will also depend on operational performance in other areas of the group's activities

The measures include operational targets in the water, wastewater and electricity distribution businesses, maintaining the company's corporate responsibility performance in the Business in the Community's (BitC) Corporate Responsibility Index, an authoritative and broad external benchmark of responsible business practice in relation to the environment and society, for improving the group's score in the Dow Jones European and World Sustainability Index, and achieving improvements in employee satisfaction measured by responses to questions in an externally conducted and verified employee opinion survey

Personal objectives account for the balance of the bonus opportunity Paul Capell's personal objectives include financial measures relating to the international business

The executive directors' annual bonus plan measures for 2007/08 are summarised in table 18

(b) 2006/07
The financial measures to determine annual bonuses for 2006/07 were PBEIT and PBET (weighted equally) Targets were set for the financial performance of the group and the major businesses The maximum bonus opportunity totalled 50 per cent of salary with the allocation between group and business performance varying between executives Non-financial targets accounted for up to a further 25 per cent of salary Five per cent was based on achieving a water and wastewater customer service target of 65 per cent of respondents to an externally conducted survey scoring four or five, i e being very or extremely satisfied with how the company dealt with their query or contact Two and a half per cent was based on achieving a score in the BitC Corporate Responsibility Index of 96 per cent, two and a half per cent on scores in the 2006/07 employee opinion survey and 15 per cent on the achievement of individual objectives

A breakdown of achievement against financial, customer service, corporate responsibility and employee satisfaction targets, the achievement of personal objectives and the outcome of the 2006/07 annual bonus plan for executive directors is shown in table 19 The corporate responsibility performance was 96 per cent The customer service performance was 74 per cent

Neither of the employee related targets (based on the results of the employee opinion survey) was achieved resulting in no bonus being payable for that element

C – Other benefits
Directors are paid a car allowance of £14,000 a year or have the use of a company car, are reimbursed the cost of fuel for business and private use, and are provided with medical and life insurance and, if not a member of the defined benefit pension scheme, permanent health insurance

D – Long-term incentives
(i) Performance share plan
Executive directors and other senior executives participate in the performance share plan Awards are granted at the discretion of the plan's trustee (United Utilities Employee Share Trust Limited) on the recommendation of the remuneration committee Each year, participants may be awarded a right to acquire a maximum number of shares worth up to a percentage of their annual salary at the date of the award, at no cost to them The number of shares awarded is based on the market price of a share at that time The plan's rules provide for a maximum award of 100 per cent of annual salary However, annual awards made to date to directors have been limited to 80 per cent of salary Awards to other executives range between 15 and 60 per cent of salary Grants are normally made within 42 days of the publication of results The main grant normally occurs after the publication of the preliminary results A subsequent grant may be made after the publication of the interim results for executives who have become eligible after the main grant has been made

The proportion of the award that will vest depends upon the group's performance against specified targets over a performance

Table 18 Executive directors' annual bonus plan measures 2007/08

	Financial performance measures		Operational performance measures			Personal objectives	
	Group PBEIT	Group PBET	Operational targets	Corporate responsibility	Employee satisfaction		Total
Philip Green	25	25	20	2.5	2.5	25	100
Tim Weller	25	25	20	2.5	2.5	25	100
Charlie Cornish	25	25	20	2.5	2.5	25	100
Paul Capell	15	15	5	2.5	2.5	60	100

Notes.
• Figures are a percentage of base earnings during the year

Table 19. Executive directors' annual bonus plan outcome 2006/07

	Financial performance measures		Operational performance measures						Personal objectives			
			Customer service		Corporate responsibility performance		Employee satisfaction				Total	
Award	Max	Actual	Max	Actual	Max	Actual	Max	Actual	Max	Actual	Max	Actual
Philip Green	50	49.5	5	5	2.5	2.5	2.5	–	15	14.1	75	71.1
Simon Batey	50	49.5	5	5	2.5	2.5	2.5	–	15	8.0	75	65.0
Charlie Cornish	50	49.5	5	5	2.5	2.5	2.5	–	15	14.1	75	71.1
Tom Drury	50	24.5	5	5	2.5	2.5	2.5	–	15	10.2	75	42.2
Gordon Waters	50	48.3	5	5	2.5	2.5	2.5	–	15	15.0	75	70.8
Tim Weller	50	49.5	5	5	2.5	2.5	2.5	–	15	12.4	75	69.4

Notes.
• Figures are a percentage of base earnings during the year

period This period is not less than three years, beginning at the start of the financial year during which the award is made There is no re-testing if the performance criteria are not met

To date, the performance criteria have been the company's total shareholder return (TSR) performance when compared with the TSR performance of a comparator group of other companies, and underlying business performance

TSR is widely used as an externally verifiable measure of a shareholder's return Relating awards to the company's relative TSR performance supports the policy objectives of linking executives' rewards directly to the group's performance and shareholders' interests and gives executives the opportunity to increase their earnings by meeting and out-performing key long-term measures

The remuneration committee has the discretion to make adjustments to the comparator group or the period over which relative TSR is measured during the performance period to maintain the integrity of the plan, for example, following a takeover bid or activity or merger/demerger announcement During the year, the remuneration committee considered the treatment of changes affecting companies in the comparator groups for awards made in 2004/05, 2005/06 and 2006/07

No award will vest if the company's TSR performance is below the median for the comparator group If performance is between median and upper quartile, the proportion of the maximum number of shares in the award which will vest will be calculated on a straight-line basis between 25 per cent and 100 per cent External advisers regularly assess and report to the committee on the company's TSR performance and ranking in the comparator group Their report at the end of the performance period enables the committee to determine the extent to which this performance condition has been met

The vesting of awards is also subject to the remuneration committee being satisfied that the company's recorded TSR performance is consistent with underlying business performance The committee tests whether this condition has been satisfied after the end of each performance period in accordance with the terms of each award Reference may be made to actual against planned performance in key corporate financial measures The committee takes account of the impact of the transition to International Financial Reporting Standards when assessing underlying business performance against the performance measures

There is no automatic waiving of performance conditions if there is a change of control, capital reconstruction or winding up of the company The extent (if any) to which awards will vest and any modifications of performance conditions are at the trustee's discretion, with the consent of the remuneration committee

When a participant's employment terminates during a performance period and the reason falls within the 'good leaver' provisions of the plan, the vesting of an award is at the trustee's discretion If discretion is exercised, the maximum number of shares in an award is pro-rated to service in the performance period and vesting is subject to satisfying the performance conditions (modified if appropriate) Except in the case of the death of a participant, there is normally no early vesting of awards Awards lapse where terminations during the performance period do not satisfy the good leaver provisions

Participants normally have three months from the date the award vests in which to exercise their right to acquire the number of shares that have vested Awards are normally satisfied by the transfer of shares from the trustee to participants The trustee may periodically buy shares in the market to ensure that it can satisfy its liabilities when an award vests These purchases are normally financed by the company making a loan to the trustee The company takes account of the vesting timetable and likely scale of vesting in determining the financial assistance it provides for the trustee The company reviews this arrangement from time to time to ensure its cost effectiveness Awards may also be satisfied by allotting shares Details of the number of shares held by the trust at 4 June 2007 are given in the notes to table 9 on page 44

The performance share plan was amended during the financial year in the manner approved by shareholders at the 2006 annual general meeting Full details of the amendments made were given in the annual report 2006 but principally they included the introduction of notional dividend reinvestment on the number of shares comprised in awards, a reduction in the scale of vesting for median performance and minor changes to aid the administration of the plan Details of how the notional dividend reinvestment provisions have affected directors' individual awards are set out in table 24 on pages 59 and 60

(a) 2007/08 grant

During the year, the committee reviewed the operation of the comparative TSR performance condition It concluded that for the 2007/08 award United Utilities' TSR performance over three years would be measured against a TSR index rather than a comparator group ranking The inclusion of appropriate companies in a comparator group is critical for relative performance to be meaningful However, it is also important that the group should be of a reasonable size to avoid the performance of a few companies having a disproportionate impact on the outcome of the plan, to be able to accommodate changes in the comparator group and to avoid too high a leverage between the company's relative position and the proportion of the award that vests The comparator group approach has become increasingly inappropriate as the number of comparable companies has declined Using an index allows for a meaningful comparison of performance to be made and a smoother sliding scale of vesting of awards The index will be constructed by assessing the TSR performance of the following companies with their influence on the index being weighted according to their relevance and size

Table 20 TSR – weighting of comparator companies

Company	Weighting
Kelda	100%
National Grid	25%
Northumbrian Water	75%
Pennon Group	75%
Scottish & Southern Energy	25%
Severn Trent	100%

It is proposed that none of the award will vest if United Utilities' performance is below the index 25 per cent of the award will vest for a performance equal to the index and 100 per cent for outperforming the index by 12 per cent over the three-year performance period to 31 March 2010 Vesting will be on a sliding scale for performance between these points The vesting of awards will also be subject to the remuneration committee being satisfied that the company's recorded TSR performance is consistent with underlying business performance

(b) 2006/07 grant
Dunng the year, option awards to a maximum value of 80 per cent of annual salary were made to directors in respect of the 2006/07 performance share plan The extent to which awards vest will be based on the company's TSR performance relative to the comparator group of companies over the penod 1 April 2006 to 31 March 2009 The TSR comparator group compnses the following 16 companies in addition to United Utilities AMEC, AWG, Balfour Beatty, BG Group, Bntish Energy, BT Group, Centrica, International Power, Kelda Group, National Grid, Northumbrian Water, Pennon Group, Scottish & Southern Energy, ScottishPower, Severn Trent and Vindian The committee has taken account of corporate events affecting AWG, ScottishPower, Severn Trent and Vindian since the start of the performance penod Awards will vest after the end of the performance period provided that the remuneration committee is satisfied that the company's recorded TSR performance is consistent with the company's underlying business performance

The vesting scale is shown in table 21

Table 21. 2006/07 Performance share plan vesting scale

Comparator group size (No of companies)		17
Ranking in comparator group	% of max award vesting	% of salary
1 to 4	100	80
5	92	73 6
6	75	60
7	63	46 4
8	58	33 6
9	42	20
10 or below	–	–

The group's total shareholder return of 18 7 per cent from 1 April 2006 to 31 March 2007 placed it in 15th position

(c) 2005/06 grant
Directors have awards to a maximum value of 80 per cent of annual salary in respect of the 2005/06 performance share plan The extent to which awards vest will be based on the company's TSR performance relative to the comparator group of companies over the penod 1 April 2005 to 31 March 2008 The TSR comparator group compnses the following 16 companies in addition to United Utilities AMEC, AWG, BAA, Balfour Beatty, BG Group, BT Group, Centrica, International Power, Kelda Group, National Grid, Northumbrian Water, Pennon Group, Scottish & Southern Energy, ScottishPower, Severn Trent and Vindian The committee has taken account of corporate events affecting AWG, BAA, ScottishPower, Severn Trent and Vindian since the start of the performance penod Awards will vest after the end of the performance penod provided that the remuneration committee is satisfied that the company's recorded TSR performance is consistent with the company's underlying business performance

The vesting scale is shown in table 22

Table 22· 2005/06 Performance share plan vesting scale

Comparator group size (No of companies)		17
Ranking in comparator group	% of max award vesting	% of salary
1 to 4	100	80
5	93	74 4
6	78	62 4
7	63	50 4
8	48	38 4
9	33	26 4
10 or below	–	–

The group's total shareholder return of 39 7 per cent from 1 April 2005 to 31 March 2007 placed it in 17th position

(d) 2004/05
Directors have awards to a maximum value of 80 per cent of annual salary in respect of the 2004/05 performance share plan The extent to which awards vest will be based on the company's TSR performance relative to the comparator group of companies over the penod 1 April 2004 to 31 March 2007 The TSR comparator group compnses the following 16 companies in addition to United Utilities AMEC, AWG, BAA, Balfour Beatty, BG Group, BT Group, Centrica, International Power, Kelda Group, National Grid, Northumbrian Water, Pennon Group, Scottish & Southern Energy, ScottishPower, Severn Trent and Vindian In addition, three smaller companies, Bristol Water, East Surrey Holdings and International Energy Group, were included as a notional combined 17th company made up in proportion to their market capitalisations at the start of the performance penod The committee has taken account of corporate events affecting AWG, BAA, ScottishPower, Severn Trent, Vindian and the notional 17th company since the start of the performance penod Awards will vest after the end of the performance penod provided that the remuneration committee is satisfied that the company's recorded TSR performance is consistent with the company's underlying business performance

The vesting scale is shown in table 23

Table 23 2004/05 Performance share plan vesting scale

Comparator group size (No of companies)		18
Ranking in comparator group	% of max award vesting	% of salary
1 to 4	100	80
5	97	77 6
6	82	65 6
7	68	54 4
8	54	43 2
9	40	32
10 or below	–	–

The group's total shareholder return of 99 3 per cent from 1 April 2004 to 31 March 2007 placed it in 15th position As a result none of the 2004/05 awards will vest

Details of executive directors' continuing scheme interests in the performance share plan, including those awarded during the year, are set out in table 24

Table 24 Executive directors' continuing scheme interests in the performance share plan (audited information)

							Award details	Contingent scheme interest at 1 April 2006		Contingent scheme interest awarded during the year		**Contingent scheme interest at 31 March 2007**	
		Award date	Performance period	% of salary	Value at award date £ 000	Market price of a share at award pence	Max no of shares	Max no of shares	Value £ 000	No of shares	Value £ 000	**Max no of shares**	**Value £'000**
John Roberts													
2004/05	Ordinary A shares	18 8 04	1 4 04 to 31 3 07	80	384 0	527 0 341 25	51,885 28,825	73,447 –	506 4 –	(24,483) –	n/a –	**48,964** **–**	**369 9** **–**
2005/06	Ordinary	30 6 05	1 4 05 to 31 3 08	80	403 2	657 5	61,324	61,324	422 8	(40 902) –	n/a	**20,422**	**154 3**
Total					787 2			134,771	929 2	(65,385)	–	**69,386**	**524 2**
Philip Green													
2005/06	Ordinary	13 2 06	1 4 05 to 31 3 08	80	540 0	688 5	78,432	78,432	540 8	–	–	**78,432**	**592 6**
2006/07	Ordinary	8 9 06	1 4 06 to 31 3 09	80	556 0	676 0	82 249	–	–	87,489	557 3	**87,489**	**661 0**
Total					1,096 0			78,432	540 8	87,489	557 3	**165,921**	**1,253 6**
Simon Batey													
2004/05	Ordinary A shares	30 6 04	1 4 04 to 31 3 07	80	264 0	547 0 347 75	35,658 19,810	50,477 –	348 0 –	(11,202) –	n/a –	**39,275** **–**	**296 7** **–**
2005/06	Ordinary	30 6 05	1 4 05 to 31 3 08	80	277 2	657 5	42,160	42,160	290 7	(23,427)	n/a	**18,733**	**141 5**
Total					541 2			92,637	638 7	(34,629)	–	**58,008**	**438 2**
Charlie Cornish													
2004/05	Ordinary A shares	30 6 04	1 4 04 to 31 3 07	80	188 0	547 0 347 75	25,407 14,115	35,965 –	248 0 –	– –	– –	**35,965** **–**	**271 7** **–**
2005/06	Ordinary	30 6 05	1 4 05 to 31 3 08	80	200 0	657 5	30,419	30 419	209 7	–	–	**30,419**	**229 8**
2006/07	Ordinary	8 9 06	1 4 06 to 31 3 09	80	272 0	676 0	40,237	–	–	42,799	272 6	**42,799**	**323 3**
Total					660 0			66,384	457 7	42,799	272 6	**109,183**	**824 8**
Tom Drury													
2004/05	Ordinary A shares	30 6 04	1 4 04 to 31 3 07	80	162 0	547 0 347 75	21,888 12,160	30 984 –	213 6 –	– –	– –	**30,984** **–**	**234 1** **–**
2005/06	Ordinary	30 6 05	1 4 05 to 31 3 08	80	248 0	657 5	37,719	37,719	260 0	–	–	**37,719**	**285 0**
2006/07	Ordinary	8 9 06	1 4 06 to 31 3 09	80	255 4	676 0	37,787	–	–	40,194	256 0	**40,194**	**303 7**
Total					665 4			68,703	473 6	40,194	256 0	**108,897**	**822 8**

Table 24 continued. Executive directors' continuing scheme interests in the performance share plan (audited information)

							Award details	Contingent scheme interest at 1 April 2006		Contingent scheme interest awarded during the year		**Contingent scheme interest at 31 March 2007**	
		Award date	Performance period	% of salary	Value at award date £ 000	Market price of a share at award pence	Max no of shares	Max no of shares	Value £ 000	No of shares	Value £'000	**Max. no of shares**	**Value £'000**
Gordon Waters													
2004/05	Ordinary A shares	30 6 04	1 4 04 to 31 3 07	80	224 0	547 0 347 75	30,258 16,810	42,832	295 3	–	–	**42,832**	**323 6**
2005/06	Ordinary	30 6 05	1 4 05 to 31 3 08	80	235 2	657 5	35,772	35,772	246 6	–	–	**35,772**	**270 3**
2006/07	Ordinary	8 9 06	1 4 06 to 31 3 09	80	264 6	676 0	39,143	–	–	41,636	265 2	**41,636**	**314 6**
Total					723 8			78,604	541 9	41 636	265 2	**120,240**	**908 5**
Tim Weller													
2006/07	Ordinary	8 9 06	1 4 06 to 31 3 09	80	320 0	676 0	47,338	–	–	50,354	320 8	**50,354**	**380 4**
Total					320 0			–	–	50,354	320 8	**50,354**	**380 4**

Notes

- The values shown for 1 April 2006 have been calculated using the mid market price of a share at close of business on 31 March 2006 of 689 5 pence
- The values shown for 31 March 2007 have been calculated using the mid-market price of an ordinary share at close of business on 30 March 2007 of 755 5 pence
- The contingent scheme interest at 1 April 2006 for the 2004/05 awards incorporate an adjustment in the number of shares in awards to take account of the second stage of the rights issue The number of ordinary shares increased by a factor of 1 41559048 and the number of A shares reduced to zero This reflects the position of shareholders taking up their rights and takes account of the subscription cost
- The market price of a share at award is the mid market price of an ordinary or A share at close of business on the last trading day immediately prior to the award date This is used to calculate the maximum number of shares comprising the award
- John Roberts 2004/05 award was part of a special grant to five executives whose awards could not be made until a rule change relating to retirement had been approved at the 2004 annual general meeting The market prices of an ordinary and A share at the date of their awards were 527 0 pence and 341 25 pence respectively However as disclosed in the note accompanying the resolution to the annual general meeting to ensure that the beneficiaries of the rule change were treated neither more nor less favourably than participants in the main grant the maximum number of shares in their awards was calculated using the market prices of 547 0 pence (ordinary share) and 347 75 pence (A share) applicable to the main grant
- Philip Green's 2005/06 award was granted on the date he joined the group
- The contingent scheme interest awarded during the year in respect of the 2006/07 plan comprises the number of award shares granted and additional shares resulting from the notional reinvestment of notional dividend payable during the year on the number of shares subject to the award The value of contingent scheme interest awarded during the year is the value of the initial award plus the value of notional dividends payable during the year
- The reduction in contingent scheme interest during the year and the consequential reduced contingent scheme interest at 31 March 2007 in respect of the 2004/05 and 2005/06 awards for John Roberts and Simon Batey are based on the assumption that the plan s trustees will exercise their discretion after the end of the respective performance periods and allow the awards to vest with the maximum number of shares in their awards being time pro-rated to their dates of leaving
- Details of the criteria used for grants under the performance share plan are on pages 57 to 58 Tom Drury s 2004/05 award was granted prior to his joining the board The performance conditions for the 2004/05 award set out on page 58 apply to 50 per cent of his award The vesting of the other 50 per cent is subject to performance against cumulative earnings before interest tax and amortisation (EBITA) and average return on capital employed (ROCE) targets over the three years from 1 April 2004 to 31 March 2007 set out in the business plan for Vertex Data Science Limited agreed immediately before the start of the performance period There is a sliding scale of vesting

(e) 2003/04 grant

Dunng the year, awards granted under the 2003/04 plan vested The extent to which awards vested was based on the company's TSR performance relative to the comparator group of companies over the penod 1 Apnl 2003 to 31 March 2006 At the beginning of the performance penod the comparator group compnsed the following 15 companies in addition to United Utilities BAA, BG Group, Boots Company, British Energy, Centrica, International Power, J Sainsbury, Kelda Group, Morrisons, National Grid Group, Scottish & Southern Energy, ScottishPower, Severn Trent, Tesco and Vindian During the performance penod British Energy delisted It was retained in the comparator group and United Utilities' TSR performance relative to it was compared from the beginning of the performance penod until the day before the delisting United Utilities' TSR for the performance penod was 66 5 per cent which placed it eighth out of 16 The remuneration committee was satisfied that the TSR performance was consistent with the company's underlying business performance In particular, performance exceeded the earnings per share, dividend cover and interest cover targets for 2005/06 set out in the group's five-year business plan to 2007/08 41 per cent of the maximum award, therefore, vested in accordance with the company's relative TSR performance, 59 per cent lapsed Further details of directors' scheme interests in the performance share plan, vested during the year, are set out in table 25

Table 25 Executive directors' scheme interests in the performance share plan vested during the year (audited information)

	Award details							Contingent scheme interest at 1 April 2006		Contingent scheme interest lapsed during the year	Contingent scheme interest vested during the year		Value of award at exercise	
	Award date	Performance period	% of salary	Value at award date £ 000		Market price of a share at award pence	Max no of shares	Max no of shares	Value £ 000	No of shares	No of shares	Value £ 000	Market price of a share at exercise pence	Value £ 000
John Roberts														
2003/04	29 9 03	1 4 03 to 31 3 06	80	360 0	Ordinary	469 0	57,843	81,882	564 6	48,311	33,571	222 4	647 0	217 2
					A share	276 0	32,135	–	–	–	–	–	–	–
Simon Batey														
2003/04	29 9 03	1 4 03 to 31 3 06	80	240 0	Ordinary	469 0	38,556	54,579	376 3	32,202	22,377	148 2	662 5	148 2
					A share	276 0	21,420	–	–	–	–	–	–	–
Charlie Cornish														
2003/04	29 9 03	1 4 03 to 31 3 06	80	188 0	Ordinary	469 0	28,710	40 641	280 2	23,979	16,662	110 4	645 0	107 5
					A share	276 0	15,950	–	–	–	–	–	–	–
Gordon Waters														
2003/04	29 9 03	1 4 03 to 31 3 06	80	184 0	Ordinary	469 0	29,565	41,851	288 6	24,693	17,158	113 7	644 0	110 5
					A share	276 0	16,425	–	–	–	–	–	–	–

Notes.

- The market price of a share at award is the mid market price of an ordinary or A share at close of business on the last trading day immediately prior to the award date This is used to calculate the maximum number of shares comprising the award
- The maximum number of shares comprising the contingent scheme interest at 1 April 2006 incorporates an adjustment to take account of the rights issue The values of shares comprising awards based on the last quoted cum-rights share price of 531 5 pence was divided by the theoretical ex rights price of 459 54 pence to determine the revised numbers of shares shown above
- The values shown for 1 April 2006 have been calculated using the mid-market price of a share of 689 5 pence at close of business on 31 March 2006
- Awards vested on 6 June 2006 in respect of 41 per cent of the maximum number of shares under option and lapsed in respect of 59 per cent The values for scheme interests vesting during the year have been calculated using the mid market price of a share of 662 5 pence on close of business on that date
- The above awards were granted as option awards' whereby the participant is granted an option to acquire the number of shares which vests under the plan The options were exercisable over a period of three months from the vesting date No consideration was payable by the executives either upon grant of the option award or upon the subsequent exercise of the option

(ii) Proposed matching share award plan

Full details of the proposed matching share award plan are included in the shareholders' circular and notice for the 2007 annual general meeting at which approval of the plan's rules will be sought The rules will be available for inspection

The decision to seek shareholder approval for the adoption of the new matching share award plan follows a detailed review of long-term incentives It was considered necessary to bring the incentive potential into line with the market Participants must make a long-term investment in United Utilities by acquiring shares with their bonus to benefit from the plan These will be matched by the company after three years subject to achievement of a balance of performance measures so ensuring that executives are encouraged to deliver shareholder returns as well as improving the underlying financial and operational performance Operational performance is seen as a key determinant of success, particularly in view of the regulatory framework in which United Utilities operates

To participate in the plan, executive directors will be required to invest 20 per cent of their previous year's annual bonus in shares There will also be the opportunity to voluntarily invest additional bonus into shares The total investment in the plan will initially be limited to 50 per cent of annual bonus Other selected senior executives will be invited to voluntarily invest up to 50 per cent of their bonus in shares In all cases, invested shares must be retained for the duration of the performance period which will be three years It is proposed that the first awards will be based on the outcome of the 2006/07 annual bonus plan

Participants who have invested part of their bonus in shares will receive a corresponding matching award over shares with a value at the award date equal to 2 1 for any compulsorily invested bonus and 1 1 for any voluntarily invested bonus

All matching ratios are calculated on a 'gross of tax' basis The number of matching shares subject to an award will be augmented by the notional reinvestment of any dividends payable on them from the beginning of the performance period until the date the awards vest The plan's rules limit the total value of matching shares subject to an award to 100 per cent of base salary

Matching awards will normally vest subject to satisfying performance conditions which will be measured over a fixed three-year period with no retesting and the participant remaining in employment throughout the performance period If an event occurs which causes the remuneration committee reasonably to consider that the targets and/or measures are no longer appropriate, it may recommend the trustee to waive, vary or replace any or all of the targets and/or measures in such a way as, in the reasonable opinion of the committee, produces a fairer measure of performance for the performance period (or any abbreviated part of it), provided that the varied or replacement targets and/or measures are not materially more difficult to satisfy than the original targets and/or measures (as the case may be) would have been had the event in question not occurred

If there is a change of control or voluntary winding up of the company, the award may be exercised at the trustee's discretion and the number of shares over which the award may be exercised will depend on the extent to which the trustee determines the performance conditions (amended or otherwise) have been achieved and taking into account any other criteria (such as the time pro-rating of awards) as the trustee considers relevant If there is a reconstruction or demerger, the trustee may vary the terms and/or allow the early vesting of the award having due regard to the object and purposes of the award

If a participant ceases to be an employee because of death, ill health, retirement on or after reaching contractual retirement age or redundancy at any time during the performance period, the award may be exercised at the trustee's discretion and the number of shares over which the award may be exercised will depend on the extent to which the trustee determines the performance conditions (amended or otherwise) have been achieved and will be reduced on a time pro-rating basis

Initially, half of the shares under a matching award will be subject to the relative TSR measure and scale of vesting that it is proposed to apply to awards made under the performance share plan from 2007

Vesting of the remaining half of the shares in the matching award will be subject to key operational measures For the first awards, there will be 17 measures in four operational areas A quarter of this portion of the award (12 5 per cent of the total award) will vest for satisfying all of the measures in an operational area All 17 measures will need to be achieved for the whole of this half of the award to vest

The scale of vesting is set out in table 26

Table 26. Vesting scale

Operational areas	Total no of measures	Number of measures to be achieved for vesting under each measure			
		0% vesting	25% vesting	50% vesting	100% vesting
1 Quality & environment	5	< 3	3	4	5
2 Customer service	4	< 2	2	3	4
3 Finance & efficiency	4	< 2	2	3	4
4 Employee related	4	< 2	2	3	4
Value of vesting per operational area (% of total matching award)		0%	3 125%	6 25%	12 5%

Notes

Vesting under each operational area is not dependent upon achieving a certain level of performance across the other three measures

The targets will be set by the remuneration committee before awards are granted and, depending on the measure, will require maintenance or improvement of the company's performance

The measures in each operational area for which targets will be set are

1 Quality & environment
   - 1 1 OPI water quality index performance – a comparative index of performance across all water companies
   - 1 2 Bacteriological failure incidents
   - 1 3 Wastewater compliance
   - 1 4 Pollution incidents
   - 1 5 Leakage

2 Customer service – all measures as reported by the relevant regulator
   - 2 1 Customer minutes lost
   - 2 2 Customer interruptions
   - 2 3 Customer satisfaction (Electricity)
   - 2 4 Customer satisfaction (Water)

3 Finance & efficiency
   - 3 1 Water – improvement in the relative efficiency band as published by the regulator
   - 3 2 Wastewater – improvement in the relative efficiency band as published by the regulator
   - 3 3 Electricity – improvement in the relative efficiency ranking as published by the regulator
   - 3 4 PBET

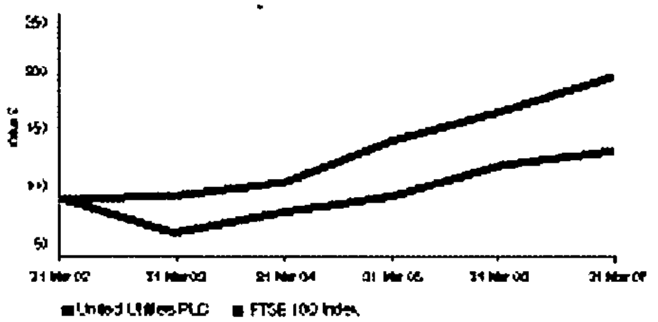
4 Employee related all measures verified against employee survey results published by the company's external consultant
   - 4 1 Overall job satisfaction
   - 4 2 Overall satisfaction with their business as an employer
   - 4 3 "Directors and senior managers in their part of the business don't just talk about our values, they live by them"
   - 4 4 Employee engagement

The performance period for the first awards will be 1 April 2007 to 31 March 2010

Performance graph

Chart 2 compares the company's annual TSR performance for the past five years against the FTSE 100 Index This index was chosen as it is the most appropriate broad equity market index This comparison also supplements the information on the group's TSR performance relative to the comparator groups in the performance share plan The TSR indices used in the chart have been calculated in accordance with the Directors' Remuneration Report Regulations 2002 relative to a base date of 31 March 2002

Chart 2: Total shareholder return
Source: Thomson Financial



Notes

- This graph shows the value by 31 March 2007 of £100 invested in United Utilities on 31 March 2002 compared with the value of £100 invested in the FTSE 100 Index The other points plotted are the values at intervening financial year ends

Share options

Grants of executive share options were made under the company share option plan 1999 up to and including 2002 From 2003, awards under the performance share plan have replaced further grants of executive share options

Executive directors are eligible to participate in the all-employee SAYE scheme (ShareSave) Neither the award nor the exercise of ShareSave options is dependent upon the satisfaction of performance conditions The last grant of options was ShareSave 2004 Details of their interest in ShareSave options are shown in table 27

Executive directors' shareholdings

Executive directors are expected to build up and retain a target shareholding equal to the value of their basic salary, normally within five years of appointment Performance share plan awards are delivered in shares and executives can retain all the shares that vest if they make a cash payment to meet their PAYE statutory liabilities The company prefers a flexible approach to the accumulation of a shareholding, which takes account of individual circumstances, and has decided not to require executives to retain a proportion of shares that vest under its incentive plans Executive directors' interests in shares, as at 31 March 2007, are listed in table 9 of the directors' report on page 44 The value of these interests relative to their yearly salaries are shown in table 28

Table 28 Executive directors' shareholdings

	Salary £'000	Value of shareholding £'000	Value relative to salary %	Target to be achieved by
Philip Green	695 0	758 5	109 1	13 02 11
Charlie Cornish	340 0	78 3	23 0	27 01 09
Tim Weller	400 0	294 4	73 6	01 07 11

Notes

- The value of the shareholding is based on a share price of 754 5 pence This is the share price averaged over the final three months of the financial year

Matched share investment scheme for Philip Green

Full details of the matched share investment scheme for Philip Green, introduced as part of his terms of appointment, were disclosed in the remuneration report for 2006 In accordance with the rules of that scheme, Philip Green invested in 100,000 shares and a conditional matched award of 100,000 shares was made to him on 16 January 2007 which will transfer to him at the end of the five-year retention period on 12 February 2011, subject to his still being employed by the company at that date The number of shares subject to the matching share award will be increased by the notional reinvestment of dividends payable on the matched shares over the course of the five-year retention period Details of his scheme interests are shown in table 29

Table 27 Directors' interests in options (audited information)

	At 1 April 2007	Granted/ (lapsed)	Exercised during the year	At 31 March 2007	Exercise price per share pence	First date exercisable	Last date exercisable
Simon Batey							
ShareSave 2004	1,751	(1,751)	–	–	396 0	–	–
Total	1,751	(1,751)	–	–			
Gordon Waters							
ShareSave 2002	2,648	(217)	–	**2,431**	432 3	25 12 06	24 12 07
Total	2,648	(217)	–	**2,431**			

Notes

- The mid-market price of a share on 30 March 2007 was 755 5 pence and the range in the year was 626 0 pence to 799 0 pence
- No amount is payable by a participant for the grant of an option
- For ShareSave 2002 the number of shares under option at 1 April 2006 and 31 March 2007 and the exercise price reflect adjustments to take account of the rights issue
- The partial lapsing of and the first and last dates exercisable for Gordon Waters ShareSave option reflect the application of the plan's rules in respect of his death
- The aggregate notional gain made by directors on the exercise of options during the year (based on the difference between the mid-market price of a share on the day on which options were exercised and the exercise price) was £nil (2006 £7 852)

Table 29: Philip Green's continuing scheme interests in the matched share investment scheme (audited information)

			Award details		Contingent scheme interest at 1 April 2006		Contingent scheme interest awarded during the year		**Contingent scheme interest at 31 March 2007**	
Award date	Retention period	Market price of a share at award pence	No of shares	Value £'000	No of shares	Value £'000	No of shares	Value £'000	**No of shares**	**Value £'000**
16 1 07	13 2 06 to 12 2 11	761 0	100,000	761 0	–	–	106,371	805 9	**106,371**	**803 6**

Notes

- The market price of a share at award is the mid-market price of a share at close of business on the award date
- The contingent scheme interest awarded during the year comprises the initial award of 100 000 shares and 6 371 shares added in respect of notional dividends payable on the shares during the year
- The value of contingent scheme interest awarded during the year is the value of the initial award plus the value of notional dividends payable during the year
- The value of the contingent scheme interest at 31 March 2007 has been calculated using the mid-market price of a share of 755 5 pence at close of business on 30 March 2007

Matched share investment scheme for Tim Weller
Tim Weller commenced employment with the company on 1 July 2006 and was appointed to the board of the company on 1 August 2006 As part of the terms of his recruitment and retention, the company agreed to establish a matched share investment scheme This is a long-term incentive scheme under which Tim Weller is the sole participant Full details of the scheme are set out below The arrangement was introduced specifically to facilitate Tim Weller's recruitment The company considered the circumstances of his recruitment were such that it was important and necessary to introduce these arrangements to attract him as the new chief financial officer and to retain him up to and beyond the implementation of the next regulatory reviews

Tim Weller first became eligible to participate in the scheme upon commencement of his employment on 1 July 2006 The principal terms are

- he agreed to acquire, at the start of his contract and at his expense, shares in the company to the value of £250,000 and has invested in 39,000 shares in the company (Investment Shares),
- the company has matched the Investment Shares on a one-for-one basis by making a matching share award in the form of a nil cost option over 39,000 shares in the company (Matched Shares),
- the exercise price payable under the option shall be zero,
- in normal circumstances, the option will be capable of being exercised by Tim Weller at the end of a five-year period commencing from the date he joined the company provided that
  - a) he has maintained throughout this period a shareholding in the company of at least the number of Investment Shares, and
  - b) he remains an employee within the group for the whole of the five-year period,
- the number of shares subject to the matching share award will be increased by the notional reinvestment of dividends payable on the Matched Shares over the course of the five-year period,
- in the event that Tim Weller ceases to be an employee because of ill health, death or any reason at the discretion of the trustee, at any time during this five-year period, or he is dismissed without cause during years four and five, the number of shares over which his matching share award (including those notionally added by way of dividend reinvestment as mentioned above) may be exercised will be reduced on the basis of a time pro-rating depending on how much of the five-year period has elapsed as at the date of such cessation of employment As the arrangement has been introduced in lieu of making a compensatory payment to Tim Weller for losses incurred in leaving his previous employer and as he was required to make an immediate and sustained investment in the company, it was considered inappropriate to impose performance conditions in addition to the other conditions applying to the exercise of the matching share award For the same reasons, if there is a change of control or voluntary winding up of the company in the five-year period, the award may be exercised and there will be no time pro-rating If there is a reconstruction or demerger, the trustee may vary the terms and/or allow the early vesting of the matching share award having due regards to the object and purposes of the award,
- the matching award will be exercisable for a period of six months after the end of the five-year period and will lapse if not exercised by then This period may be extended if Tim Weller is prevented from exercising because of restrictions in place under the model code operated by the company,
- the matching share award will not be capable of assignment and, until it is exercised, Tim Weller will have no right to vote in respect of the shares subject to the matching share award,
- shares transferred pursuant to the exercise of the matching share award will rank pari passu in all respects with the shares in the company already in issue, and in the event of any increase or variation in the share capital of the company, the remuneration committee may recommend such adjustment to the matching share award as it considers reasonable

The provisions under the scheme for Tim Weller which relate to

- the person to whom the matching share award may be made,
- the limits on the number of shares which may be used under the scheme,
- the maximum entitlement of Tim Weller,
- the basis for determining Tim Weller's entitlement to the matching share award or shares pursuant to it, and
- the basis for determining the adjustment of the matching share award granted under the scheme following any increase or variation in the share capital of the company

cannot be amended to the advantage of Tim Weller without the prior approval of the shareholders in a general meeting (except for minor amendments to benefit the administration of the long-term incentive scheme, to take into account any change in legislation or to obtain or maintain favourable tax, exchange control or regulatory treatment for Tim Weller or the company or members of its group)

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The benefits to Tim Weller under the scheme are not pensionable The company believes that this arrangement and particularly the time period it relates to, which extends beyond the implementation of the next regulatory reviews, is a forceful alignment of interests between Tim Weller and shareholders The matched award of 39,000 shares was made to Tim Weller on 14 February 2007 Details of his scheme interest are shown in table 30

Table 30 Tim Weller's continuing scheme interests in the matched share investment scheme (audited information)

			Award details		Contingent scheme interest at 1 April 2006		Contingent scheme interest awarded during the year		**Contingent scheme interest at 31 March 2007**	
Award date	Retention period	Market price of a share at award pence	No of shares	Value £000	No of shares	Value £000	No of shares	Value £000	**No of shares**	**Value £'000**
14 2 07	1 7 06 to 30 6 11	772 5	39,000	301 3	–	–	41,484	318 8	**41,484**	**313 4**

Notes.

- The market price of a share at award is the mid market price of a share at close of business on the award date
- The contingent scheme interest awarded during the year comprises the initial award of 39 000 shares and 2 484 shares added in respect of notional dividends payable on the shares during the year
- The value of contingent scheme interest awarded during the year is the value of the initial award plus the value of notional dividends payable during the year
- The value of the contingent scheme interest at 31 March 2007 has been calculated using the mid-market price of a share of 755 5 pence at close of business on 30 March 2007

Special long-term incentive scheme for Charlie Cornish

In order to facilitate his retention up to and beyond the next regulatory reviews, a special long-term incentive scheme has been introduced for Charlie Cornish He is the sole participant Under the scheme an award equal in value to his annual salary was granted to Charlie Cornish on 16 March 2007 The award is in the form of an option over 47,027 shares

The principal terms are

- the exercise price payable under the option shall be zero,
- in normal circumstances, the option will be capable of being exercised by Charlie Cornish at the end of a four-year performance period from 1 April 2006 to 31 March 2010 provided that he remains an employee within the group for the whole of the four-year period,
- the number of shares subject to the award will be increased by the notional reinvestment of dividends payable on them during and until the date that the award vests after the end of the four-year performance period,
- the number of shares over which the option may be exercised will depend upon the extent to which the performance conditions attached to the award have been satisfied over the four-year performance period,
- the performance conditions are the same as those set out for the operational performance conditions for the 2007 award under the proposed matching share award plan disclosed in this report, including the facility to waive, vary or replace any or all of the targets and/or measures if an event occurs which causes the remuneration committee reasonably to consider that the targets and/or measures are no longer appropriate,
- in the event that Charlie Cornish ceases to be an employee because of death, ill health or redundancy or for any reason at the discretion of the trustee, at any time during the performance period, the award may be exercised at the trustee's discretion and the number of shares over which the award may be exercised will depend upon the extent to which the trustee determines the performance conditions (amended or otherwise) have been achieved and the number of shares may also be reduced on a time pro-rating basis If there is a change of control or voluntary winding up of the company the award may be exercised over such number of shares determined by reference to the extent to which the performance conditions have been satisfied and any time pro-rating reduction which may be applied If there is a reconstruction or demerger, the trustee may vary the terms and/or allow the early vesting of the award having due regard to the object and purposes of the award,
- the award will be exercisable for a period of six months after the issue of a certificate by the company specifying the extent to which the performance conditions have been met following the end of the performance period and will lapse if not exercised by then This period may be extended if Charlie Cornish is prevented from exercising because of restrictions in place under the model code operated by the company The company shall arrange for such certificate to be issued within nine months after the end of the performance period,
- the award is not capable of assignment and, until it is exercised, Charlie Cornish will have no right to vote in respect of the shares subject to the award,
- shares transferred pursuant to the exercise of the award will rank pari passu in all respects with the shares in the company already in issue, and in the event of any increase or variation in the share capital of the company, the remuneration committee may recommend such adjustment to the award as it considers reasonable

The provisions under the scheme for Charlie Cornish which relate to

- the person to whom the award may be made,
- the limits on the number of shares which may be used under the scheme,
- the maximum entitlement of Charlie Cornish,
- the basis for determining Charlie Cornish's entitlement to the award or shares pursuant to it, and
- the basis for determining the adjustment of the award granted under the scheme following any increase or variation in the share capital of the company cannot be amended to the advantage of Charlie Cornish without the prior approval of the shareholders in general meeting (except for minor amendments to benefit the administration of the long-term incentive scheme, to take into account any change in legislation or to obtain or maintain favourable tax, exchange control or regulatory treatment for Charlie Cornish or the company or members of its group) The benefits to Charlie Cornish under the scheme are not pensionable Details of Charlie Cornish's scheme interest are shown in table 31

Table 31 Charlie Cornish's continuing scheme interests in his special long-term incentive scheme (audited information)

			Award details		Contingent scheme interest at 1 April 2006		Contingent scheme interest awarded during the year		**Contingent scheme interest at 31 March 2007**	
Award date	Performance period	Market price of a share at award pence	No of shares	Value £000	No of shares	Value £000	No of shares	Value £000	**No of shares**	**Value £'000**
16.3.07	1.4.06 to 31.3.10	723.0	47,027	340.0	–	–	50,022	361.1	**50,022**	**377.9**

Notes

- The market price of a share at award is the mid-market price of a share at close of business on the day before the award date.
- The contingent scheme interest awarded during the year comprises the initial award of 47,027 shares and 2,995 shares added in respect of notional dividends payable on the shares during the year.
- The value of contingent scheme interest awarded during the year is the value of the initial award plus the value of notional dividends payable during the year.
- The value of the contingent scheme interest at 31 March 2007 has been calculated using the mid market price of a share of 755.5 pence at close of business on 30 March 2007.

Pension arrangements

Several pension schemes operate within the group. The group, with trustee agreement where required, has made the rule changes necessary to ensure that the schemes qualify as registered pension schemes under the new legislative regime. The executive directors are all members of the United Utilities Pension Scheme (UUPS).

The remuneration committee recognises that pension is an important but potentially costly element of remuneration. Decisions have previously been made to close entry to the defined benefit section of UUPS to newly recruited directors and other senior executives, not to introduce any new unfunded unapproved arrangements to provide pension benefits above those approved by HM Revenue & Customs and to close entry to the defined benefit executive section (which provides enhanced benefits for existing scheme members).

Newly recruited executive directors may join the defined contribution section of UUPS. They may make a regular contribution of up to seven per cent of basic pay and may make additional voluntary contributions. The company contributes up to 25 per cent of basic pay.

When scheme members reach the lifetime allowance they are given the choice of continuing to accrue benefits within the pension scheme (and pay the higher tax charge for which no compensation will be paid) or be paid a cash allowance instead of accruing further pension benefits. The cash allowances are calculated as a percentage of salary and do not exceed the cost of the company's pension contributions. A cash allowance of 12 per cent is payable in lieu of the standard defined contribution rate of 14 per cent, 22 per cent in lieu of the enhanced defined contribution rate of 25 per cent and 25 per cent in lieu of the company's contribution for members in the defined benefit section of the pension scheme. As at 31 March 2007, no executive had taken the cash alternative.

Directors' regular contribution rates are levied on their pensionable pay, provided the amount for the year, when added to the company's contribution, does not exceed the annual allowance.

During the year the company made available to all members of the company's pension schemes, the opportunity to participate in a 'salary sacrifice' arrangement. The arrangement allows pension scheme members to cease making their regular pension contributions. Their gross salary is correspondingly reduced by the value of the regular contributions they would have made to the pension scheme. For members of the defined contribution section, the company makes an additional contribution equal to the regular contribution that would have been paid by the member. The arrangement does not affect accrued or the future accrual of benefits for members of defined benefit plans.

Directors' pension arrangements

Philip Green, Charlie Cornish and Tim Weller are members of the defined contribution section. Prior to participating in the salary sacrifice arrangement, Philip Green's regular contribution rate was three per cent of basic salary. The company contributed six per cent of basic salary to the pension scheme and an additional 19 per cent to his private pension plan. Charlie Cornish and Tim Weller contributed seven per cent and the company 25 per cent of their basic salary to the pension scheme. The normal pension age is 65.

Simon Batey's, Tom Drury's and Gordon Waters' pension arrangements fell within the defined benefit section which is now closed to new executives. The scheme provides a pension for them on normal retirement at age 60 based on a maximum accrual rate of 1/30th of pensionable earnings for each completed year of service. The maximum pension is two thirds of pensionable earnings. Early retirement is possible from age 50 if the company agrees. In the event of early retirement, pension benefits are actuarially reduced. The regular contribution rate to the scheme for Simon Batey was five per cent and for Tom Drury and Gordon Waters six per cent of their pensionable pay. Simon Batey, Tom Drury and Gordon Waters participated in the company's salary sacrifice scheme. They, therefore, all ceased making regular contributions to the pension scheme.

Pension benefits are calculated on basic salary only. Tom Drury and Gordon Waters previously had a contractual entitlement to a pensionable bonus. Their bonus is no longer pensionable. To partially offset the reduction in their pensionable pay calculation, their pension benefits are based on notional pensionable pay of 1.225 and 1.3 times their basic pay respectively.

Employer funded retirement benefit scheme (EFRBS)

Arising from previous policy, the company had in place unfunded unapproved arrangements (now known as employer funded retirement benefit schemes) for Simon Batey, Tom Drury and Gordon Waters (and a limited number of other senior executives), the intention of which was to provide pension benefits calculated on the same basis as for executives whose pensionable earnings were not limited by the former earnings cap.

The committee decided to offer to deferred pensioners and those in receipt of pension benefits the option to transfer within three months from 6 April 2006 part or all of their unfunded arrangement to the registered pension scheme. Those in receipt of pension benefits were also offered until 6 July 2006 the facility to exchange their ongoing unfunded benefits for a cash lump sum. During the year this offer was extended to current executives and deferred members with EFRBS arrangements.

Current executives with unfunded arrangements (all of whom were members of the defined benefit section of UUPS) were given the choice of transferring the value of part or all of their accrued unfunded benefit into the registered pension scheme or to retain it under the EFRBS or to exchange it for a cash lump sum They were also given the choice of whether all future pension accrual should be within the registered scheme, or whether any benefits generated in excess of the lifetime allowance should accrue under EFRBS

At 31 March 2007, there were eight EFRBS arrangements in place One related to a current executive, two to deferred pensioners and five to pension benefits in payment Further information on payments made during the year and the total cost of the unfunded arrangements is given in note 19 to the accounts

Directors' accrued pension benefits

The pension benefits earned during the year by directors who were members of the defined benefit section of the pensions scheme are shown in table 32

During the year ended 31 March 2007, the company paid contributions totalling £182,349 (2005/06 £nil) to the defined contribution section of the pension scheme and to a personal pension plan for Philip Green in respect of 2006/07 Contributions totalling £96,900 (2005/06 £56,875) for Charlie Cornish and £85,073 (2005/06 £nil) for Tim Weller were made to the defined contribution section of the pension scheme These figures include amounts of £12,163, £11,900 and £16,333 respectively for Philip Green, Charlie Cornish and Tim Weller in substitution for their regular pension scheme contributions and for which there was a corresponding reduction in the amounts shown as their gross salaries in table 16 In addition, contributions totalling £24,442 were made in respect of 2005/06 for the period of Philip Green's employment during that year

Contracts of service and compensation for termination

The company's policy is that the executive directors normally have one-year notice periods The company may offer a longer notice period if it considers that necessary to recruit a new director If it offers an initial notice period of more than one year, it will usually reduce that to a rolling one-year notice period after the initial period has expired At 31 March 2007, all current executive directors had one-year notice periods

Contracts terminate automatically upon the director reaching age 65 unless the company agrees that a director may continue to work after attaining that age No special arrangements apply if there is a change of control

As at 31 March 2007, service contracts did not provide explicitly for termination payments (other than for holidays due but not taken), liquidated damages or payments in lieu of notice If a contract is to be terminated, the remuneration committee will, in each circumstance, determine the compensation that will be paid, normally by reference to fixed elements of remuneration and the notice period There is no automatic entitlement to payments under the annual bonus or performance share plan Any annual bonus payment is at the discretion of the company Performance share plan vesting is at the discretion of the trustees based on a recommendation from the remuneration committee and an award will not normally vest unless the termination is for a 'good leaver' reason such as retirement or because of ill health, or there are other special circumstances Payments are then pro-rated and subject to the performance conditions on which awards were granted (modified if appropriate) being satisfied

The committee will apply such mitigation it considers is fair and reasonable It will take into account the best practice provisions of the Combined Code and will take legal advice on the company's liability to pay compensation Its policy is to take a robust line on reducing compensation It may phase payments to reflect a departing employee's obligation to mitigate loss The committee reviews this policy each year No changes were made during the year However, after the end of the year, the committee reviewed its policy on compensation for termination and introduced a liquidated damages provision for future contracts

Simon Batey left the company on 31 July 2006 Details of his leaving arrangements were disclosed in the 2006 remuneration report, except for the benefit arising from calculating his pension

Table 32 Executive directors' pension benefits (defined benefit scheme) (audited information)

	Accumulated total accrued pension at 1 April 2006		Pension accrued during the year				**Accumulated total accrued pension at 31 March 2007**	
	£ 000 p a	Transfer value £ 000	Increase net of inflation(1) £ 000 p a	Directors contributions £ 000	Transfer value of net increase(2) £ 000	Total change in transfer value(3) £ 000	**£ 000 p a.**	**Transfer value £'000**
Simon Batey	72 2	1 161 4	11 7	15 5	176 8	211 2	**84 6**	**1,388 1**
Tom Drury	123 3	1,524 3	7 4	23 2	67 9	135 4	**136 1**	**1,682 9**
Gordon Waters	132 4	2,651 0	12 7	18 4	240 5	381 7	**149 1**	**3,051 1**

Notes.

- Pension accruals shown are the amounts that would be paid annually on retirement based on service to the end of the year or date of leaving employment or death if earlier
- Transfer values have been calculated in accordance with version 8 1 of guidance note GN11 issued by the actuarial profession
- The transfer value of the net increase in pension (2) represents the incremental value to the director of his service during the year, calculated on the assumption that service terminated at the year end or at the date of leaving employment or death if earlier It is based on the accrued pension increase net of inflation (1) and is calculated after deducting the director's contribution and/or salary sacrifice
- The total change in the transfer value (3) includes the effect of fluctuations in the transfer value due to factors beyond the control of the company and directors such as stock market movements It is calculated after deducting the director's contribution
- The transfer value represents a liability of the company to make pension payments in the future but not a sum paid to the individual
- Simon Batey left the company on 31 July 2006 The increase in his accrued pension net of inflation of £11,716 a year includes £6,673 a year in respect of an augmentation to his deferred pension granted by the company as part of the compensation for his loss of office The transfer value of the net increase in pension accrued of £176 843 includes the value of the augmentation of £109 530
- Simon Batey Tom Drury and Gordon Waters participated in the company's 'salary sacrifice scheme Instead of making member contributions to the pension scheme their gross salaries disclosed in table 16 were reduced by the respective amounts shown as directors contributions in table 32 These amounts are equivalent to what would have been their member contributions based on their pensionable pay
- Voluntary contributions paid by directors and resulting benefits are not shown
- Gordon Waters died on 24 December 2006

on service to 31 January 2007 i e as if he had worked for the company until the end of his notice period This information (which was not available at the time of last year's report) is included in the notes to table 32 on page 67

Tom Drury was the managing director of Vertex Data Science Limited He left the group on 31 March 2007 following the disposal of that company After mitigation, he received a payment of £329,712 as compensation for loss of office No allowance was made for loss of pension benefit accrual or loss of other benefits Details of directors' contracts as at 31 March 2007 are set out in table 33

Table 33 Executive directors' service contracts as at 31 March 2007

	Date of contract	Unexpired term (to 65th birthday)	Notice period
Philip Green	13 02 06	12 05 18	12 months (rolling)
Tim Weller	01 07 06	08 06 28	12 months (rolling)
Charlie Cornish	05 01 04	30 11 24	12 months (rolling)
Tom Drury	09 05 05	–	12 months (rolling)

Notes

- Tom Drury left the company on 31 March 2007
- No explicit contractual compensation for early termination (other than payment for outstanding holidays)

Paul Capell joined the company and was appointed to the board on 1 May 2007 His salary is £350,000 a year As at the date of this report, he was not a member of the pension scheme His contract has an unexpired term to 20 January 2022 (his 65th birthday) and provides for an initial notice period of 24 months, reducing to 12 months (rolling) after one year's service The contract contains a liquidated damages provision whereby if it is terminated other than for specified causes related to misconduct or capability, the company will make an initial lump sum payment equivalent to one half of his notice entitlement in relation to his basic salary, employer pension contribution and car allowance payable under his contract In addition he will receive further payments by instalments which in total will equate to the remaining half of his notice entitlement in relation to his basic salary, employer pension contribution and car allowance The instalments will be made monthly beginning seven months from the date of termination of his employment and ceasing on the first anniversary of his termination date The amount of the monthly payment will be reduced by the value of any salary, pension contribution and car allowance earned by him in new paid employment in that month

Non-executive directorships

The company recognises that its executive directors may be invited to become non-executive directors of companies outside the group and exposure to such non-executive duties can broaden experience and knowledge, which will be to the benefit of the company Subject to board approval (which will not be given if the proposed appointment is with a competing company, would otherwise lead to a conflict of interest or could have a detrimental effect on a director's performance), executive directors are allowed to accept one non-executive directorship and to retain the fee Simon Batey served as a non-executive director of Arriva plc, for which he earned and retained a fee of £13,333 from the start of the year up to his resignation on 31 July 2006 Simon Batey also represented the group as a non-executive director of THUS Group plc due to the group's investment in this company This directorship was unpaid On 17 November 2006, Tim Weller resigned from his non-executive directorship of Stanley Leisure plc From the date of his appointment to the board of United Utilities PLC to the date of his resignation Mr Weller earned and retained £10,333 in respect of this directorship Philip Green was appointed as a non-executive director of Lloyds TSB Bank plc on 10 May 2007

Employee share schemes

The board believes that share ownership is an effective way of strengthening employees' involvement in the development of the business and bringing together their interests and those of shareholders It offers employees the opportunity to build up a shareholding in the group

The main all-employee scheme is the Inland Revenue approved share incentive plan, 'ShareBuy' This is a flexible way for employees to acquire shares in the company by buying 'partnership' shares up to the lower of £1,500 or ten per cent of taxable pay each year The funds are deducted from pre-tax pay and passed to an independent trustee who makes a monthly purchase of shares at full market price Employees can reinvest the dividends on partnership shares to buy more shares under the plan In 2004, the company introduced 'matching' shares It gives one free share for every five partnership shares bought The shares need to be held in trust for a five-year term in order to retain the maximum tax advantages

Grants have also been made to employees through the SAYE share option savings scheme, 'ShareSave', whereby an employee is granted an option to buy shares at the end of a three or five-year term during which they can save up to £250 each month from their net pay The option price is fixed at a price not lower than 20 per cent below the market price at the date of grant The number of shares that can be bought is determined by the amount saved by the employee over the term In addition to the executive directors, a limited number of senior executives also have the opportunity to acquire shares by participating in the group's performance share plan This plan has replaced the grant of executive share options Further information on the operation of the group's share schemes can be found in note 26 to the accounts on page 114

Approved by the board of directors on 4 June 2007 and signed on its behalf by

David Jones
Remuneration committee chairman

Independent auditors' report

Independent auditors' report to the members of United Utilities PLC

We have audited the group and parent company financial statements (the 'financial statements') of United Utilities PLC for the year ended 31 March 2007 which comprise the consolidated income statement, the consolidated and parent company balance sheets, the consolidated and parent company cashflow statements, the consolidated and parent company statements of recognised income and expense, statement of accounting policies and the related notes 1 to 30 These financial statements have been prepared under the accounting policies set out therein We have also audited the information in the directors' remuneration report that is described as having been audited

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985 Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report, the directors' remuneration report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the statement of directors' responsibilities

Our responsibility is to audit the financial statements and the part of the directors' remuneration report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland)

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985 and, as regards the group financial statements, Article 4 of the IAS Regulation We also report to you whether in our opinion the information given in the directors' report is consistent with the financial statements

The information given in the directors' report includes the information supplied in the chairman's and chief executive officer's reviews and the business review as cross-referenced from the business review section of the directors' report

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

We review whether the corporate governance statement reflects the company's compliance with the nine provisions of the 2003 Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the group's corporate governance procedures or its risk and control procedures

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

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the directors' remuneration report to be audited 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 group's and company's circumstances, consistently applied and adequately disclosed

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the directors' remuneration report to be audited 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 and the part of the directors' remuneration report to be audited

Opinion

In our opinion

- the group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the group's affairs as at 31 March 2007 and of its profit for the year then ended,
- the parent company financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union as applied in accordance with the provisions of the Companies Act 1985, of the state of the parent company's affairs as at 31 March 2007,
- the financial statements and the part of the directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985 and, as regards the group financial statements, Article 4 of the IAS Regulation, and
- the information given in the directors' report is consistent with the financial statements

Deloitte & Touche LLP

Deloitte & Touche LLP
Chartered Accountants and Registered Auditors
Manchester, England

4 June 2007

Consolidated income statement

for the year ended 31 March

Continuing operations	Note	2007 £m	2006 £m
Revenue	1	**2,323 0**	2,086 0
Other income		**22.2**	21 1
Employee benefits expense	2	**(280 3)**	(257 3)
Depreciation and amortisation expense	3	**(288 5)**	(282 8)
Infrastructure renewals expenditure		**(101 2)**	(70 6)
Other operating costs		**(847 7)**	(766 9)
Total operating expenses		**(1,495 5)**	(1,356 5)
Operating profit	1, 3	**827 5**	729 5
Investment income	4	**138 2**	68 5
Finance expense	5	**(308 4)**	(352 9)
Investment income and finance expense		**(170 2)**	(284 4)
Share of results of associated company	13	**18 7**	-
Profit before taxation		**676 0**	445 1
Taxation	6	**(175 3)**	(122 0)
Profit for the year from continuing operations		**500 7**	323 1
Discontinued operations			
Loss for the period from discontinued operations	7	**(67 2)**	(114 9)
Profit for the year		**433 5**	208 2
Attributable to			
Equity holders of the company		**433 5**	207 9
Minority interest		**-**	0 3
		433 5	208 2
Earnings per share	9		
From continuing and discontinued operations			
Basic		**49 4p**	24 3p
Diluted		**49 2p**	24 2p
From continuing operations			
Basic		**57 1p**	37 8p
Diluted		**56 9p**	37 6p

The results of the group's business process outsourcing business, Vertex, have been disclosed within discontinued operations in 2007 (see note 7) Corresponding amounts for 2006 have been re-presented accordingly

Operating profit and investment income for 2006 have been re-presented, as the group has changed its presentation of interest income and expenditure associated with its defined benefit pension schemes (see note 4)

Balance sheets

at 31 March

	Note	Group		Company	
		2007 £m	2006 £m	2007 £m	2006 £m
ASSETS					
Non-current assets					
Property, plant and equipment	10	**8,894 6**	8,543 9	**0 6**	0 8
Goodwill	11	**5 0**	153 1	**–**	–
Other intangible assets	12	**115 5**	236 2	**–**	–
Investments	13	**201 8**	170 7	**5,268 3**	5,501 7
Trade and other receivables	15	**21 6**	22 0	**–**	–
Retirement benefit surplus	19	**62 2**	19 3	**10 1**	–
Deferred tax asset	20	**–**	–	**7 3**	7 4
Derivative financial instruments	18	**15 2**	40 8	**–**	–
		9,315 9	9,186 0	**5,286 3**	5,509 9
Current assets					
Inventories	14	**24 3**	28 2	**–**	–
Trade and other receivables	15	**418 2**	490 1	**993 6**	1,130 6
Investments	13	**38 5**	29 7	**–**	–
Cash and short-term deposits	16	**2,403 3**	1,513 5	**336 7**	120 4
Derivative financial instruments	18	**61 0**	48 9	**18 8**	–
		2,945 3	2,110 4	**1,349 1**	1,251 0
Total assets		**12,261 2**	11,296 4	**6,635 4**	6,760 9
LIABILITIES					
Non-current liabilities					
Trade and other payables	22	**(414.3)**	(383 7)	**–**	–
Borrowings	17	**(4,854 9)**	(5,081 1)	**(765 2)**	(880 9)
Retirement benefit obligations	19	**–**	–	**–**	(1 2)
Deferred tax liabilities	20	**(1,550 8)**	(1,426 6)	**–**	–
Provisions	21	**(30 4)**	(16 6)	**(12 5)**	–
Derivative financial instruments	18	**(173 5)**	(57 6)	**(100 1)**	(32 7)
		(7,023 9)	(6,965 6)	**(877 8)**	(914 8)
Current liabilities					
Trade and other payables	22	**(749 2)**	(855 1)	**(502 5)**	(550 8)
Borrowings	17	**(1,509 5)**	(619 1)	**(928 0)**	(478 2)
Current income tax liabilities		**(168 0)**	(112 8)	**–**	–
Provisions	21	**(8 5)**	(36 5)	**(2 0)**	–
Derivative financial instruments	18	**(67 3)**	(76 4)	**(7 3)**	(5 8)
		(2,502 5)	(1,699 9)	**(1,439 8)**	(1,034 8)
Total liabilities		**(9,526 4)**	(8,665 5)	**(2,317 6)**	(1,949 6)
Total net assets		**2,734 8**	2,630 9	**4,317 8**	4,811 3
EQUITY					
Capital and reserves attributable to equity holders of the company					
Share capital	23	**879 8**	875 4	**879 8**	875 4
Share premium account	23	**1,421 9**	1,407 8	**1,421 9**	1,407 8
Revaluation reserve	23	**158 8**	158 8	**–**	–
Treasury shares	23	**(0 3)**	(0 3)	**(0 3)**	(0 3)
Cumulative exchange reserve	23	**(4 2)**	2 2	**(1 7)**	5 2
Retained earnings	23	**278 8**	185 3	**2,018.1**	2,523 2
Shareholders' equity		**2,734 8**	2,629 2	**4,317.8**	4,811 3
Minority interest		**–**	1 7	–	–
Total equity		**2,734 8**	2,630 9	**4,317 8**	4,811 3

Approved by the board of directors on 4 June 2007 and signed on its behalf by

Sir Richard Evans
Chairman

Tim Weller
Chief financial officer

Statements of recognised income and expense

for the year ended 31 March

		Group		Company	
	Note	2007 £m	2006 £m	2007 £m	2006 £m
Actuarial gains/(losses) on defined benefit pension schemes	19, 23	**46 5**	119 2	**(21 4)**	5 2
Revaluation of investments	13, 23	**8 9**	14 6	**-**	-
Fair value gain/(loss) on cashflow hedges	23	**2 8**	(0 9)	**-**	-
Foreign exchange adjustments	23	**(6 4)**	(1 5)	**(6 9)**	4 1
Tax on items taken directly to equity	23	**(14.8)**	(35 6)	**6 4**	(1 6)
Net income/(expense) recognised directly in equity		**37 0**	95 8	**(21 9)**	7 7
Profit/(loss) for the year		**433.5**	208 2	**(106 7)**	315 0
Total recognised income and expense for the year		**470.5**	304 0	**(128 6)**	322 7

Attributable to			
Equity holders of the company		**470.5**	303 7
Minority interest		**-**	0 3
		470 5	304 0

Cashflow statements

for the year ended 31 March

	Note	Group 2007 £m	Group 2006 £m	Company 2007 £m	Company 2006 £m
Operating activities					
Cash generated from/(used in) operations	28	**1,035 8**	997 2	**62 2**	(25 3)
Interest paid		**(385 3)**	(345 0)	**(81 2)**	(66 5)
Interest received and similar income		**111 6**	66 2	**13 6**	12 5
Tax paid		**(35 2)**	(2 5)	**(30 6)**	–
Net cash generated from/(used in) operating activities (continuing operations)		**726 9**	715 9	**(36 0)**	(79 3)
Net cash generated from/(used in) operating activities (discontinued operations)	28	**28 4**	(4 5)	**–**	–
		755 3	711 4	**(36 0)**	(79 3)
Investing activities					
Acquisition of subsidiaries (net of cash and cash equivalents acquired)	24	**–**	–	**–**	(25 3)
Financial restructuring of subsidiaries		**–**	–	**–**	(559 0)
Disposal of subsidiaries	7, 28	**206 4**	–	**227 6**	–
Purchase of investments		**–**	(85 3)	**–**	–
Purchase of property, plant and equipment		**(659 3)**	(598 1)	**–**	–
Purchase of other intangible assets		**(5 9)**	(31 6)	**–**	–
Proceeds from sale of property, plant and equipment		**34 3**	29 1	**–**	–
Financial restructuring of joint ventures		**–**	13 2	**–**	–
Net cash (used in)/generated from investing activities (continuing operations)		**(424 5)**	(672 7)	**227 6**	(584 3)
Net cash used in investing activities (discontinued operations)		**(20 7)**	(106 5)	**–**	–
		(445 2)	(779 2)	**227 6**	(584 3)
Financing activities					
Proceeds from issue of ordinary shares	23	**18 5**	528 3	**18 5**	528 3
Proceeds from structured financing		**81 4**	–	**–**	–
Proceeds from borrowings		**1,700 8**	943 8	**629 9**	458 6
Repayment of borrowings		**(825 4)**	(472 6)	**(236 4)**	(212 1)
Dividends paid to equity holders of the company		**(387 3)**	(344 7)	**(387 3)**	(344 7)
Net cash generated from financing activities (continuing operations)		**588 0**	654 8	**24 7**	430 1
Net cash used in financing activities (discontinued operations)		**(7 7)**	(0 7)	**–**	–
		580 3	654 1	**24 7**	430 1
Effects of exchange rate changes (continuing operations)		**6 4**	(8 0)	**–**	–
Net increase/(decrease) in cash and cash equivalents (continuing operations)		**896 8**	690 0	**216 3**	(233 5)
Net decrease in cash and cash equivalents (discontinued operations)		**–**	(111 7)	**–**	–
Cash and cash equivalents at beginning of the year	16	**1,443 9**	865 6	**120 4**	353 9
Cash and cash equivalents at end of the year	16	**2,340 7**	1,443 9	**336 7**	120 4

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

a) Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted for use in the European Union (EU), including International Accounting Standards (IAS) and Interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC)

The financial statements have been prepared on the historical cost basis, except for the revaluation of financial instruments

The preparation of financial statements, in conformity with generally accepted accounting principles (GAAP) under IFRS, requires management to make estimates and assumptions that affect the amounts of assets and liabilities at the date of the financial statements and the amounts of revenues and expenses during the reporting period Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from these estimates

b) Basis of consolidation

The group financial statements consolidate the financial statements of the company and entities controlled by the company (its subsidiaries), made up to 31 March each year, and incorporate the results of its share of jointly controlled entities using proportionate consolidation

The results of subsidiaries and joint ventures acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate

Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used under the relevant local GAAP into line with those used by the group

Subsidiaries

Control is achieved where the company has the power to govern the financial and operating policies, generally accompanied by a shareholding of more than one half of the voting rights, of an investee entity so as to obtain benefits from its activities

On acquisition, the assets and liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill Any deficiency of the cost of acquisition below the fair values of the identifiable net assets acquired is credited to the income statement in the period of acquisition The interest of minority shareholders is stated at the minority's proportion of the fair values of the assets and liabilities recognised Minority interests in the net assets of consolidated subsidiaries are identified separately from the group's equity therein Minority interests consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses

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

Associates

An associate is an entity over which the group, either directly or indirectly, is in a position to exercise significant influence by participating in, but not controlling, the financial and operating policies of the entity Associates are accounted for using the equity method Losses of an associate in excess of the group's interest in the associate are not recognised, except to the extent that the group has incurred obligations in respect of the associate Unrealised profits and losses recognised by the group on transactions with an associate are eliminated to the extent of the group's interest in the associate concerned

Joint ventures

Joint ventures are entities in which the group holds an interest on a long-term basis and which are jointly controlled with one or more parties under a contractual arrangement The group's share of joint venture income, expenses, assets, liabilities and cashflows are included in the consolidated financial statements on a proportionate consolidation basis using the same accounting methods as adopted for subsidiaries

c) Non-current assets held for sale

Non-current assets (and disposal groups) classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition Management must be committed to the sale which should be expected to qualify for recognition as a completed sale within one year from the date of classification

d) Intangible assets

Goodwill

Goodwill arising on consolidation is recognised as an asset

Following initial recognition, goodwill is subject to impairment reviews, at least annually, and measured at initial value less accumulated impairment losses Any impairment is recognised immediately in the income statement and is not subsequently reversed

On disposal of a subsidiary, or jointly controlled entity, the attributable amount of goodwill is included in the determination of the gain or loss on disposal

Goodwill written off to reserves under UK GAAP prior to 1998 has not been reinstated and is not included in determining any subsequent profit or loss on disposal

Other intangible assets

Other intangible assets are measured initially at cost and are amortised on a straight-line basis over their estimated useful lives Carrying amount is reduced by any provision for impairment where necessary

On a business combination, as well as recording separable intangible assets already recognised in the balance sheet of the acquired entity at their fair value, identifiable intangible assets that arise from contractual or other legal rights are also included in the acquisition balance sheet at fair value

Amortisation periods for categories of intangible assets are

Computer software 3-10 years
Other intangible assets 2-20 years

e) Property, plant and equipment
Property, plant and equipment comprises infrastructure assets (mains, sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls) and other assets (including properties, overground plant and equipment and electricity operational assets)

Water and wastewater infrastructure assets
Infrastructure assets comprise a network of water and wastewater systems Expenditure on the infrastructure assets relating to increases in capacity or enhancements of the network are treated as additions Amounts incurred in maintaining the operating capability of the network in accordance with defined standards of service are expensed in the year in which the expenditure is incurred Infrastructure assets are depreciated by writing off their deemed cost, less the estimated residual value, evenly over their useful lives, which range from 15 to 300 years

Employee costs incurred in implementing the capital schemes of the group are capitalised within infrastructure assets

Other assets
All other property, plant and equipment is stated at historical cost less accumulated depreciation

Historical cost includes expenditure that is directly attributable to the acquisition of the items Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred

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

Buildings 30-60 years
Operational assets 5-80 years
Fixtures, fittings, tools and equipment 3-40 years

Depreciation methods, residual values and useful lives are reassessed annually and, if necessary, changes are accounted for prospectively

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

f) Impairment of tangible and intangible assets excluding goodwill
Intangible assets with definite useful lives and property, plant and equipment are reviewed for impairment at each reporting date to determine whether there is any indication that those assets may have suffered an impairment loss If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any Where the asset does not generate cashflows that are independent from other assets, the group estimates the recoverable amount of the cash generating unit to which the asset belongs

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

If the recoverable amount of an asset (or cash generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash generating unit) is reduced to its recoverable amount Impairment losses in respect of non-current assets are recognised in the income statement within operating costs

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

g) Financial instruments
Financial assets and financial liabilities are recognised on the group's balance sheet when the group becomes a party to the contractual provisions of the instrument

Cash and short-term deposits
Cash and short-term deposits include cash at bank and in hand, deposits and other short-term highly liquid investments which are readily convertible into known amounts of cash, have a short maturity of three months or less from the date of acquisition and which are subject to an insignificant risk of change in value In the consolidated cashflow statement and related notes, cash and cash equivalents include cash and short-term deposits and bank overdrafts

Financial investments
Investments (other than interests in associates, subsidiaries, joint ventures and fixed deposits) are recognised and derecognised on a trade date and are initially measured at fair value, including transaction costs Investments are classified as available-for-sale and are measured at subsequent reporting dates at fair value Gains and losses arising from changes in fair value are recognised directly in equity, until the security is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is included in the net profit or loss for the period

Trade receivables
Trade receivables are stated at nominal value less allowances for estimated irrecoverable amounts

Trade payables
Trade payables are stated at their nominal value

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

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

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

Derivative financial instruments and hedge accounting
Interest rate swap agreements and financial futures are used to manage interest rate exposure, while the group enters into cross-currency swaps to manage its exposure to fluctuations in foreign exchange rates The group does not use derivative financial instruments for speculative purposes

All financial derivatives are recognised in the balance sheet at fair value Changes in the fair value of all derivative financial instruments are recognised in the income statement within finance expense as they arise, except for derivatives that are designated and effective in terms of cashflow hedging relationships, in which case the gains and losses are deferred in equity

Where hedge accounting has not been applied, the group may elect to designate a financial liability at inception as fair value through profit or loss provided the financial liability meets the conditions specified in IAS 39 'Financial Instruments Recognition and Measurement' Where possible, hedge accounting is applied

Fair value hedges
For an effective hedge of an exposure to changes in the fair value, the hedged item is adjusted for changes in fair value attributable to the risk being hedged with the corresponding entry in profit or loss Gains or losses from remeasuring the derivative are recognised in profit or loss

Where changes in the fair value of a derivative differ from changes in the fair value of the hedged item attributable to the risks being hedged, the hedge ineffectiveness is recorded in the income statement within finance costs

Hedge accounting is discontinued prospectively when the hedging instrument is sold, terminated or exercised, where the hedge relationship no longer meets the criteria for hedge accounting in accordance with IFRS, or where the hedge designation is revoked Any adjustment that has been recognised to the hedged item, for which the effective interest rate is used, is amortised to the income statement and is based on the recalculated effective interest rate at the time at which amortisation commences

Cashflow hedges
Changes in the fair value of derivative financial instruments that are designated and effective as hedges of future cashflows are recognised directly in equity and the ineffective portion is recognised immediately in the income statement If the cashflow hedge for foreign currency risk of a firm commitment results in the recognition of a non-financial asset or a liability, then, at the time the non-financial asset or liability is recognised, the associated gains or losses on the derivative that had previously been recognised in equity are included in the initial recognition of the non-financial asset or liability For hedges that do not result in the recognition of a non-financial asset or liability, amounts deferred in equity are recognised in the income statement in the same period in which the hedged item affects net profit or loss

Hedge ineffectiveness is recognised directly in the income statement within finance costs

Hedge accounting is discontinued when the hedge designation is revoked, or the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting At that time, any cumulative gain or loss on the hedging instrument recognised in equity is retained in equity until the forecast transaction occurs If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to net profit or loss for the period

Financial assets and liabilities designated at fair value through profit or loss
The group applies this designation where the complexity of the swaps means that they are disallowed from being allocated in a hedge relationship despite there being significant fair value offset between the hedged item and the derivative itself The otherwise inconsistent accounting treatment that would have resulted allows the group to satisfy the criteria for this designation The treatment of financial assets and liabilities designated at fair value through profit and loss is consistent with the group's documented risk management strategy

h) Foreign currency translation
Transactions and balances
Transactions in foreign currencies are recorded at the exchange rates ruling on the dates of the transactions At each balance sheet date, monetary assets and liabilities denominated in foreign currencies are translated into sterling at the relevant rates of exchange ruling on the balance sheet date Gains and losses arising on retranslation are included in net profit or loss for the period Exchange differences arising on investments in equity instruments classified as available for sale are included in the gains or losses arising from changes in fair value which are recognised directly in equity

In order to hedge its exposure to certain foreign exchange risks, the group enters into forward contracts, options and other derivative instruments (see derivative financial instruments and hedge accounting in note g)

Group companies
On consolidation, the balance sheets of overseas subsidiaries and joint ventures (none of which has the currency of a hyperinflationary economy) are translated into sterling at exchange rates applicable at the balance sheet date The income statements are translated into sterling using the average rate unless exchange rates fluctuate significantly in which case the exchange rate at the date the transaction occurred is used Exchange differences resulting from the translation of such balance sheets at rates ruling at the beginning and end of the period, together with the differences between income statements translated at average rates and rates ruling at the period end, are dealt with as movements on the group's cumulative exchange reserve, a separate component of equity Such translation differences are recognised as income or as expenses in the period in which the operation is disposed of

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate The group has elected to treat goodwill and fair value adjustments arising on acquisitions before the date of implementation of IFRS 3 'Business Combinations' (1 April 1999) as sterling denominated assets and liabilities

i) Borrowing costs and finance income
All borrowing costs and finance income are recognised in the income statement in the period in which they are accrued

j) Construction contracts
Where the outcome of a construction contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract activity at the balance sheet date, as measured by the proportion that contract costs incurred for work performed to date bear to the estimated total contract costs, except where this would not be representative of the stage

of completion Variations in contract work, claims and incentive payments are included to the extent that they have been agreed with the customer

Where the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised to the extent of contract costs incurred that it is probable will be recoverable Contract costs are recognised as expenses in the period in which they are incurred

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately

k) Operating profit
Operating profit is stated after charging operating expenses but before investment income and finance expense

l) Current asset investments
Current asset investments are stated at the lower of cost and net realisable value

m) Taxation
The tax expense represents the sum of current tax and deferred tax

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

Taxable profit differs from the net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible

Deferred taxation
Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit Deferred tax liabilities are provided, using the liability method, on all taxable temporary differences at the balance sheet date Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and interests in joint ventures, except where the group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future

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

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer more likely than not that sufficient taxable profits will be available to allow all or part of the asset to be recovered

Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited to equity, in which case the deferred tax is also dealt with within equity

n) Employee benefits
Retirement benefit obligations
The group operates two defined benefit pension schemes, which are independent of the group's finances, for the substantial majority of its employees Actuarial valuations of the schemes are carried out as determined by the pension scheme trustees using the projected unit credit method at intervals of not more than three years, the rates of contribution payable and the pension cost being determined on the advice of the actuaries, having regard to the results of these valuations In any intervening years, the actuaries review the continuing appropriateness of the contribution rates

Defined benefit assets are measured at fair value while liabilities are measured at present value The difference between the two amounts is recognised as a surplus or obligation in the balance sheet

The cost of providing pension benefits to employees relating to the current year's service is included within the income statement within employee costs The difference between the expected return on scheme assets and interest on scheme liabilities is included within the income statement within investment income

All actuarial gains and losses are recognised outside the income statement in retained earnings and presented in the statement of recognised income and expense

In addition, the group also operates defined contribution pension schemes Payments are charged as employee costs as they fall due The group has no further payment obligations once the contributions have been paid

Share-based compensation arrangements
The group operates equity-settled, share-based compensation plans In accordance with the transitional provisions, IFRS 2 'Share-based Payments' has been applied to all grants of equity instruments after 7 November 2002 that were unvested as of 1 April 2004

The group issues equity-settled share-based payments to certain employees Equity-settled share-based payments are measured at fair value at the date of grant The fair value determined at the grant date is expensed on a straight-line basis over the vesting period, based on estimates of the number of options that are expected to vest Fair value is based on both simulation and binomial models, according to the relevant measures of performance

At each balance sheet date, the group revises its estimate of the number of options that are expected to become exercisable with the impact of any revision being recognised in the income statement, and a corresponding adjustment to equity over the remaining vesting period The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised

o) Provisions
Provisions are recognised when the group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated

Environmental expenditure that relates to current or future revenues is expensed or capitalised as appropriate Expenditure that relates to an existing condition caused by past operations that does not contribute to current or future earnings is expensed Liabilities for environmental remediation costs are recognised when there is a legal or constructive obligation, environmental assessments or clean up are probable, and the associated costs can be reliably estimated

p) Revenue recognition
Revenue represents the fair value of the income receivable in the ordinary course of business for goods and services provided Where relevant, this includes an estimate of the sales value of units supplied to customers between the date of the last meter reading and the period end, exclusive of value added tax and foreign sales tax

The group recognises revenue generally at the time of delivery and when collection of the resulting receivable is reasonably assured Should the group consider that the criteria for revenue recognition are not met for a transaction, revenue recognition would be delayed until such time as the transaction becomes fully earned Payments received in advance of revenue recognition are recorded as deferred revenue

q) Grants and contributions
Grants and contributions receivable in respect of property, plant and equipment are treated as deferred income, which is credited to the income statement over the estimated economic lives of the related assets

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

Finance leases
Finance leases are capitalised in the consolidated balance sheet at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease The corresponding liability is shown as a finance lease obligation to the lessor Leasing repayments comprise both a capital and a finance element Where the lease is of a fixed interest nature, the finance element is written off to the income statement so as to produce an approximately constant periodic rate of charge on the outstanding obligation Where the lease is of a floating interest rate nature, the finance element written off to the income statement reflects the floating interest rate charge incurred during the period on the outstanding obligation Such assets are depreciated over the shorter of their estimated useful lives and the period of the lease

Operating leases
Operating lease rentals are charged to the income statement on a straight-line basis over the period of the lease

s) Critical accounting judgements and key sources of estimation uncertainty
In the process of applying the group's accounting policies, the group is required to make certain estimates, judgements and assumptions that it believes are reasonable based upon the information available These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the periods presented

On an ongoing basis, the group evaluates its estimates using historical experience, consultation with experts and other methods considered reasonable in the particular circumstances Actual results may differ significantly from the estimates, the effect of which is recognised in the period in which the facts that give rise to the revision become known

The following paragraphs detail the estimates and judgements the group believes to have the most significant impact on the annual results under IFRS

Carrying value of property, plant and equipment
The estimated useful economic lives of property, plant and equipment (PPE) are based on management's judgement and experience When management identifies that actual useful lives differ materially from the estimates used to calculate depreciation, that charge is adjusted prospectively Due to the significance of PPE investment to the group, variations between actual and estimated useful lives could impact operating results both positively and negatively, although historically, few changes to estimated useful lives have been required

The group is required to evaluate the carrying values of PPE for impairment whenever circumstances indicate, in management's judgement, that the carrying value of such assets may not be recoverable An impairment review requires management to make subjective judgements concerning the cashflows, growth rates and discount rates of the cash generating units under review

Revenue recognition
The group recognises revenue generally at the time of delivery and when collection of the resulting receivable is reasonably assured Should management consider that the criteria for revenue recognition are not met for a transaction, revenue recognition would be delayed until such time as the transaction becomes fully earned Payments received in advance of revenue recognition are recorded as deferred revenue

United Utilities North West raises bills and recognises revenue in accordance with its entitlement to receive revenue in line with the limits established by the periodic regulatory price review processes For water and wastewater customers with water meters, the receivable billed is dependent upon the volume supplied including an estimate of the sales value of units supplied between the date of the last meter reading and the year end Meters are read on a cyclical basis and the group recognises revenue for unbilled amounts based on estimated usage from the last billing through to the end of the financial year The estimated usage is based on historical data, judgement and assumptions, actual results could differ from these estimates, which would result in operating revenues being adjusted in the period that the revision to the estimates is determined For customers who do not have a meter, the receivable billed is dependent upon the rateable value of the property, as assessed by an independent rating officer

The customers of the electricity distribution business are the electricity supply companies that utilise United Utilities Electricity's distribution network to distribute electricity from generators to the end consumer The receivable billed is dependent upon the volume of electricity distributed, including estimates of the units distributed to customers The estimated usage is based on historical data, judgement and assumptions Operating revenues are gradually adjusted to reflect actual usage in the period over which the meters are read

For the group's other businesses, revenue is recognised in line with activity and performance, normally using amounts specified in contractual obligations and when collectability is reasonably assured In general

- variable revenues, for example, revenues dependent upon customer volumes in the period, are recognised only when those variable activities are performed,
- performance incentives are recognised in revenue only to the extent that incentives are reasonably considered to have been earned, and

- revenue received in advance of performance is recognised as deferred income When performance occurs, the deferred income is released and simultaneously reported as revenue

A breakdown of revenues by segment is contained in note 1 to the consolidated financial statements

Provision for doubtful receivables
At each balance sheet date, the company and each of its subsidiaries evaluate the collectability of trade receivables and record provisions for doubtful receivables based on experience These provisions are based on, amongst other things, comparisons of the relative age of accounts and consideration of actual write-off history The actual level of receivables collected may differ from the estimated levels of recovery, which could impact operating results positively or negatively

Accounting for provisions and contingencies
The group is subject to a number of claims incidental to the normal conduct of its business, relating to and including commercial, contractual and employment matters, which are handled and defended in the ordinary course of business The group routinely assesses the likelihood of any adverse judgements or outcomes to these matters as well as ranges of probable and reasonably estimated losses Reasonable estimates involve judgements made by management after considering information including notifications, settlements, estimates performed by independent parties and legal counsel, available facts, identification of other potentially responsible parties and their ability to contribute, and prior experience A provision is recognised when it is probable that an obligation exists for which a reliable estimate can be made of the obligation after careful analysis of the individual matter The required provision may change in the future due to new developments and as additional information becomes available Matters that either are possible obligations or do not meet the recognition criteria for a provision are disclosed, unless the possibility of transferring economic benefits is remote

Goodwill
The group records all assets and liabilities acquired in purchase acquisitions, including goodwill, at fair value Goodwill is not amortised but is subject, at a minimum, to annual tests for impairment The initial goodwill recorded and subsequent impairment analyses require management to make subjective judgements concerning the fair value of cash generating units Estimates of fair value are consistent with market information and the group's plans and forecasts

Retirement benefits
The group operates two defined benefit schemes, one of which has a defined contribution section, which are independent of the group's finances Actuarial valuations of the schemes are carried out as determined by the trustees at intervals of not more than three years The pension cost under IAS 19 'Employee Benefits' is assessed in accordance with the advice of a firm of actuaries based on the latest actuarial valuation and assumptions determined by the actuary The assumptions are based on information supplied to the actuary by the company, supplemented by discussions between the actuary and management The assumptions are disclosed in note 19 Profit before taxation is affected by the actuarial assumptions used These assumptions include investment returns on the schemes' assets, discount rates, pay growth and increases to pensions in payment and deferred pensions and may differ from actual results due to changing market and economic conditions and longer or shorter lives of participants

Derivatives and borrowings
The group's default treatment is for borrowings to be carried at amortised cost, whilst derivatives are recognised separately on the balance sheet at fair value with movements in those fair values reflected through the income statement This has the potential to introduce considerable volatility to both the income statement and balance sheet Therefore, for fair value hedges, changes in the recognised value of hedged debt that are attributable to the hedged risk are adjusted through the income statement In the case of cashflow hedges, movements in the fair value of derivatives are deferred within reserves until they can be recycled through the income statement to offset the future income statement effect of changes in the hedged risk In order to apply this treatment, it must be demonstrated that the derivative has been, and will continue to be, an effective hedge of the hedged risk within the debt item Changes in the fair value of all derivatives are recognised in the income statement, except for derivatives that are designated and effective in terms of cashflow hedging relationships, in which case the gains and losses are deferred in equity The group applies the fair value through profit or loss option where the complexity of the swaps means that they are disallowed from being allocated in a hedge relationship despite there being significant fair value offset between the hedged item and the derivative itself This policy is considered to be of significance due to the magnitude of the group's level of borrowings

Recently issued accounting pronouncements

International Financial Reporting Standards
At the date of authorisation of these financial statements, the following relevant standards and interpretations were in issue but not yet effective The directors anticipate that the group will adopt these standards and interpretations on their effective dates

The directors anticipate that the adoption of the following standards will have a material impact on the group's financial statements

- IAS 23 Amendment – 'Borrowing Costs'
  On 29 March 2007, the International Accounting Standards Board (IASB) issued a revised IAS 23 'Borrowing Costs' The main change from the previous version is the removal of the option of immediately recognising as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale The revised standard is effective for periods commencing on or after 1 January 2009 The group is, therefore, required to capitalise borrowing costs as part of the cost of qualifying assets from 1 April 2009

- IFRS 7 'Financial Instruments Disclosures'
  On 18 August 2005, the IASB issued IFRS 7 'Financial Instruments Disclosures' This standard adds certain new disclosures about financial instruments to those currently required by IAS 32 The standard is effective for periods commencing after 1 January 2007 As a result of the adoption of this standard, the group's disclosures regarding financial instruments will change from those currently disclosed in the financial statements

The directors anticipate that the adoption of these standards and interpretations will have no material impact on the group's financial statements

- IAS 1 Amendment – 'Capital Disclosures', is effective for periods commencing on or after 1 January 2007

- IFRS 8 'Operating Segments', issued in November 2006, is effective for periods commencing on or after 1 January 2009

- IFRIC 8 'Scope of IFRS 2', issued in January 2006, is effective for periods commencing on or after 1 May 2006 subject to endorsement by the EU
- IFRIC 9 'Reassessment of Embedded Derivatives', issued in March 2006, is effective for periods commencing on or after 1 June 2006
- IFRIC 10 'Interim Financial Reporting and Impairment', issued in July 2006, is effective for periods commencing on or after 1 November 2006
- IFRIC 11 'Group and Treasury Share Transactions', issued in November 2006, is effective for periods commencing on or after 1 March 2007
- IFRIC 12 'Service Concession Arrangements', issued in November 2006, is effective for periods commencing on or after 1 January 2008

Interpretations in issue but not considered relevant to the activities of the group are as follows

- IFRIC 1 'Changes in Existing Decommissioning, Restoration and Similar Liabilities'
- IFRIC 2 'Members' Shares in Cooperative Entities and Similar Instruments'
- IFRIC 5 'Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds'
- IFRIC 6 'Liabilities Arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment'
- IFRIC 7 'Applying the Re-statement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies'

1 Segment reportıng

The group's revenue predomınantly arıses from the sale of servıces

Durıng the year, for management purposes, the group's busıness was dıvıded ınto Unıted Utılıtıes North West, Unıted Utılıtıes Contract Solutıons and Vertex, whıch ıs dısclosed as a dıscontınued operatıon (see note 7) These dıvısıons form the basıs on whıch the followıng prımary segment ınformatıon ıs reported

Sınce the prevıous fınancıal statements, management has revıewed the approprıateness of Unıted Utılıtıes' segment reportıng ın lıght of the contınuıng evolutıon of the group As a result, management ıdentıfıed the above segments, whıch ıt belıeves alıgn the analysıs more closely wıth the way ın whıch the busıness ıs now managed, ın accordance wıth IAS 14 'Segment Reportıng' The maın ımpact has been the reclassıfıcatıon of the results of Unıted Utılıtıes Property Solutıons from Unıted Utılıtıes Contract Solutıons (formerly called Infrastructure Management) to Other actıvıtıes The 2006 segments have been re-stated for the ımpact of thıs change

The group was also prevıously ınvolved ın telecommunıcatıons (Your Communıcatıons) Thıs operatıon was dıscontınued wıth effect from 26 February 2006 (see note 7)

Tradıng between segments ıs carrıed out on an arm's length basıs and transactıons are prıced accordıngly External market prıces are used where avaılable, where not avaılable, margıns generated are compared to those generated from external sales and adjusted where necessary

Year ended 31 March 2007	Unıted Utılıtıes North West £m	Unıted Utılıtıes Contract Solutıons £m	Other actıvıtıes £m	Group £m
Contınuıng operatıons				
Total revenue	1,636 2	742 2	53 0	2,431 4
Inter-segment revenue	(6 5)	(93 7)	(8 2)	(108 4)
External revenue	**1,629 7**	**648 5**	**44 8**	**2,323 0**
Segmental operatıng profit	**750 1**	**69 1**	**8 3**	**827 5**
Investment ıncome				138 2
Fınance expense				(308 4)
Share of results of assocıated company				18 7
Profit before taxatıon				**676 0**
Taxatıon				(175 3)
Profit for the year from contınuıng operatıons				**500 7**

Year ended 31 March 2006 (re-stated)	Unıted Utılıtıes North West £m	Unıted Utılıtıes Contract Solutıons £m	Other actıvıtıes £m	Group £m
Contınuıng operatıons				
Total revenue	1,502 9	654 5	39 9	2,197 3
Inter-segment revenue	(8 1)	(94 4)	(8 8)	(111 3)
External revenue	1,494 8	560 1	31 1	2,086 0
Segmental operatıng profit	637 5	68 5	23 5	729 5
Investment ıncome				68 5
Fınance expense				(352 9)
Profit before taxatıon				445 1
Taxatıon				(122 0)
Profit for the year from contınuıng operatıons				323 1

1 Segment reporting continued

Year ended 31 March 2007	United Utilities North West £m	United Utilities Contract Solutions £m	Vertex £m	Other activities £m	Group £m
Other information					
Capital additions	646 7	41 8	22 5	1 9	712.9
Depreciation and amortisation	259 7	27 3	–*	1 5	288 5
Balance sheet					
Segment assets	10,700 8	630 2	–	930 2	12,261 2
Segment liabilities	(7,875 6)	(583 9)	–	(1,066 9)	(9,526 4)

Year ended 31 March 2006	United Utilities North West £m	United Utilities Contract Solutions £m	Vertex £m	Other activities £m	Group £m
Other information					
Capital additions	511 9	48 9	205 0	6 0	771 8
Depreciation and amortisation	265 3	17 5	–*	–	282 8
Balance sheet					
Segment assets	9 426 6	647 9	321 1	900 8	11,296 4
Segment liabilities	(6,406 5)	(465 3)	(175 3)	(1,618 4)	(8,665 5)

Depreciation and amortisation in respect of the group s discontinued operations is disclosed in note 7

Of the group's consolidated revenue and assets for continuing operations, greater than 90 per cent is derived from customers located in the United Kingdom, for both of the years ended 31 March 2007 and 31 March 2006, and hence no geographical analysis is presented

2 Directors and employees

Directors' remuneration

	2007 £m	2006 £m
Fees to non-executive directors	0 6	0 6
Salaries	2 0	1 8
Benefits	1 1	0 1
Bonus	1 3	0 8
Share-based payments	0 6	1 0
	5 6	4 3

Benefits of £1 1 million (2006 £0 1 million) include £0 7 million (2006 £nil) in respect of compensation for loss of office

Further information about the remuneration of individual directors and details of their pension arrangements is provided in the directors' remuneration report on pages 52 to 68

Remuneration of key management personnel

	2007 £m	2006 £m
Salaries and short-term employee benefits	6 1	4 9
Post employment benefits	0 3	2 9
Share-based payments	0 9	2 3
	7 3	10 1

Key management personnel comprises all executive directors and certain senior managers who are members of the executive leadership team

2 Directors and employees continued

Employee benefits expense

	Group		Company	
	2007 £m	2006 £m	2007 £m	2006 £m
Wages and salaries	**295 8**	269 9	**12 1**	10 0
Social security costs	**24 9**	23 3	**1 3**	1 1
Post employment benefits	**59 3**	54 0	**1 9**	1 8
	380 0	347 2	**15 3**	12 9
Capital schemes and charges against provisions	**(99 7)**	(89 9)	**-**	-
Employee benefits expense attributable to continuing operations	**280 3**	257 3	**15 3**	12 9
Employee benefits expense attributable to discontinued operations	**201 7**	216 7	**-**	-
	482 0	474 0	**15 3**	12 9
Less employee benefits expense attributable to joint ventures	**(4 7)**	(4 3)	**-**	-
	477 3	469 7	**15 3**	12 9

Average number of employees during the year (full time equivalent)

	2007 number	2006 number
United Utilities North West	**4,831**	4,775
United Utilities Contract Solutions	**3,539**	3 197
Vertex (discontinued operation)	**8,277**	8,203
Your Communications (discontinued operation)	**-**	653
Other activities	**221**	201
	16,868	17,029

3 Operating profit

The following items have been charged/(credited) to the income statement in arriving at the group's operating profit from continuing operations and the profit/(loss) from discontinued operations

	Continuing operations		Discontinued operations		Total	Total
	2007 £m	2006 £m	2007 £m	2006 £m	2007 £m	2006 £m
Employee benefits expense						
Employee costs (see note 2)	**280 3**	257 3	**201 7**	216 7	**482 0**	474 0
Depreciation and amortisation expense						
Depreciation of property, plant and equipment						
Owned assets (see note 10)	**275 6**	246 9	**4 2**	29 6	**279 8**	276 5
Under finance leases (see note 10)	**1 9**	1 7	**0 1**	-	**2 0**	1 7
Amortisation of other intangible assets (see note 12)	**11 0**	34 2	**9 9**	26 0	**20 9**	60 2
Other income						
Profit on disposal of property, plant and equipment	**(5 8)**	(4 7)	**-**	(0 1)	**(5 8)**	(4 8)
Other operating costs						
Other operating leases payable						
Property	**5 5**	3 3	**4.9**	8 1	**10 4**	11 4
Plant and equipment	**1 5**	3 2	**0 2**	-	**1 7**	3 2
Amortisation of government grants (see note 22)	**(14 0)**	(11 4)	**-**	-	**(14 0)**	(11 4)
Research and development expenses	**2 4**	1 9	**-**	-	**2 4**	1 9

3 Operating profit continued

During the year, the group obtained the following services from the group's auditors, at the costs detailed below

	2007 £m	2006 £m
Audit services		
Statutory audit	**1 1**	0 9
Audit-related regulatory reporting – other	**0 2**	0 5
Audit-related regulatory reporting – Sarbanes-Oxley preparation	**2 3**	0 2
	3 6	1 6
Further assurance services		
Advisory services – tax services	**0 1**	–
Compliance services	**0 9**	0 9
	4 6	2 5

Compliance services relate mainly to fees for transaction support

Included in the above statutory audit fee is £50,000 (2006 £50,000) in relation to the company

4 Investment income

	2007 £m	2007 £m	2006 £m	2006 £m
Interest receivable		**82 2**		34 9
Preference dividends receivable		**–**		0 3
Foreign exchange gains on forward contracts		**30 9**		16 8
Expected return on pension schemes' assets (see note 19)	**138 0**		122 8	
Interest cost on pension schemes' obligations (see note 19)	**(112 9)**		(106 3)	
Net pension interest income		**25 1**		16 5
		138 2		68 5

The group has changed its presentation of interest income and expenditure associated with its defined benefit pension schemes (see note 19) The amounts were previously disclosed within employee benefits expense in arriving at operating profit, but have been reclassified to investment income in the income statement as the directors believe this provides a fairer presentation of the nature of the income and costs Corresponding amounts for 2006 have been re-presented accordingly

5 Finance expense

	2007 £m	2006 £m
Interest payable on bank borrowings	**308 2**	278 1
Interest payable on finance leases	**2 9**	3 5
Fair value (gain)/loss on debt and derivative instruments	**(2 7)**	71 3
	308 4	352 9

The group has changed its presentation of interest on swaps and interest on debt under the fair value option The amounts were previously disclosed within interest payable on bank borrowings but have been reclassified to the fair value movement on debt and derivative instruments line as the directors believe this provides a fairer presentation of the nature of the interest Corresponding amounts for 2006 have been re-presented accordingly

6 Taxation

Continuing operations	2007 £m	2006 £m
Current tax		
UK corporation tax	**123 6**	60 2
Foreign tax	**3 1**	2 3
Prior year	**(50 9)**	(13 1)
Deferred tax		
Current year	**79 7**	64 6
Prior year	**19 8**	8 0
Total tax charge for the year	**175 3**	122 0

Discontinued operations	2007 £m	2006 £m
Current tax		
UK corporation tax	**(3 4)**	(49 7)
Foreign tax	**1 3**	1 1
Prior year	**-**	11 2
Deferred tax		
Current year	**9 0**	(11 6)
Prior year	**0 9**	(16 3)
Total tax charge/(credit) for the period	**7 8**	(65 3)

The tables below reconcile the notional tax charge at the UK corporation tax rate to the effective tax rate for the year

Continuing operations	2007 £m	2007 %	2006 £m	2006 %
Profit before tax	**676 0**		445 1	
Adjustment for share of results of associated company	**(18 7)**		-	
	657 3		445 1	
Tax at the UK corporation tax rate of 30 per cent	**197 2**	**30 0**	133 5	30 0
Adjustments in respect of prior periods	**(31 1)**	**(4 7)**	(5 1)	(1 2)
Net expense/(income) not deductible/(taxable)	**9 2**	**1 4**	(6 4)	(1 4)
Total tax charge and effective tax rate for the year	**175 3**	**26 7**	122 0	27 4

Discontinued operations	2007 £m	2007 %	2006 £m	2006 %
Profit/(loss) before tax	**19 2**		(171 1)	
Tax at the UK corporation tax rate of 30 per cent	**5 8**	**30 0**	(51 3)	30 0
Adjustments in respect of prior periods	**0 9**	**4 8**	(5 1)	3 0
Net expense/(income) not deductible/(taxable)	**(0 8)**	**(4 1)**	14 5	(8 5)
Total tax charge/(credit) and effective tax rate for the period on trading profit/(loss)	**5 9**	**30 7**	(41 9)	24 5
Tax on loss on disposal of discontinued operations	**1 9**		(23 4)	
	7 8		(65 3)	

A current tax credit of £31 1 million (2006 £5 1 million) arose in the year following the agreement of prior year tax returns

7 Discontinued operations

On 26 March 2007, the group sold the Vertex business as part of its declared strategy of concentrating on its core skills of managing water, wastewater, electricity and gas networks The purchaser was a consortium of US based private equity firms led by Oak Hill Capital Partners and also including GenNx360 and Knox Lawrence International

The results of Vertex have been disclosed within discontinued operations in the group's financial statements The detailed trading results and loss on disposal of Vertex for the period ended 26 March 2007 and the loss for the year ended 31 March 2006 are shown below Cashflows in relation to discontinued operations are separately disclosed in the group's cashflow statement

Discontinued operations	Period ended 26 March 2007 Vertex £m	Year ended 31 March 2006 Vertex £m
Revenue		
External sales	303 4	300 8
Intra-group sales	89 5	119 6
Total revenue	392 9	420 4
Depreciation and amortisation	(14 2)	(37 5)
Other operating expenses	(363 7)	(388 9)
Operating expenses	(377 9)	(426 4)
Operating profit/(loss)	15 0	(6 0)
Investment income and finance expense	4 2	0 2
Profit/(loss) before taxation	19 2	(5 8)
Taxation on (profit)/loss	(5 9)	1 7
Profit/(loss) for the period from discontinued operations	13 3	(4 1)
Loss on disposal of discontinued operations before taxation and assumption of deferred contingent consideration	(65 1)	–
Assumption of deferred contingent consideration	(13 5)	–
Loss on disposal of discontinued operations before taxation	(78 6)	–
Taxation on loss on disposal of discontinued operations	(1 9)	–
Total loss for the period from discontinued operations	(67 2)	(4 1)

Revenue from the group's discontinued operations was derived principally from the United Kingdom

Profit/(loss) before taxation includes profit generated from intercompany trading of £8 7 million (2006 £13 5 million)

The net assets of Vertex at the date of disposal and at 31 March 2006 were as follows

	26 March 2007 £m	31 March 2006 £m
Intangible assets	262 6	233 3
Property, plant and equipment	21 4	25 1
Trade receivables	73 5	77 6
Retirement benefit obligations	(6 3)	–
Trade and other payables	(53 4)	(161 2)
Non-current liabilities	(142 5)	(24 3)
	155 3	150 5[1]
Loss on disposal before taxation	(78 6)	
Repayment of intercompany debt	107 6	
Transaction costs	8 6	
Total fair value of consideration	192 9[2]	

Note:

(1) The comparative net assets of the Vertex business have been presented on a basis consistent with the disposal balance sheet

(2) Total fair value of consideration comprises cash of £206 4 million less the assumption of deferred contingent consideration of £13 5 million (see note 24)

7 Dıscontınued operatıons continued

On 26 February 2006, the group sold the Your Communıcatıons' busıness as part of ıts declared strategy of a progressıve exıt from the telecoms market The purchaser was THUS Group plc and the consıderatıon comprısed an ınıtıal consıderatıon of 391,532,852 ordınary shares wıth a market value of 15 5 pence each (ın aggregate £60 7 mıllıon), together wıth the optıon to acquıre up to a further 4 8 per cent of shares ın THUS Group plc dependent upon the future share prıce of THUS Group plc Thıs optıon was valued at £13 2 mıllıon at 31 March 2006 and ıs classıfıed as a derıvatıve asset (see note 18)

Prıor to the sale, at 30 September 2005, on recognıtıon of the assets and lıabılıtıes of the Your Communıcatıons' busıness as a dısposal group ın accordance wıth IFRS 5 'Non-current Assets held for Sale and Dıscontınued Operatıons', an adjustment to faır value was recognısed The adjustment to carryıng value of £147 7 mıllıon was allocated agaınst property, plant and equıpment £105 4 mıllıon (see note 10), goodwıll £24 4 mıllıon (see note 11) and other ıntangıble assets £17 9 mıllıon (see note 12)

The results of Your Communıcatıons have been dısclosed wıthın dıscontınued operatıons ın the group's fınancıal statements The detaıled tradıng results and gaın on dısposal of Your Communıcatıons for the perıod ended 26 February 2006 are shown below Cashflows ın relatıon to dıscontınued operatıons are separately dısclosed ın the group's cashflow statement

Dıscontınued operatıons	Period ended 26 February 2006 Your Communıcatıons £m
Revenue	
External sales	163 6
Intra-group sales	11 8
Total revenue	175 4
Depreciatıon and amortısatıon	(18 1)
Other operatıng expenses	(162 2)
Operatıng expenses	(180 3)
Operatıng loss	(4 9)
Investment ıncome and fınance expense	(12 7)
Loss before taxatıon	(17 6)
Taxatıon on loss	8 6
Loss for the perıod from dıscontınued operatıons	(9 0)
Adjustment to value before taxatıon	(147 7)
Taxatıon on adjustment to value	31 6
Net adjustment to value	(116 1)
Loss on dısposal of dıscontınued operatıons	(9 1)
Taxatıon on loss on dısposal of dıscontınued operatıons	23 4
Net profıt on dısposal after taxatıon	14 3
Total loss for the perıod from dıscontınued operatıons	(110 8)

Revenue from the group's dıscontınued operatıons was derıved prıncıpally from the Unıted Kıngdom

The net assets of Your Communıcatıons at the date of dısposal were as follows

	26 February 2006 £m
Other ıntangıble assets	7 9
Property, plant and equıpment	55 8
Inventorıes	7 4
Trade receıvables	40 3
Retırement benefıt oblıgatıons	(8 3)
Trade payables	(25 7)
Non-current lıabılıtıes	(0 2)
	77 2
Loss on dısposal before taxatıon	(9 1)
Total faır value of consıderatıon satısfıed by ordınary shares and contıngent share optıons less transactıon costs	68 1

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8 Dividends

	2007 £m	2006 £m
Amounts recognised as distributions to equity holders in the year comprise		
Ordinary shares		
Final dividend for the year ended 31 March 2006 at 29 58 pence per share (2005 28 61 pence)	**259 0**	172 0
Interim dividend for the year ended 31 March 2007 at 14 63 pence per share (2006 14 29 pence)	**128 3**	124 8
A shares		
Final dividend for the year ended 31 March 2006 at nil pence per share (2005 14 307 pence)	**-**	47 4
	387 3	344 2
Proposed final dividend for the year ended 31 March 2007 at 30 30 pence per share (2006 29 58 pence)	**266 6**	259 0

The proposed final dividends for the years ended 31 March 2007 and 31 March 2006 were subject to approval by equity holders of the company and hence have not been included as liabilities in the financial statements at 31 March 2007 and 31 March 2006 respectively

In July 2005, following completion of the second stage of the rights issue, the A shares were consolidated and reclassified as ordinary shares on the basis of one ordinary share for two A shares (see note 23)

9 Earnings per share

	2007 £m	2006 £m
Profit for the year attributable to equity holders of the company – continuing and discontinued operations	**433 5**	207 9
Adjustment for loss for the period from discontinued operations	**67 2**	114 9
Profit for the year attributable to equity holders of the company – continuing operations	**500 7**	322 8

	2007 pence	2006 pence
Earnings per share from continuing and discontinued operations		
Basic	**49 4**	24 3
Diluted	**49 2**	24 2
Earnings per share from continuing operations		
Basic	**57 1**	37 8
Diluted	**56 9**	37 6
Earnings per share from discontinued operations		
Basic	**(7 7)**	(13 5)
Diluted	**(7 7)**	(13 5)

Basic earnings per share have been calculated by dividing profit for the financial year attributable to equity holders of the company by 876 8 million, being the weighted average number of shares in issue during the year (2006 853 9 million)

Diluted earnings per share have been calculated by dividing profit for the financial year attributable to equity holders of the company by 880 6 million, being the weighted average number of shares in issue during the year including dilutive shares (2006 858 4 million) The dilutive adjustment has not been applied where the result is a loss per share due to its anti-dilutive effect

The difference between the weighted average number of shares used in the basic and the diluted earnings per share calculations represents those ordinary shares deemed to have been issued for no consideration on the conversion of all potential dilutive ordinary shares in accordance with IAS 33 'Earnings Per Share'

The weighted average number of shares can be reconciled to the weighted average number of shares including dilutive shares as follows

	2007 million	2006 million
Average number of ordinary shares in issue – basic	**876 8**	853 9
Average number of potentially dilutive ordinary shares under option	**5 7**	9 1
Number of ordinary shares that would have been issued at fair value	**(1 9)**	(4 6)
Average number of ordinary shares – diluted	**880 6**	858 4

10 Property, plant and equipment

Group	Land and buildings £m	Infrastructure assets £m	Operational assets £m	Fixtures fittings tools and equipment £m	Assets in course of construction £m	Total £m
Cost						
At 1 April 2005	352 1	3,026 8	5,476 1	545 7	1,207 2	10,607 9
Additions	9 7	47 9	173 4	38 7	269 7	539 4
Acquisitions	–	–	–	4 6	–	4 6
Transfers	(5 3)	136 7	501 6	24 1	(672 7)	(15 6)
Disposals	(11 9)	(13 4)	(286 5)	(100 8)	(14 0)	(426 6)
Currency translation differences	0 1	2 6	(0 2)	0 1	0 1	2 7
At 31 March 2006	344 7	3,200 6	5,864 4	512 4	790 3	10,712 4
Additions	9 0	53 3	152 7	47 5	423 2	685 7
Transfers	6 4	135 6	316 5	17 3	(475 8)	–
Disposals	(13 1)	(0 7)	(23 2)	(119 0)	(6 7)	(162 7)
Currency translation differences	(0 2)	(1 9)	–	(0 4)	–	(2 5)
At 31 March 2007	**346 8**	**3,386 9**	**6,310 4**	**457 8**	**731 0**	**11,232 9**
Accumulated depreciation						
At 1 April 2005	105 2	68 3	1,670 3	289 6	–	2,133 4
Charge for the year	12 6	27 3	192 5	45 8	–	278 2
Transfers	(7 8)	–	(0 1)	(2 0)	–	(9 9)
Disposals	(6 1)	(5 0)	(238 4)	(82 7)	(7 1)	(339 3)
Adjustment to value (see note 7)	–	–	88 8	9 5	7 1	105 4
Currency translation differences	–	0 6	(0 1)	0 2	–	0 7
At 31 March 2006	103 9	91 2	1 713 0	260 4	–	2,168 5
Charge for the year	12 4	28 7	192 2	48 5	–	281 8
Transfers	–	(2 1)	–	2 1	–	–
Disposals	(6 7)	(0 2)	(13 3)	(92 6)	–	(112 8)
Currency translation differences	–	0 6	–	0 2	–	0 8
At 31 March 2007	**109 6**	**118 2**	**1,891 9**	**218 6**	**–**	**2,338 3**
Net book value at 31 March 2007	**237 2**	**3,268 7**	**4,418 5**	**239 2**	**731 0**	**8,894 6**
Net book value at 31 March 2006	240 8	3,109 4	4,151 4	252 0	790 3	8,543 9

The carrying amount of the group's operational assets includes an amount of £66 0 million (2006 £68 1 million) in respect of assets held under finance leases

At 31 March 2007, the group had entered into contractual commitments for the acquisition of property, plant and equipment amounting to £370 7 million (2006 £183 1 million)

Company	Fixtures fittings tools and equipment £m
Cost	
At 1 April 2005, 31 March 2006 and 31 March 2007	**4 8**
Accumulated depreciation	
At 1 April 2005 and 31 March 2006	4 0
Charge for the year	0 2
At 31 March 2007	**4 2**
Net book value at 31 March 2007	**0 6**
Net book value at 31 March 2006	0 8

The company had no contractual commitments for the acquisition of property, plant and equipment at 31 March 2007 or at 31 March 2006

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11 Goodwill

Group	£m
Cost	
At 1 April 2005	100 6
Additions	75 5
Adjustment to value (see note 7)	(24 4)
Currency translation differences	1 4
At 31 March 2006	153 1
Additions	3 2
Impairment	(0 8)
Disposals	(149 7)
Currency translation differences	(0 8)
At 31 March 2007	**5 0**

Goodwill is subject to impairment testing annually, or more frequently if there are indications of impairment The recoverable amounts of cash generating units (CGUs) are determined from value-in-use calculations that use amounts from approved budgets and plans for the next five years and extrapolate cashflows for a further five years based on an estimated growth rate of 2 8 per cent The discount rate applied to the cashflow projections was 12 0 per cent (2006 11 9 per cent) The range of growth rates used of 2 8 to 5 0 per cent (2006 2 5 to 3 0 per cent) was based on industry growth rates

Goodwill is allocated to the appropriate CGU according to the business segment The net book value of goodwill by these segments was as follows

Group	2007 £m	2006 £m
United Utilities Contract Solutions	5 0	6 2
Vertex (discontinued operation)	–	146 9
	5 0	153 1

During the year, an impairment of £0 8 million was recognised within discontinued operations in respect of goodwill related to First Revenue Assurance LLC, a subsidiary of Vertex (2006 £nil)

12 Other intangible assets

Group	Computer software £m	Other £m	Total £m
Cost			
At 1 April 2005	393 7	107 8	501 5
Additions – internally generated	1 2	–	1 2
Additions – purchased	51 7	0 3	52 0
Acquisitions	5 7	93 4	99 1
Disposals	(159 9)	(70 6)	(230 5)
At 31 March 2006	292 4	130 9	423 3
Additions – purchased	22 2	1 8	24 0
Disposals	(85 7)	(113 4)	(199 1)
Currency translation differences	–	(0 7)	(0 7)
At 31 March 2007	**228 9**	**18 6**	**247 5**
Amortisation			
At 1 April 2005	250 3	58 4	308 7
Charge for the year	45 5	14 7	60 2
Disposals	(138 4)	(61 3)	(199 7)
Adjustment to value (see note 7)	–	17 9	17 9
At 31 March 2006	157 4	29 7	187 1
Charge for the year	12 0	8 9	20 9
Disposals	(44 5)	(31 2)	(75 7)
Currency translation differences	–	(0 3)	(0 3)
At 31 March 2007	**124 9**	**7 1**	**132 0**
Net book value at 31 March 2007	**104 0**	**11 5**	**115 5**
Net book value at 31 March 2006	135 0	101 2	236 2

At 31 March 2007, the group had entered into contractual commitments for the acquisition of other intangible assets amounting to £nil (2006 £3 0 million) The company had no contractual commitments for the acquisition of other intangible assets at 31 March 2007 or at 31 March 2006

The 'other' intangible assets category relates mainly to customer related intangibles such as customer contracts and customer lists

13 Investments

Non-current asset investments

Group	Associate £m	Other investments £m	Total £m
At 1 April 2005	–	9 7	9 7
Additions	60 7	85 7	146 4
Disposals	–	(0 4)	(0 4)
Revaluation	–	14 6	14 6
Exchange adjustments	–	0 4	0 4
At 31 March 2006	60 7	110 0	170 7
Additions	4 3	–	4 3
Disposals	–	(0 4)	(0 4)
Revaluation	–	8 9	8 9
Share of results of associated company	18 7	–	18 7
Exchange adjustments	–	(0 4)	(0 4)
At 31 March 2007	**83 7**	**118 1**	**201 8**

On 26 February 2006, the group acquired 391,532,852 ordinary shares in THUS Group plc as consideration for the sale of the Your Communications' business (see note 7) This investment, in listed equity securities, presents the group with opportunity for return through dividend income and trading gains These securities have no fixed maturity or coupon rate

During the year the number of shares held in THUS Group plc was reduced to 39,153,285 as part of a ten for one share consolidation

On 1 February 2007, the group received a further 2,274,701 shares with a fair value of £4 3 million in THUS Group plc as a result of the vesting of part of the option received as part of the consideration for the sale of the Your Communications' business

13 Investments continued

On 1 June 2005, the group acquired a 15 0 per cent shareholding in Northern Gas Networks Holdings Limited In the opinion of the directors, there is no material difference between the book and fair values of this investment

The group's 22 6 per cent (2006 21 7 per cent) investment in THUS Group plc qualifies as an associate in accordance with IAS 28 'Investments in Associates' Equity accounting has been applied in respect of this investment in the group's financial statements for the year ended 31 March 2007 The group's share of the post acquisition results for the five weeks ended 31 March 2006 has not been separately disclosed in the income statement or statement of recognised income and expense for the prior year, on the grounds of materiality

The fair values of the group's financial instruments are shown in note 18

Details of principal operating subsidiary undertakings, unlisted joint ventures and associates, are set out below These undertakings are included within the consolidated group financial statements

	Class of share capital held	Proportion of share capital owned/voting rights %	Nature of business
Subsidiary undertakings			
Great Britain			
United Utilities Water PLC	Ordinary	100 0	Water and wastewater services and network management
United Utilities Electricity PLC	Ordinary	100 0	Electricity distribution and related services
United Utilities International Limited	Ordinary	100 0	Consulting services and project management
United Utilities Facilities Management Limited	Ordinary	100 0	Facilities management
United Utilities Waste Management Limited	Ordinary	100 0	Waste management
United Utilities Industrial (Gwent) Limited	Ordinary	100 0	Waste management
United Utilities Industrial Limited	Ordinary	100 0	Water treatment operations
United Utilities Property Solutions Limited	Ordinary	100 0*	Property management
United Utilities Operational Services Limited	Ordinary	100 0	Operation and maintenance of water and wastewater assets of Dwr Cymru
United Utilities Operational Services (Highland) Limited	Ordinary	100 0	Operation and maintenance of wastewater assets
United Utilities Operational Services (Tay) Limited	Ordinary	100 0	Operation and maintenance of wastewater assets
United Utilities Operational Services (Moray) Limited	Ordinary	100 0	Operation and maintenance of wastewater assets
United Utilities Networks Limited	Ordinary	100 0	Multi-utility metering and network operations
United Utilities Operations Limited	Ordinary	100 0	Operation and maintenance of Northern Gas Networks' gas assets and management of capital programme
Australia			
United Utilities Australia Pty Limited	Ordinary	100 0	Water treatment operations, technical and management services
United Utilities Macarthur Operations Pty Limited	Ordinary	100 0	Technical and management services
Yabulu Water Pty Limited	Ordinary	100 0	Technical and management services
UU Victor Harbor Pty Limited	Ordinary	100 0	Wastewater treatment operations
UU Onkaparinga Pty Limited	Ordinary	100 0	Technical and management services
Joint ventures			
Great Britain			
Catchment Limited	Ordinary	50 0	Contract operations and maintenance services
Catchment (Tay) Limited	Ordinary	33 0	Contract operations and maintenance services
Catchment (Moray) Limited	Ordinary	33 0	Contract operations and maintenance services
Meter Fit (North West) Limited	Ordinary	50 0	Metering installation services
Meter Fit (North East) Limited	Ordinary	50 0	Metering installation services
UUGM Limited	Ordinary	60 0	Consulting services and project management
4Delivery Limited	Ordinary	40 0	Consulting services and project management
Australia			
Yan Yean Water Pty Limited	Ordinary	50 0	Water treatment operations
Macarthur Water Pty Limited	Ordinary	50 0	Water treatment operations
Riverland Water Pty Limited	Ordinary	50 0	Water treatment operations
Campaspe Asset Management Services Pty Limited	Ordinary	50 0	Asset management and water treatment
Estonia			
AS Tallinna Vesi	Ordinary	26 5	Contract operations and maintenance services
Bulgaria			
Sofiyska Voda AD	Ordinary	57 8	Contract operations and maintenance services
Poland			
Aqua SA	Ordinary	33 2	Contract operations and maintenance services
Associate			
Great Britain			
THUS Group plc	Ordinary	22 6*	Telecommunications

Shares are held by subsidiary undertakings, except where marked with an asterisk where shares are held directly by United Utilities PLC

13 Investments continued

A full list of the company's subsidiary undertakings is included within the company's annual return, which will be filed with the Registrar of Companies by 8 August 2007

In relation to the group's interests in joint ventures and the financial performance of the group's associate, the assets, liabilities, gross income and expenses are summarised below

	Associate 31 March 2007 £m	Associate 31 March 2006 £m	**Group share of joint ventures 31 March 2007 £m**	Group share of joint ventures 31 March 2006 £m
Non-current assets	**510 4**	444 0	**274 6**	263 8
Current assets	**144 4**	186 8	**110 3**	106 9
Non-current liabilities	**(51 4)**	(101 4)	**(222 6)**	(215 6)
Current liabilities	**(132 2)**	(143 8)	**(81 1)**	(69 4)
	471 2	385 6	**81 2**	85 7

	Associate 2007 £m	Associate 2006 £m	**Group share of joint ventures 2007 £m**	Group share of joint ventures 2006 £m
Gross income	**532 7**	350 0	**204 2**	165 3
Expenses	**(547 8)**	(378 3)	**(188 1)**	(152 4)
Taxation	**69 6**	–	**(3 4)**	(2 8)
Post tax results – continuing	**54 5**	(28 3)	**12 7**	10 1
Post tax results – discontinued	**29 4**	2 1	**–**	–
Profit/(loss) for the year	**83 9**	(26 2)	**12 7**	10 1

The joint ventures and associate have no significant contingent liabilities to which the group is exposed and the group has no significant contingent liabilities in relation to its interests in the joint ventures and associate

Non-current asset investments

Company	Associate £m	Shares in subsidiary undertakings £m	Total £m
At 1 April 2005	–	4,833 1	4,833 1
Additions	73 9	594 7	668 6
At 31 March 2006	73 9	5,427 8	5,501 7
Reclassification to derivatives	(13 2)	–	(13 2)
Additions	4 3	–	4 3
Disposals	–	(224 5)	(224 5)
At 31 March 2007	**65 0**	**5,203 3**	**5,268 3**

Current asset investments

Current asset investments comprise properties held by the group for development and sale of £38 5 million (2006 £29 7 million)

14 Inventories

Group	**2007 £m**	2006 £m
Raw materials and finished goods	**10 8**	9 4
Work in progress	**13 5**	18 8
	24 3	28 2

15 Trade and other receivables

	Group		Company	
	2007 £m	2006 £m	**2007 £m**	2006 £m
Trade receivables	**161 5**	231 4	**1 7**	–
Amounts owed by subsidiary undertakings	**–**	–	**988 8**	1,110 2
Amounts owed by related parties	**11 9**	0 6	**–**	–
Other debtors	**30 6**	38 2	**–**	18 3
Prepayments and accrued income	**235 8**	241 9	**3 1**	2 1
	439 8	512 1	**993 6**	1,130 6

Trade and other receivables have been analysed between non-current and current as follows

	Group		Company	
	2007 £m	2006 £m	**2007 £m**	2006 £m
Non-current	**21 6**	22 0	**–**	–
Current	**418 2**	490 1	**993 6**	1 130 6
	439 8	512 1	**993 6**	1,130 6

Trade receivables do not carry interest and are stated net of allowances for doubtful receivables of £147 7 million (2006 £155 6 million)

The group has no significant concentration of credit risk with exposure spread over a large number of customers

The directors consider that the carrying amount of trade and other receivables approximates to their fair value

The average credit period taken on sales is 28 days (2006 35 days)

16 Cash and cash equivalents

	Group		Company	
	2007 £m	2006 £m	**2007 £m**	2006 £m
Cash at bank and in hand	**73 3**	127 0	**5 2**	120 4
Short-term bank deposits	**2,330 0**	1,386 5	**331 5**	–
Cash and short-term deposits	**2,403 3**	1 513 5	**336 7**	120 4
Bank overdrafts (included in borrowings, see note 17)	**(62 6)**	(69 6)	**–**	–
Cash and cash equivalents in the cashflow statement	**2,340 7**	1,443 9	**336 7**	120 4

The effective interest rate on short-term deposits during the year ended 31 March 2007 was 3 91 per cent (2006 4 30 per cent) These deposits have a weighted average maturity of 27 days (2006 13 days) In the years ended 31 March 2007 and 31 March 2006, short-term deposits included a significant amount denominated in Japanese yen Excluding the impact of the Japanese yen deposits, the effective interest rate on short-term deposits denominated in sterling was 4 91 per cent (2006 4 59 per cent)

17 Borrowings

Group
This note provides information about the contractual terms of the group's loans and borrowings For more information about the group's exposure to interest rate and foreign currency risk, see note 18

Group	**2007 £m**	2006 £m
Non-current liabilities		
Bonds	**4,080 3**	4 252 9
Bank and other term borrowings	**711 3**	753 0
Finance lease obligations	**63 3**	75 2
	4,854 9	5,081 1
Current liabilities		
Bonds	**696 7**	19 7
Euro-commercial paper	**451 6**	218 3
Bank and other term borrowings	**286 6**	306 2
Bank overdrafts	**62 6**	69 6
Finance lease obligations	**12 0**	5 3
	1,509 5	619 1
	6,364 4	5,700 2

17 Borrowings continued

Terms and debt repayment schedule

The principal economic terms and conditions of outstanding loans and borrowings were as follows

Group	Currency	Year of maturity	2007 Carrying value £m	2006 Carrying value £m
Borrowings in fair value hedge relationships				
5 625% 300m bond	GBP	2027	**295 9**	317 6
5% 200m bond	GBP	2035	**188 4**	202 4
5 25% 150m bond	GBP	2010	**145 8**	148 9
5 375% 150m bond	GBP	2018	**142 9**	150 8
6 625% 1,000m bond	EUR	2007	**673 8**	690 9
4 875% 600m bond	EUR	2009	**403 4**	420 4
4 25% 500m bond	EUR	2020	**321 7**	337 6
6 45% 500m bond	USD	2008	**255 7**	291 7
5 375% 350m bond	USD	2019	**170 6**	190 4
4 55% 250m bond	USD	2018	**113 7**	126 1
5 02% 10,000m reverse dual currency bond	JPY	2029	**53 9**	60 8
0 44%+HIBOR 150m (floating) bond	HKD	2007	**9 8**	11 1
Borrowings in cashflow hedge relationships				
EIB 90m (floating) loan – 5 6%	GBP	2013	**90 0**	90 1
Borrowings designated at fair value through profit and loss				
8 875% 250m bond	GBP	2026	**344 7**	358 9
6 875% 400m bond	USD	2028	**217 5**	240 1
0 705% 3 000m bond	JPY	2008	**12 9**	14 7
1 135% 3,000m bond	JPY	2013	**12 5**	13 6
0 75% 1,000m bond	JPY	2007	**–**	4 9
Borrowings measured at amortised cost				
1 97%+RPI 200m IL bond	GBP	2016	**200 7**	–
8 875% 200m bond	GBP	2026	**194 9**	194 9
1 9799%+RPI 100m IL bond	GBP	2035	**104 7**	101 5
1 7829%+RPI 100m IL bond	GBP	2040	**103 6**	100 5
1 5802%+RPI 100m IL bond	GBP	2042	**103 3**	100 0
1 4746%+RPI 100m IL bond	GBP	2046	**103 0**	–
1 847%+RPI 100m IL bond	GBP	2056	**102 5**	–
1 815%+RPI 100m IL bond	GBP	2056	**102 1**	–
1 662%+RPI 100m IL bond	GBP	2056	**101 9**	–
3 375%+RPI 50m IL bond	GBP	2032	**55 4**	54 8
1 3258%+RPI 50m IL bond	GBP	2041	**51 7**	50 1
1 397%+RPI 50m IL bond	GBP	2046	**51 6**	50 1
1 5366%+RPI 50m IL bond	GBP	2043	**51 5**	–
1 7937%+RPI 50m IL bond	GBP	2049	**51 4**	–
1 5865%+RPI 50m IL bond	GBP	2056	**50 9**	–
1 556%+RPI 50m IL bond	GBP	2056	**50 6**	–
1 435%+RPI 50m IL bond	GBP	2056	**50 5**	–
1 3805%+RPI 35m IL bond	GBP	2056	**35 3**	–
Commission for the New Towns loan – 14 83%	GBP	2053	**31 2**	31 4
1 591%+RPI 25m IL bond	GBP	2056	**25 4**	–
0 24%+LIBOR 6 5m (floating) bond	GBP	2013	**6 5**	6 5
4 21% 10m bond	EUR	2008	**6 8**	7 0
0 385%+LIBOR 10m (floating) bond	USD	2008	**5 1**	5 8
0 365%+LIBOR 10m (floating) bond	USD	2009	**5 1**	5 8
0 765% 3,000m bond	JPY	2006	**–**	14 7
Long-term bank borrowings floating – 5 41%–5 608%	GBP	2007-2012	**253 0**	256 0
Long-term bank borrowings – 6 55%–6 89%	GBP	2007-2008	**210 0**	223 6
Euro-commercial paper – 5 34%–5 65%	GBP	2007-2008	**65 9**	190 0
Euro-commercial paper – 3 8%–3 914%	EUR	2007-2008	**382 8**	13 9
Euro-commercial paper – 5 452%	USD	2007-2008	**2 9**	14 4
Long-term debt issued by joint ventures	Various	Various	**213 0**	206 3
Committed facilities – drawn	GBP	2007	**–**	251 8
Other borrowings				
Finance lease obligations – 4 26%	GBP	2014	**75 3**	80 5
Bank overdrafts	GBP	2007	**62 6**	69 6
			6,364 4	5,700 2

Abbreviations used in the above table are defined on page 97

17 Borrowings continued

Loans and borrowings are unsecured Funding raised in currencies other than sterling is generally swapped to sterling to match funding costs to income

The fair values of the group's financial instruments are shown in note 18

Borrowing facilities
The group had available committed bank facilities of £1,300 0 million at 31 March 2007 (2006 £1,000 0 million) of which £1,297 2 million was unutilised (2006 £745 4 million) The utilisation of £2 8 million as at 31 March 2007 represents guarantees against off-balance sheet liabilities detailed on page 33 As at 31 March 2006, the group had drawn £251 8 million in addition to the guarantees of £2 8 million Of the amounts unutilised, £125 0 million expires within one year (2006 £295 0 million), £100 0 million expires after one year but in less than two years (2006 £125 0 million), and the remaining £1,072 2 million expires in more than two years (2006 £325 4 million) Bank overdrafts are repayable on demand

Finance lease obligations
Finance lease liabilities are payable as follows

Group	Minimum lease payments		Present value of minimum lease payments	
	2007 £m	2006 £m	**2007 £m**	2006 £m
Amounts payable under finance leases				
Within one year	**12 0**	5 3	**12 0**	5 3
In the second to fifth years inclusive	**54 4**	51 8	**43 8**	32 9
After five years	**31 8**	52 6	**19 5**	42 3
	98 2	109 7	**75 3**	80 5
Less future finance charges	**(22 9)**	(29 2)	**–**	–
Present value of lease obligations	**75 3**	80 5	**75 3**	80 5
Less amount due for settlement within 12 months			**(12 0)**	(5 3)
Amount due for settlement after 12 months			**63 3**	75 2

Finance lease obligations relate to operational assets Interest rates implicit in the minimum lease payments were fixed on completion of the asset build when the primary period of the lease commenced In addition, contingent rentals are either payable or receivable, which adjust the minimum lease payments to reflect changes in future market rates of interest These contingent rentals are recognised as an increase or reduction in finance expense in the period to which they relate Contingent rentals recognised as a reduction in finance expense in the year total £3 4 million (2006 £3 5 million) The net finance charge for the year, after adjusting for contingent rentals, was £2 9 million (2006 £3 5 million) (see note 5) and the effective borrowing rate (after adjusting for contingent rentals) for the year was 4 260 per cent (2006 4 467 per cent) The average remaining lease term is seven years (2006 eight years)

In addition, the minimum lease payments are subject to adjustment for future tax changes Any adjustment to the rentals is recognised as an increase or reduction in the future finance expense over the remaining term of the lease

The group's obligations under finance leases are unsecured

The minimum lease payments for 2006 have been re-presented to show separately gross payments and future finance charges

The directors consider the fair value of the group's lease obligations approximate to their carrying value

Company
The following analysis provides information about the contractual terms of the company's loans and borrowings

Company	**2007 £m**	2006 £m
Non-current liabilities		
Bonds	**764 1**	880 0
Bank and other term borrowings	**1 1**	0 9
	765 2	880 9
Current liabilities		
Euro-commercial paper	**451 6**	218 3
Bonds	**12 9**	8 1
Bank and other term borrowings	**–**	251 8
Amounts owed to subsidiary undertakings	**463 5**	–
	928 0	478 2
	1,693 2	1,359 1

17 Borrowings continued

Terms and debt repayment schedule

The principal economic terms and conditions of outstanding loans and borrowings were as follows

Company	Currency	Year of maturity	2007 Carrying value £m	2006 Carrying value £m
Borrowings in fair value hedge relationships				
6 45% 500m bond	USD	2008	**255 7**	291 7
5 375% 350m bond	USD	2019	**170 6**	190 4
4 55% 250m bond	USD	2018	**113 7**	126 1
Borrowings designated at fair value through profit and loss				
0 705% 3,000m bond	JPY	2008	**12 9**	14 7
Borrowings measured at amortised cost				
6 875% 400m bond	USD	2028	**200 6**	240 1
4 21% 10m bond	EUR	2008	**6 8**	7 0
0 24%+LIBOR 6 5m (floating) bond	GBP	2013	**6 5**	6 5
0 385%+LIBOR 10m (floating) bond	USD	2008	**5 1**	5 8
0 365%+LIBOR 10m (floating) bond	USD	2009	**5 1**	5 8
Long-term bank borrowings floating – 5 41%–5 608%	GBP	2009	**1 1**	0 9
Euro-commercial paper – 5 34%–5 65%	GBP	2007-2008	**65 9**	190 0
Euro-commercial paper – 3 8%–3 914%	EUR	2007-2008	**382 8**	13 9
Euro-commercial paper – 5 452%	USD	2007-2008	**2 9**	14 4
Committed facilities – drawn	GBP	2007	**–**	251 8
Amounts owed to subsidiary undertakings	GBP	n/a	**463 5**	–
			1,693 2	1,359 1

Notes

Base interest rates

LIBOR	London Interbank Offered Rate (Source British Bankers Association)
HIBOR	Hong Kong Interbank Offered Rate (Source Hong Kong Association of Banks)
EIB	European Investment Bank rate

Currency

GBP	pound sterling
EUR	euro
HKD	Hong Kong dollar
USD	United States dollar
JPY	Japanese yen

Index-linked debt

IL	Index-linked debt – This debt is adjusted for movements in the Retail Price Index with reference to a base Retail Price Index established at trade date
RPI	The UK general index of retail prices (for all items) as published by the Office for National Statistics (Jan 1987=100) as published by HM Government

Loans and borrowings are unsecured Funding raised in currencies other than sterling is generally swapped to sterling to match funding costs to income

The fair values of the company's financial instruments are shown in note 18

Borrowing facilities

The company had available committed bank facilities of £850 0 million (2006 £510 0 million) of which £847 2 million was unutilised at 31 March 2007 (2006 £255 4 million) The utilisation of £2 8 million as at 31 March 2007 represents guarantees against off-balance sheet liabilities detailed on page 33 As at 31 March 2006, the company had drawn £251 8 million in addition to the guarantees of £2 8 million Of the amounts unutilised, £80 0 million expires within one year (2006 £100 0 million), £50 0 million expires after one year but in less than two years (2006 £55 0 million), and the remaining £717 2 million expires in more than two years (2006 £100 4 million) Bank overdrafts are repayable on demand

18 Financial instruments

Exposure to credit, interest rate and foreign exchange risks arises in the normal course of the group's business Derivatives are used to hedge exposure to fluctuations in interest rates and foreign exchange rates

Risk management
The primary financial risks faced by the group are interest rate risk and currency risk The board has reviewed and agreed policies for managing each of these risks, as summarised below The board has also approved all of the classes of financial instruments used by the group The group's treasury function, which is authorised to conduct the day-to-day treasury activities of the group, reports at least annually to the board The use of financial derivatives is governed by the group's policies, which are approved by the board and provide written principles on the use of financial derivatives

All of the group's activities involve analysis, acceptance and management of some degree of risk or combination of risks The most important types of financial risk are credit risk, liquidity risk and market risk Market risk includes currency, interest rate and equity price risks

The group's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls and to monitor the risks and limits continually by means of reliable and up-to-date systems The group modifies and enhances its risk management policies and systems to reflect changes in markets and products The board formulates a high level group risk management policy, monitors risk and receives reports that allow it to review the effectiveness of the group's risk management policy

Credit risk
Credit risk is the risk that financial loss arises from the failure of a customer or counterparty to meet its financial obligations under a contract It arises principally from lending, trade finance and leasing activities The group has dedicated standards, policies and procedures to control and monitor all such risks

The counterparties under these activities consist of financial institutions and other bodies with good credit ratings Although the group is potentially exposed to credit loss in the event of non-performance by these counterparties, credit risk is controlled through credit rating reviews and by limiting the total amount of exposure to any one party Management does not anticipate that any counterparty will fail to meet its obligations

The group does not believe that it is exposed to any material concentrations of credit risk The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivatives, in the balance sheet

Liquidity risk
Liquidity risk is the risk that the group will not have sufficient funds to meet its financial obligations or commitments The group maintains a strong liquidity position and manages the liquidity profile of its assets, liabilities and commitments so that cashflows are appropriately balanced and all financial obligations are met when due

Market risk
Market risk is the risk that movements in market rates, including foreign exchange rates, interest rates, equity and commodity prices will reduce the group's income The management of market risk is undertaken using limits approved by the chief financial officer under delegated authority from the board

The group borrows in the major global debt markets in a range of currencies at both fixed and floating rates of interest, using derivatives, where appropriate, to generate the desired effective currency profile and interest basis

Interest rate risk
The group's fixed rate borrowings are exposed to a risk of change in their fair value due to changes in interest rates The group's floating rate borrowings are exposed to a risk of change in cashflows due to changes in interest rates Investments in equity securities and short-term receivables and payables are not exposed to interest rate risk

The group uses interest rate swap contracts and financial futures to hedge these exposures

Under an interest rate swap, the group agrees with another party to exchange at specific intervals the difference between fixed rate and floating rate interest amounts calculated by reference to an agreed notional principal amount The notional principal of these instruments reflects the extent of the group's involvement in the instruments, but does not represent its exposure to credit risk, which is assessed by reference to the fair value

Non-current asset investments, trade and other receivables and trade and other payables are not directly exposed to interest rate risk

Currency risk
The group is exposed to currency risk on borrowings that are denominated in currencies other than the respective functional currencies of group entities The group utilises cross-currency swap contracts to hedge this exposure

Under a cross-currency swap, the group agrees with another party to exchange the principal amount of two currencies, together with interest amounts in the two currencies agreed by reference to a specific interest rate basis and the principal amount The principal of these instruments reflects the extent of the group's involvement in the instruments, but does not represent its exposure to credit risk, which is assessed by reference to the fair value

As noted above, the group uses derivatives to manage its exposure to currency risk on its borrowings Subsidiary undertakings make no significant sales or purchases in currencies other than their functional currencies Accordingly, the group has no material unhedged foreign currency exposures

Hedging
The group adopts a policy of ensuring that approximately 80 per cent of its borrowings is on a fixed rate basis over the five-year regulatory period Interest rate derivative financial instruments have been entered into to achieve an appropriate mix of fixed and floating rate exposure The residual short-term interest rate exposure is hedged using exchange traded financial futures

18 Financial instruments continued

The derivative financial instruments utilised by the group to achieve the hedging of these exposures can be summarised as follows

Interest rate swaps
Interest rate swaps are used to manage the interest rate profile of borrowings in order to reduce the financial risk to the group from potential future changes in medium-term interest rates

Interest rate and cross-currency swaps are denominated in sterling, United States dollars, Japanese yen, euro and Hong Kong dollars and mature between 2007 and 2035 Swaps are executed in conjunction with bond issues to ensure that the combined cashflows equate to floating sterling In these cases, interest on the swap is received to coincide with bond interest payments which are generally annual on fixed rate bonds Interest received on these swaps will match the nominal interest paid on the bonds, these rates are detailed in borrowings note 17 'Terms and debt repayment schedule' The floating sterling side payable on these swaps will generally occur semi annually Taking into account the latest fixings prior to year end, rates range from 5 73 to 7 30 per cent on these floating legs Additionally, swaps are executed to fix floating rate cashflows over the regulatory period Cashflows on these regulatory swaps will coincide with the floating cashflow it is intended to fix Interest received on these regulatory swaps is floating sterling and the fixed payable side ranges from 4 81 to 5 67 per cent

Financial futures
Financial futures are used to manage the group's exposure to possible future changes in short-term interest rates The financial future contracts are traded on the London International Financial Futures and Options Exchange

Forward contracts
The group generally hedges foreign exchange transaction exposures up to one year forward Hedges are put in place using forward contracts at the time that the forecast exposure becomes reasonably certain

Cross-currency swaps
The group uses cross-currency swaps to hedge currency exposures where debt is raised in one currency to fund business activity in a different currency

The group does not use derivative financial instruments for speculative purposes, and has not pledged collateral in relation to any of its derivative instruments The derivative financial instruments do not contain any early settlement or termination options

Those derivative instruments that are not part of a designated and effective hedging relationship are classified as held for trading and are therefore measured at fair value through profit and loss Where fair value hedges exist they are designated as a hedge of interest rate risk and/or currency risk

The cashflow hedge relates to the management of cashflow on a particular floating rate loan over the regulatory period to 2010 The group largely manages all of its financing cashflows over the observed five-year regulatory period, however, the majority of these economic hedges do not qualify for hedge accounting as they would be overlaid onto transactions which are already within fair value hedge relationships

18 Financial instruments continued

Effective interest rate and repricing analysis

In respect of interest bearing financial liabilities, the following tables indicate their average effective interest rates at the reporting date and the periods in which they mature or, if earlier, reprice

Group At 31 March 2007		Average effective interest rate %	Total £m	1 year or less £m	1-2 years £m	2-3 years £m	3-4 years £m	4-5 years £m	More than 5 years £m
Borrowings in hedge relationships									
Fixed rate instruments									
5 625% GBP 300m bond due 2027		5 69	295 9	–	–	–	–	–	295 9
5% GBP 200m bond due 2035		5 12	188 4	–	–	–	–	–	188 4
5 25% GBP 150m bond due 2010		5 34	145 8	–	–	145 8	–	–	–
5 375% GBP 150m bond due 2018		5 44	142 9	–	–	–	–	–	142 9
6 625% EUR 1,000m bond due 2007		6 49	673 8	673 8	–	–	–	–	–
4 875% EUR 600m bond due 2009		5 10	403 4	–	403 4	–	–	–	–
4 25% EUR 500m bond due 2020		4 38	321 7	–	–	–	–	–	321 7
6 45% USD 500m bond due 2008		6 64	255 7	–	255 7	–	–	–	–
5 375% USD 350m bond due 2019		5 57	170 6	–	–	–	–	–	170 6
4 55% USD 250m bond due 2018		4 71	113 7	–	–	–	–	–	113 7
5 02% JPY 10,000m reverse dual currency bond due 2029		5 02	53 9	–	–	–	–	–	53 9
Effect of swaps	(4)	6 13	–	2,092 0	(659 1)	(145 8)	–	–	(1,287 1)
Floating rate instruments									
EIB 90m loan due 2013	(1)	5 60	90 0	90 0	–	–	–	–	–
HKD 150m bond due 2007	(1)	4 71	9 8	9 8	–	–	–	–	–
Effect of swaps	(4)	4 99	–	(90 0)	–	90 0	–	–	–
			2,865 6	2,775 6	–	90 0	–	–	–
Borrowings designated at fair value through profit and loss									
Fixed rate instruments									
8 875% GBP 250m bond due 2026		5 87	344 7	–	–	–	–	–	344 7
6 875% USD 400m bond due 2028		7 10	217 5	–	–	–	–	–	217 5
0 705% JPY 3,000m bond due 2008		0 71	12 9	12 9	–	–	–	–	–
1 135% JPY 3,000m bond due 2013		1 14	12 5	–	–	–	–	–	12 5
Effect of swaps	(4)	6 59	–	574 7	–	–	–	–	(574 7)
			587 6	587 6	–	–	–	–	–
Borrowings measured at amortised cost									
Fixed rate instruments									
8 875% GBP 200m bond due 2026		9 16	194 9	–	–	–	–	–	194 9
4 21% EUR 10m bond due 2008		4 26	6 8	–	6 8	–	–	–	–
Commission for the New Towns loan – 14 83%		11 40	31 2	0 2	0 2	0 2	0 2	0 3	30 1
Long-term bank borrowings		6 72	210 0	205 0	5 0	–	–	–	–
Euro-commercial paper	(3)	5 60	451 6	451 6	–	–	–	–	–
Other debt		6 31	76 9	14 7	–	0 1	–	–	62 1
Floating rate instruments									
USD 10m bond due 2008		5 74	5 1	5 1	–	–	–	–	–
USD 10m bond due 2009		5 73	5 1	5 1	–	–	–	–	–
Long-term bank borrowings	(1)	5 56	253 0	253 0	–	–	–	–	–
Finance lease obligations		4 26	75 3	75 3	–	–	–	–	–
GBP 6 5m bond due 2013	(1)	5 94	6 5	6 5	–	–	–	–	–
Bank overdrafts	(2)	Various	62 6	62 6	–	–	–	–	–
Other debt	(3)	Various	134 9	134 9	–	–	–	–	–
Loan notes		4 56	1 2	1 2	–	–	–	–	–
			1,515 1	1,215 2	12 0	0 3	0 2	0 3	287 1

18 Financial instruments continued

Group At 31 March 2007		Average effective interest rate %	Total £m	1 year or less £m	1-2 years £m	2-3 years £m	3-4 years £m	4-5 years £m	More than 5 years £m
Borrowings measured at amortised cost (continued)									
Index linked instruments									
1 97% GBP 200m IL bank loan due 2016	(5)	1 97+RPI	200 7	200 7	–	–	–	–	–
1 9799% GBP 100m IL bond due 2035	(5)	1 9799+RPI	104 7	104 7	–	–	–	–	–
1 7829% GBP 100m IL bond due 2040	(5)	1 7829+RPI	103 6	103 6	–	–	–	–	–
1 5802% GBP 100m IL bond due 2042	(5)	1 5802+RPI	103 3	103 3	–	–	–	–	–
1 4746% GBP 100m IL bond due 2046	(5)	1 4746+RPI	103 0	103 0	–	–	–	–	–
1 847% GBP 100m IL bond due 2056	(5)	1 847+RPI	102 5	102 5	–	–	–	–	–
1 815% GBP 100m IL bond due 2056	(5)	1 815+RPI	102 1	102 1	–	–	–	–	–
1 662% GBP 100m IL bond due 2056	(5)	1 662+RPI	101 9	101 9	–	–	–	–	–
3 375% GBP 50m IL bond due 2032	(5)	3 375+RPI	55 4	55 4	–	–	–	–	–
1 3258% GBP 50m IL bond due 2041	(5)	1 3258+RPI	51 7	51 7	–	–	–	–	–
1 397% GBP 50m IL bond due 2046	(5)	1 397+RPI	51 6	51 6	–	–	–	–	–
1 5366% GBP 50m IL bond due 2043	(5)	1 5366+RPI	51 5	51 5	–	–	–	–	–
1 7937% GBP 50m IL bond due 2049	(5)	1 7937+RPI	51 4	51 4	–	–	–	–	–
1 5865% GBP 50m IL bond due 2056	(5)	1 5865+RPI	50 9	50 9	–	–	–	–	–
1 556% GBP 50m IL bond due 2056	(5)	1 556+RPI	50 6	50 6	–	–	–	–	–
1 435% GBP 50m IL bond due 2056	(5)	1 435+RPI	50 5	50 5	–	–	–	–	–
1 3805% GBP 35m IL bond due 2056	(5)	1 3805+RPI	35 3	35 3	–	–	–	–	–
1 591% GBP 25m IL bond due 2056	(5)	1 591+RPI	25 4	25 4	–	–	–	–	–
			1,396 1	1,396 1	–	–	–	–	–
Effect of a fixed hedge for the term of the regulatory business plan		5 21	–	(3,378 5)	–	2,239 7	1,138 8	–	–
Total borrowings			**6,364 4**	**2,596 0**	**12 0**	**2,330 0**	**1,139 0**	**0 3**	**287 1**

Group At 31 March 2006		Average effective interest rate %	Total £m	1 year or less £m	1-2 years £m	2-3 years £m	3-4 years £m	4-5 years £m	More than 5 years £m
Borrowings in hedge relationships									
Fixed rate instruments									
5 625% GBP 300m bond due 2027		5 69	317 6	–	–	–	–	–	317 6
5% GBP 200m bond due 2035		5 12	202 4	–	–	–	–	–	202 4
5 25% GBP 150m bond due 2010		5 34	148 9	–	–	–	148 9	–	–
5 375% GBP 150m bond due 2018		5 44	150 8	–	–	–	–	–	150 8
6 625% EUR 1,000m bond due 2007		6 49	690 9	–	690 9	–	–	–	–
4 875% EUR 600m bond due 2009		5 10	420 4	–	–	420 4	–	–	–
4 25% EUR 500m bond due 2020		4 38	337 6	–	–	–	–	–	337 6
6 45% USD 500m bond due 2008		6 64	291 7	–	–	291 7	–	–	–
5 375% USD 350m bond due 2019		5 57	190 4	–	–	–	–	–	190 4
4 55% USD 250m bond due 2018		4 71	126 1	–	–	–	–	–	126 1
5 02% JPY 10,000m reverse dual currency bond due 2029		5 02	60 8	–	–	–	–	–	60 8
Effect of swaps	(4)	5 26	–	2,937 6	(690 9)	(712 1)	(148 9)	–	(1,385 7)
Floating rate instruments									
EIB 90m loan due 2013		4 65	90 1	90 1	–	–	–	–	–
HKD 150m bond due 2007		4 50	11 1	11 1	–	–	–	–	–
Effect of swaps	(4)	4 83	–	(90 1)	–	–	90 1	–	–
			3,038 8	2,948 7	–	–	90 1	–	–
Borrowings designated at fair value through profit and loss									
Fixed rate instruments									
8 875% GBP 250m bond due 2026		5 87	358 9	–	–	–	–	–	358 9
6 875% USD 400m bond due 2028		7 10	240 1	–	–	–	–	–	240 1
0 705% JPY 3,000m bond due 2008		0 71	14 7	–	14 7	–	–	–	–
1 135% JPY 3 000m bond due 2013		1 14	13 6	–	–	–	–	–	13 6
0 75% JPY 1,000m bond due 2007		0 75	4 9	4 9	–	–	–	–	–
Effect of swaps	(4)	5 52	–	627 3	(14 7)	–	–	–	(612 6)
			632 2	632 2	–	–	–	–	–

18 Financial instruments continued

Group At 31 March 2006	Average effective interest rate %	Total £m	1 year or less £m	1-2 years £m	2-3 years £m	3-4 years £m	4-5 years £m	More than 5 years £m
Borrowings measured at amortised cost								
Fixed rate instruments								
8 875% GBP 200m bond due 2026	9 16	194 9	–	–	–	–	–	194 9
4 21% EUR 10m bond due 2008	4 26	7 0	–	–	7 0	–	–	–
Commission for the New Towns loan – 14 83%	11 40	31 4	0 3	0 2	0 2	0 2	0 2	30 3
Long-term bank borrowings	6 89	223 6	13 5	205 0	5 1	–	–	–
Euro-commercial paper [5]	4 59	218 3	218 3	–	–	–	–	–
Other debt	6 66	97 7	22 0	–	–	–	–	75 7
0 765% JPY 3,000m bond due 2006	0 77	14 7	14 7	–	–	–	–	–
Floating rate instruments								
USD 10m bond due 2008	5 35	5 8	5 8	–	–	–	–	–
USD 10m bond due 2009	5 03	5 8	5 8	–	–	–	–	–
Long-term bank borrowings	4 79	256 0	256 0	–	–	–	–	–
Finance lease obligations	4 47	80 5	80 5	–	–	–	–	–
GBP 6 5m bond due 2013	4 88	6 5	6 5	–	–	–	–	–
Committed facilities – drawn	4 79	251 8	251 8	–	–	–	–	–
Bank overdrafts	Various	69 6	69 6	–	–	–	–	–
Other debt	Various	99 2	99 2	–	–	–	–	–
Loan notes	3 585	9 4	9 4	–	–	–	–	–
		1,572 2	1 053 4	205 2	12 3	0 2	0 2	300 9
Index linked instruments								
1 5802% GBP 100m IL bond due 2042 [5]	1 5082+RPI	100 0	100 0	–	–	–	–	–
1 7829% GBP 100m IL bond due 2040 [5]	1 7829+RPI	100 5	100 5	–	–	–	–	–
1 9799% GBP 100m IL bond due 2035 [5]	1 9799+RPI	101 5	101 5	–	–	–	–	–
3 375% GBP 50m IL bond due 2032 [5]	3 375+RPI	54 8	54 8	–	–	–	–	–
1 3258% GBP 50m IL bond due 2041 [5]	1 3258+RPI	50 1	50 1	–	–	–	–	–
1 397% GBP 50m IL bond due 2046 [5]	1 397+RPI	50 1	50 1	–	–	–	–	–
		457 0	457 0	–	–	–	–	–
Effect of a fixed hedge for the term of the regulatory business plan	5 21	–	(3,378 4)	–	–	2,239 6	1,138 8	–
Total borrowings		5 700 2	1,712 9	205 2	12 3	2,329 9	1,139 0	300 9

18 Financial instruments continued

Company At 31 March 2007		Average effective interest rate %	Total £m	1 year or less £m	1-2 years £m	2-3 years £m	3-4 years £m	4-5 years £m	More than 5 years £m
Borrowings in hedge relationships									
Fixed rate instruments									
6 45% USD 500m bond due 2008		6 64	255 7	–	255 7	–	–	–	–
5 375% USD 350m bond due 2019		5 57	170 6	–	–	–	–	–	170 6
4 55% USD 250m bond due 2018		4 71	113 7	–	–	–	–	–	113 7
Effect of swaps	(4)	5 97	–	540 0	(255 7)	–	–	–	(284 3)
			540 0	540 0	–	–	–	–	–
Borrowings designated at fair value through profit and loss									
Fixed rate instruments									
0 705% JPY 3,000m bond due 2008		0 71	12 9	12 9	–	–	–	–	–
Effect of swaps	(4)	6 11	–	–	–	–	–	–	–
			12 9	12 9	–	–	–	–	–
Borrowings measured at amortised cost									
Fixed rate instruments									
6 875% USD 400m bond due 2028		7 10	200 6	–	–	–	–	–	200 6
4 21% EUR 10m bond due 2008		4 26	6 8	–	6 8	–	–	–	–
Commercial paper	(6)	5 60	451 6	451 6	–	–	–	–	–
Floating rate instruments									
USD 10m bond due 2008		5 74	5 1	5 1	–	–	–	–	–
USD 10m bond due 2009		5 73	5 1	5 1	–	–	–	–	–
Long-term bank borrowings	(1)	3 59	1 1	1 1	–	–	–	–	–
GBP 6 5m bond due 2013	(1)	5 94	6 5	6 5	–	–	–	–	–
			676 8	469 4	6 8	–	–	–	200 6
Effect of a fixed hedge for the term of the regulatory business plan		4 88	–	(190 0)	–	190 0	–	–	–
Total external borrowings			1 229 7	832 3	6 8	190 0	–	–	200 6
Amounts owed to subsidiary undertakings			463 5	463 5	–	–	–	–	–
Total borrowings			**1,693 2**	**1,295 8**	**6 8**	**190 0**	**–**	**–**	**200 6**

18 Financial instruments continued

Company At 31 March 2006		Average effective interest rate %	Total £m	1 year or less £m	1-2 years £m	2-3 years £m	3-4 years £m	4 5 years £m	More than 5 years £m
Borrowings in hedge relationships									
Fixed rate instruments									
6 45% USD 500m bond due 2008		6 64	291 7	–	–	291 7	–	–	–
5 375% USD 350m bond due 2019		5 57	190 4	–	–	–	–	–	190 4
4 55% USD 250m bond due 2018		4 71	126 1	–	–	–	–	–	126 1
Effect of swaps	(4)	5 17	–	608 2	–	(291 7)	–	–	(316 5)
			608 2	608 2	–	–	–	–	–
Borrowings designated at fair value through profit and loss									
Fixed rate instruments									
0 705% JPY 3,000m bond due 2008		0 71	14 7	–	14 7	–	–	–	–
Effect of swaps	(4)	5 06	–	14 7	(14 7)	–	–	–	–
			14 7	14 7	–	–	–	–	–
Borrowings measured at amortised cost									
Fixed rate instruments									
6 875% USD 400m bond due 2028		7 10	240 1	–	–	–	–	–	240 1
4 21% EUR 10m bond due 2008		4 26	7 0	–	–	7 0	–	–	–
Euro-commercial paper	(6)	4 59	218 3	218 3	–	–	–	–	–
Floating rate instruments									
USD 10m bond due 2008		5 35	5 8	5 8	–	–	–	–	–
USD 10m bond due 2009		5 03	5 8	5 8	–	–	–	–	–
Long-term bank borrowings	(1)	Various	0 9	0 9	–	–	–	–	–
GBP 6 5m bond due 2013	(1)	4 88	6 5	6 5	–	–	–	–	–
Committed facilities – drawn		4 79	251 8	251 8	–	–	–	–	–
			736 2	489 1	–	7 0	–	–	240 1
Effect of a fixed hedge for the term of the regulatory business plan		4 88	–	(190 0)	–	–	190 0	–	–
Total borrowings			1,359 1	922 0	–	7 0	190 0	–	240 1

Notes.

(1) Where a floating rate is quoted the latest fixing is quoted here including any appropriate margins

(2) This represents a number of bank balances across the group with various floating rates

(3) This represents a number of floating loans where interest is priced against euribor LIBOR and short term AUD bank rates

(4) The rate quoted here is the last GBP LIBOR fixing plus any margin which is payable under the relevant swap The interest receivable on these swaps will be the coupon due on the corresponding debt item

(5) The debt balance on these index linked items and thus the balance upon which interest is paid at the quoted coupon, is adjusted for movements in the Retail Price Index established at the trade date The corresponding annualised inflation rate for the year ended 31 March 2007 was 4 8 per cent (2006 2 4 per cent)

(6) Where euro-commercial paper is denominated in currency other than GBP the rate quoted here includes the effect of associated cross-currency swaps converting to GBP reference rate

Sensitivity analysis

In managing interest rate and currency risks the group aims to reduce the impact of short-term fluctuations on the group's earnings Over the longer term, permanent changes in foreign exchange and interest rates will have an impact on profit

The analysis in the table below illustrates the sensitivity of the market value of the group's financial instruments to changes in interest rates The analysis assumes a general increase or decrease of one percentage point in interest rates for all maturities and currencies from their levels at 31 March with all other variables held constant

Group	Market value 31 March 2007 £m	+1% movement in interest rate £m	–1% movement in interest rate £m
Interest rate movement			
Long-term debt	**(4,944 2)**	**519 7**	**(679 3)**
Derivatives	**(164 6)**	**(119 7)**	**150 0**
Cash and short-term deposits	**2,407 0**	**(2 0)**	**1 7**

	Market value 31 March 2006 £m	+1% movement in interest rate £m	–1% movement in interest rate £m
Interest rate movement			
Long-term debt	(5,289 1)	184 8	(213 9)
Derivatives	(44 3)	(67 3)	86 8
Cash and short-term deposits	1,513 5	(0 6)	0 6

18 Financial instruments continued

Company	Market value 31 March 2007 £m	+1% movement in interest rate £m	-1% movement in interest rate £m
Interest rate movement			
Long-term debt	**(795 7)**	**48 0**	**(54 9)**
Derivatives	**(88 6)**	**(20 8)**	**23 5**
Cash and short-term deposits	**336 8**	**(0 1)**	**-**

	Market value 31 March 2006 £m	+1% movement in interest rate £m	-1% movement in interest rate £m
Interest rate movement			
Long-term debt	(889 5)	66 9	(76 5)
Derivatives	(38 5)	(27 1)	30 4
Cash and short-term deposits	120 4	-	-

Fair values

The fair values of financial assets and liabilities, together with the carrying amounts shown in the balance sheet, are as follows

Group			2007 Carrying value £m		2007 Fair value £m		2006 Carrying value £m		2006 Fair value £m
Financial assets									
Non-current assets									
Available for sale investments			**201 8**		**201 8**		170 7		170 7
Trade and other receivables			**21 6**		**21 6**		22 0		22 0
Derivative financial instruments									
Fair value hedge derivatives – swaps	(1)	**15 2**		**15 2**		27 6		27 6	
Option over THUS Group plc shares		**-**		**-**		13 2		13 2	
			15 2		**15 2**		40 8		40 8
Current assets									
Trade and other receivables	(2)		**418 2**		**418 2**		490 1		490 1
Available for sale investments			**38 5**		**38 5**		29 7		29 7
Cash and short-term deposits	(2)		**2,403 3**		**2,407 0**		1,513 5		1,513 5
Derivative financial instruments									
Held for trading derivatives – swaps		**52 4**		**52 4**		48 9		48 9	
Option over THUS Group plc shares		**8 6**		**8 6**		-		-	
			61 0		**61 0**		48 9		48 9
Financial liabilities									
Non-current liabilities									
Trade and other payables			**(414 3)**		**(414 3)**		(383 7)		(383 7)
Borrowings									
Financial liabilities designated at fair value through profit and loss		**(574 7)**		**(574 7)**		(627 3)		(627 3)	
Financial liabilities in a hedged relationship									
Fair value hedge	(3)	**(2,092 0)**		**(2,140 2)**		(2,948 7)		(3,001 7)	
Cashflow hedge	(3)	**(90 0)**		**(90 4)**		(90 1)		(90 0)	
Other financial liabilities	(3)	**(2,098 2)**		**(2,138 9)**		(1,415 0)		(1,570 1)	
			(4,854 9)		**(4,944 2)**		(5 081 1)		(5,289 1)
Derivative financial instruments									
Fair value hedge derivatives – swaps			**(173 5)**		**(173 5)**		(57 6)		(57 6)
Current liabilities									
Trade and other payables	(2)		**(749 2)**		**(749 2)**		(855 1)		(855 1)
Borrowings									
Financial liabilities designated at fair value through profit and loss		**(12 9)**		**(12 9)**		(4 9)		(4 9)	
Financial liabilities in a hedged relationship									
Fair value hedge	(3)	**(683 6)**		**(715 7)**		-		-	
Other financial liabilities	(3)	**(813 0)**		**(820 7)**		(614 2)		(614 2)	
			(1,509 5)		**(1,549 3)**		(619 1)		(619 1)
Derivative financial instruments									
Held for trading derivatives – swaps			**(67 3)**		**(67 3)**		(76 4)		(76 4)
Adjustment for accrued interest	(2)(3)		**-**		**57 5**		-		-
			(4,609 1)		**(4,677 0)**		(4,757 3)		(4,965 3)

18 Financial instruments continued

In respect of the total change in fair value of financial liabilities designated as at fair value through profit and loss of £44 6 million gain (2006 £26 8 million loss), £8 3 million loss (2006 £3 0 million loss) is attributable to changes in credit risk

Company			2007 Carrying value £m		2007 Fair value £m		2006 Carrying value £m		2006 Fair value £m
Current assets									
Trade and other receivables	(2)		993 6		993 6		1,130 6		1,130 6
Cash and short-term deposits	(2)		336 7		336 8		120 4		120 4
Derivative financial instruments									
Held for trading derivatives – swaps		10 2		10 2		–		–	
Option over THUS Group plc shares		8 6		8 6		–		–	
			18 8		18 8				
Financial liabilities									
Non-current liabilities									
Borrowings									
Financial liabilities designated at fair value through profit and loss		–		–		(14 7)		(14 7)	
Financial liabilities in a hedged relationship									
Fair value hedge	(3)	(540 0)		(553 3)		(608 2)		(608 2)	
Other financial liabilities	(3)	(225 2)		(242 4)		(258 0)		(266 6)	
			(765 2)		(795 7)		(880 9)		(889 5)
Derivative financial instruments									
Fair value hedge derivatives			(100 1)		(100 1)		(32 7)		(32 7)
Current liabilities									
Trade and other payables	(3)		(502 5)		(502 5)		(550 8)		(550 8)
Borrowings									
Financial liabilities designated at fair value through profit and loss		(12 9)		(12 9)		–		–	
Other financial liabilities	(3)	(915 1)		(915 1)		(478 2)		(478 2)	
			(928 0)		(928 0)		(478 2)		(478 2)
Derivative financial instruments									
Held for trading derivatives – swaps			(7 3)		(7 3)		(5 8)		(5 8)
Adjustment for accrued interest	(2)(3)		–		13 3		–		–
			(954 0)		(971 1)		(697 4)		(706 0)

Note

(1) Included in the group fair value table is an asset relating to a cashflow hedge the notional and fair value of which is inconsequential Within the year ended 31 March 2007 a movement in the fair value of the derivative of £2 8 million gain (2006 £0 9 million loss) was recognised and taken to reserves gross of tax

(2) The fair value price quoted includes £4 0 million interest receivable (company £0 1 million) This interest receivable is also included within the fair value of trade and other receivables The impact on the total fair value of financial instruments has been removed in the adjustment for accrued interest

(3) Fair value prices quoted include accrued interest of £61 5 million in respect of the associated borrowings (company £13 4 million) This accrued interest is also included in the fair value of trade and other payables The impact on the total fair value of financial instruments has been removed in the adjustment for accrued interest

19 Retirement benefit obligations

The group participates in a number of pension schemes principally in the UK The two major schemes are funded defined benefit schemes – the United Utilities Pension Scheme (UUPS) and the United Utilities Group of the Electricity Supply Pension Scheme (ESPS) (the 'Schemes'), both of which are closed to new employees UUPS also includes a defined contribution section which constitutes less than 0 5 per cent of the total asset value The assets of these Schemes are held in trust funds independent of the group's finances

The last actuarial valuations of the Schemes were carried out as at 31 March 2006 These valuations have been updated to take account of the requirements of IAS 19 'Employee Benefits' in order to assess the position at 31 March 2007 by projecting forward from 31 March 2006, and have been performed by an independent actuary, Mercer Human Resource Consulting

On 31 March 2005, the group made lump-sum payments of £216 0 million and £103 5 million to UUPS and ESPS respectively The payments were in lieu of the estimated company contributions that were expected to have been payable for defined benefit members over the five years from 1 April 2005 Subject to the results of the actuarial valuations at 31 March 2007, company contributions are expected to resume from 1 April 2010 In the meantime, the group will continue to pay contributions in respect of the defined contribution members and insurance premiums Other payments will be made by the group in accordance with the funding agreements between the trustees and the group

The group did not make any significant contributions to the Schemes for the year ended 31 March 2007 and does not expect to make any contributions over the year to 31 March 2008 During the year, the group contributed to its section of the Essex County Council Pension Fund

The group also operates a series of unfunded, unregistered retirement benefit schemes The cost of the unfunded, unregistered retirement benefit schemes is included in the total pension cost, on a basis consistent with IAS 19 and the assumptions set out below In accordance with these unfunded arrangements, the group made payments directly to former directors, including lump sum payments, of £nil in the year ended 31 March 2007 (2006 £2 8 million) However, the group made contributions to the Schemes of £5 1 million (2006 £nil) on behalf of the unfunded, unregistered retirement benefit schemes

19 Retirement benefit obligations continued

The total defined benefit pension cost for the period was £11 9 million (2006 £19 4 million) A pension surplus of £62 2 million is included in the balance sheet at 31 March 2007 (2006 £19 3 million) Information about the pension arrangements for executive directors is contained in the directors' remuneration report

The main financial assumptions used by the actuary were as follows

Group and Company	2007 %	2006 %
Discount rate - UUPS	5 20	4 90
Discount rate - ESPS	5 30	4 90
Expected return on assets - UUPS	6 50	6 20
Expected return on assets - ESPS	6 30	5 90
Pensionable salary growth - UUPS	3 95	3 75
Pensionable salary growth - ESPS	4 00	3 80
Pension increases	3 00	2 80
Price inflation	3 00	2 80

The current male life expectancies at age 60 underlying the value of the accrued liabilities for the Schemes are

Group and Company	2007 years	2006 years
Retired member	23 8	22 5
Non-retired member	25 9	24 8

Recent studies have shown faster rates of life expectancy improvement than had previously been expected Studies have also illustrated that mortality rates vary significantly according to the demographics of the Schemes' members These factors have been taken into account in the calculation of the defined benefit obligations of the group

At 31 March, the fair value of the Schemes' assets and liabilities recognised in the balance sheet were as follows

Group	Schemes' assets %	2007 £m	Schemes' assets %	2006 £m
Equities	65 0	1,759 3	66 6	1,825 1
Gilts	20 4	550 7	22 3	611 1
Bonds	13 6	368 9	11 0	301 4
Property	-	-	0 1	2 7
Cash	1 0	27 1	-	-
Total fair value of assets	100 0	2,706 0	100 0	2 740 3
Present value of defined benefit obligation		(2,643 8)		(2,721 0)
Net retirement benefit surplus		62 2		19 3

Company	Schemes' assets %	2007 £m	Schemes' assets %	2006 £m
Equities	65 0	259 3	66 6	79 3
Gilts	20 4	81 4	22 3	26 5
Bonds	13 6	54 2	11 0	13 1
Property	-	-	0 1	0 1
Cash	1 0	4 0	-	-
Total fair value of assets	100 0	398 9	100 0	119 0
Present value of defined benefit obligation		(388 8)		(120 2)
Net retirement benefit surplus/(obligation)		10 1		(1 2)

To develop the expected long-term rate of return on asset assumptions, the group considered the level of expected returns on risk-free investments, the historical level of the risk premium associated with the other asset classes in which the portfolio is invested and the expectations for future returns of each asset class The expected return for each asset class was then weighted based on the actual asset allocation to develop the expected long-term return on asset assumptions for the portfolio The group's actual return on Schemes' assets was a gain of £107 5 million (2006 £571 0 million) and the company's actual return on the Schemes' assets was a loss of £39 3 million (2006 £21 4 million gain)

19 Retirement benefit obligations continued

Movements in the present value of the defined benefit obligations are as follows

	Group		Company	
	2007 £m	2006 £m	**2007 £m**	2006 £m
At 1 April	**(2,721 0)**	(2,382 3)	**(120 2)**	(103 1)
Interest cost on Schemes' obligations	**(130 0)**	(130 4)	**(6 0)**	(3 3)
Actuarial gains/(losses)	**99 3**	(301 1)	**26 3**	(12 4)
Curtailments/settlements	**68 1**	62 6	**-**	-
Member contributions	**(13 7)**	(14 5)	**(0 3)**	-
Benefits paid	**103 4**	103 3	**29 4**	0 2
Transfer on disposal of businesses	**-**	-	**(316 4)**	-
Current service cost	**(48 8)**	(53 5)	**(1 4)**	(1 6)
Past service costs	**(1 1)**	(5 1)	**(0 2)**	-
At 31 March	**(2,643 8)**	(2,721 0)	**(388 8)**	(120 2)

At 31 March 2007, £7 9 million (2006 £12 8 million) of the defined benefit obligation related to unfunded benefit plans

Movements in the fair value of the Schemes' assets were as follows

	Group		Company	
	2007 £m	2006 £m	**2007 £m**	2006 £m
At 1 April	**2,740 3**	2 297 7	**119 0**	94 9
Expected return on Schemes' assets	**160 3**	150 7	**8 4**	3 8
Actuarial (losses)/gains	**(52 8)**	420 3	**(47 7)**	17 6
Curtailments/settlements	**(60 4)**	(43 7)	**-**	-
Member contributions	**13 7**	14 5	**0 3**	-
Benefits paid	**(103 4)**	(103 3)	**(29 4)**	(0 2)
Transfer on disposal of businesses	**-**	-	**343 2**	-
Company contributions	**8 3**	4 1	**5 1**	2 9
At 31 March	**2,706 0**	2,740 3	**398 9**	119 0

The net pension expense before taxation recognised in the income statement in respect of the defined benefit schemes is summarised as follows

						Group
	Continuing operations	**Discontinued operations**	**Total**	Continuing operations	Discontinued operations	Total
			2007 £m			2006 £m
Current service cost	**(41 7)**	**(7 1)**	**(48 8)**	(39 6)	(13 9)	(53 5)
Curtailments/settlements	**-**	**1 4**	**1 4**	-	10 6	10 6
Past service costs	**(0 6)**	**(0 5)**	**(1 1)**	(2 4)	(2 7)	(5 1)
Pension expense (charged)/credited to operating profit	**(42 3)**	**(6 2)**	**(48 5)**	(42 0)	(6 0)	(48 0)
Expected return on Schemes' assets	**138 0**	**22 3**	**160 3**	122 8	27 9	150 7
Interest on Schemes' obligations	**(112 9)**	**(17 1)**	**(130 0)**	(106 3)	(24 1)	(130 4)
Pension expense credited to investment income	**25 1**	**5 2**	**30 3**	16 5	3 8	20 3
Curtailments/settlements credited to loss on disposal	**-**	**6 3**	**6 3**	-	8 3	8 3
Net pension (charged)/credited before taxation	**(17 2)**	**5 3**	**(11 9)**	(25 5)	6 1	(19 4)

		Company
	2007 £m	2006 £m
Current service cost	**(1 4)**	(1 6)
Past service cost	**(0 2)**	-
Pension expense charged to operating profit	**(1 6)**	(1 6)
Expected return on Schemes' assets	**8 4**	3 8
Interest on Schemes' obligations	**(6 0)**	(3 3)
Pension expense credited to investment income	**2 4**	0 5
Transfer on disposal of businesses credited to income statement	**26 8**	-
Net pension credited/(charged) before taxation	**27 6**	(1 1)

19 Retirement benefit obligations continued

The reconciliation of the opening and closing balance sheet position is as follows

	Group 2007 £m	Group 2006 £m	Company 2007 £m	Company 2006 £m
At 1 April	**19 3**	(84 6)	**(1 2)**	(8 2)
Expenses recognised in the income statement	**(11 9)**	(19 4)	**0 8**	(1 1)
Transfer on disposal of businesses recognised in the income statement	**–**	–	**26 8**	–
Contributions paid	**8 3**	4 1	**5 1**	2 9
Actuarial gains/(losses) gross of taxation	**46 5**	119 2	**(21 4)**	5 2
At 31 March	**62 2**	19 3	**10 1**	(1 2)

Actuarial gains and losses are recognised directly in the statement of recognised income and expense At 31 March 2007, a cumulative pre-tax gain of £155 6 million (2006 £109 1 million) for the group, and a cumulative loss of £17 0 million (2006 £4 4 million gain) for the company was recorded directly in the statement of recognised income and expense

The history of the Schemes for the current and prior years is as follows

	Group 2007 £m	Group 2006 £m	Group 2005 £m	Company 2007 £m	Company 2006 £m	Company 2005 £m
Present value of defined benefit obligation	**(2,643 8)**	(2 721 0)	(2,382 3)	**(388 8)**	(120 2)	(103 1)
Fair value of Schemes' assets	**2,706 0**	2,740 3	2,297 7	**398 9**	119 0	94 9
Net retirement benefit surplus/(obligation)	**62 2**	19 3	(84 6)	**10 1**	(1 2)	(8 2)
Experience adjustments on Schemes' liabilities	**92 6**	–	(14 3)	**13 3**	–	(0 6)
Experience adjustments on Schemes assets	**(43 3)**	397 2	45 3	**(1 1)**	16 4	1 9

During the year, the group made £17 0 million (2006 £12 0 million) of contributions to defined contribution schemes, which are included in arriving at operating profit from continuing operations and a further £4 4 million (2006 £5 4 million) which are recognised within discontinued operations The company made £0 3 million (2006 £0 2 million) of contributions to defined contribution schemes

20 Deferred tax

The following are the major deferred tax liabilities and assets recognised by the group and company, and the movements thereon, during the current and prior year

	Accelerated tax depreciation £m	Retirement benefit obligations £m	Other £m	Group Total £m	Company Total £m
At 1 April 2005	1 460 0	(141 9)	19 2	1,337 3	3 1
Charged/(credited) to the income statement	96 8	–	(52 1)	44 7	(10 3)
Charged/(credited) to equity	–	35 8	0 8	36 6	(0 2)
Acquired in year	8 0	–	–	8 0	–
At 31 March 2006	1,564 8	(106 1)	(32 1)	1,426 6	(7 4)
Charged to the income statement	15 1	–	94 3	109 4	6 5
Charged/(credited) to equity	–	14 0	0 8	14 8	(6 4)
At 31 March 2007	**1,579 9**	**(92 1)**	**63 0**	**1,550 8**	**(7 3)**

Certain deferred tax assets and liabilities have been offset in accordance with IAS 12 'Income Taxes'

The Chancellor's 2007 budget proposed various changes to the rules for claiming tax allowances on capital expenditure, together with a reduction in the main corporate tax rate The impact of these changes on the group's future deferred tax position is currently under review

21 Provisions

	Group				Company		
	Restructuring £m	Onerous leases £m	Other £m	Total £m	Restructuring £m	Other £m	Total £m
At 1 April 2005	15 2	–	3 2	18 4	0 4	–	0 4
Charged to the income statement	25 5	–	3 2	28 7	–	–	–
Acquired in the year	2 3	13 6	23 9	39 8	–	–	–
Utilised in year	(24 6)	(1 6)	(7 6)	(33 8)	(0 4)	–	(0 4)
At 31 March 2006	18 4	12 0	22 7	53 1	–	–	–
Reclassification in the year	–	14 9	23 4	38 3	–	12 6	12 6
Charged to the income statement	5 0	–	1 8	6 8	–	2 0	2 0
Utilised in year	(13 0)	–	(14 9)	(27 9)	–	(0 1)	(0 1)
Disposed of in the year	(4 1)	(19 2)	(8 1)	(31 4)	–	–	–
At 31 March 2007	**6 3**	**7 7**	**24 9**	**38 9**	**–**	**14 5**	**14 5**

The directors have reviewed the liabilities of the group and, after due consideration of their nature, consider that it is appropriate to reclassify certain liabilities, in respect of potential legal claims against the group and the cost of vacant properties, from accruals to provisions The total effect is to increase provisions and decrease accruals and deferred income within trade and other payables by £38 3 million (company £12 6 million) during the year

The restructuring provision principally relates to severance and programme costs as a result of the group reorganisation and represents management's best estimate

The onerous lease provision relates to potential liabilities on vacant retail property where the group is the holder of the lead lease The provision is based on the net present value of future lease payments which run to 2020

Other provisions principally relate to legal claims against the group and represent management's best estimate of the value of settlement and costs It is estimated that these claims will be settled in more than one year

Provisions have been analysed between current and non-current as follows

				Group	Company
	Restructuring £m	Onerous leases £m	Other £m	Total £m	Other £m
At 31 March 2007					
Non-current	**–**	**7 7**	**22 7**	**30 4**	**12 5**
Current	**6 3**	**–**	**2 2**	**8 5**	**2 0**
	6 3	**7 7**	**24 9**	**38 9**	**14 5**
At 31 March 2006					
Non-current	–	9 3	7 3	16 6	–
Current	18 4	2 7	15 4	36 5	–
	18 4	12 0	22 7	53 1	–

22 Trade and other payables

	Group		Company	
Non-current	**2007 £m**	2006 £m	**2007 £m**	2006 £m
Deferred grants and contributions	**400 1**	347 3	**–**	–
Other creditors	**14 2**	36 4	**–**	–
	414 3	383 7	**–**	–

	Group		Company	
Current	**2007 £m**	2006 £m	**2007 £m**	2006 £m
Trade payables	**52 7**	87 9	**1 7**	–
Amounts owed to subsidiary undertakings	**–**	–	**455 5**	512 5
Amounts owed to related parties	**0 3**	1 5	**–**	–
Other tax and social security	**6 9**	11 5	**0 3**	–
Other creditors	**16 8**	2 0	**16 8**	1 0
Accruals and deferred income	**672 5**	752 2	**28 2**	37 3
	749 2	855 1	**502 5**	550 8

The average credit period taken for trade purchases is 23 days for the group (2006 45 days) and is 99 days (2006 100 days) for the company

22 Trade and other payables continued

The directors consider that the carrying amount of trade payables approximates to their fair value

Included in accruals and deferred income in respect of 2006 are accruals for interest relating to borrowings accounted for under the fair value option, borrowings in hedge relationships and amortised cost borrowings In 2007, the interest accruals in respect of borrowings accounted for under the fair value option have been included within the carrying value of the associated borrowings whilst the remaining interest accruals continue to be included in accruals and deferred income

Deferred grants and contributions

	2007 £m	2006 £m
At 1 April	**347 3**	313 4
Received in the year	**67 4**	45 5
Disposed of in the year	**(0 6)**	(0 2)
Credited to the income statement	**(14 0)**	(11 4)
At 31 March	**400 1**	347 3

Deferred grants are those amounts received under government grant schemes Deferred contributions are those amounts received from customers in respect of new connections to the network

23 Shareholders' equity

Group	Share capital £m	Share premium account £m	Revaluation reserve £m	Treasury shares £m	Cumulative exchange reserve £m	Retained earnings £m	Total £m
At 1 April 2005	716 2	1,038 7	158 8	(0 3)	3 7	222 5	2,139 6
Profit for the year attributable to equity holders	–	–	–	–	–	207 9	207 9
Dividends	–	–	–	–	–	(344 2)	(344 2)
New share capital issued	159 2	369 1	–	–	–	–	528 3
Post employment benefits – actuarial gains on defined benefit schemes	–	–	–	–	–	119 2	119 2
Share-based compensation – charged to the income statement	–	–	–	–	–	2 3	2 3
Revaluation of investments	–	–	–	–	–	14 6	14 6
Exercise of share options	–	–	–	–	–	(0 5)	(0 5)
Fair value loss on cashflow hedges	–	–	–	–	–	(0 9)	(0 9)
Tax on items taken directly to equity	–	–	–	–	–	(35 6)	(35 6)
Exchange adjustments	–	–	–	–	(1 5)	–	(1 5)
At 31 March 2006	875 4	1,407 8	158 8	(0 3)	2 2	185 3	2,629 2
Profit for the year attributable to equity holders	–	–	–	–	–	433 5	433 5
Dividends	–	–	–	–	–	(387 3)	(387 3)
New share capital issued	4 4	14 1	–	–	–	–	18 5
Post employment benefits – actuarial gains on defined benefit schemes	–	–	–	–	–	46 5	46 5
Share based compensation – charged to the income statement	–	–	–	–	–	3 9	3 9
Revaluation of investments	–	–	–	–	–	8 9	8 9
Fair value gain on cashflow hedges	–	–	–	–	–	2 8	2 8
Tax on items taken directly to equity	–	–	–	–	–	(14 8)	(14 8)
Exchange adjustments	–	–	–	–	(6 4)	–	(6 4)
At 31 March 2007	**879 8**	**1,421 9**	**158 8**	**(0 3)**	**(4 2)**	**278 8**	**2,734 8**

23 Shareholders' equity continued

Company	Share capital £m	Share premium account £m	Treasury shares £m	Cumulative exchange reserve £m	Retained earnings £m	Total £m
At 1 April 2005	716 2	1,038 7	(0 3)	1 1	2 547 9	4,303 6
Profit for the year attributable to equity holders	–	–	–	–	315 0	315 0
Dividends	–	–	–	–	(344 2)	(344 2)
New share capital issued	159 2	369 1	–	–	–	528 3
Post employment benefits – actuarial gains on defined benefit schemes	–	–	–	–	5 2	5 2
Share-based compensation – charged to the income statement	–	–	–	–	0 9	0 9
Tax on items taken directly to equity	–	–	–	–	(1 6)	(1 6)
Exchange adjustments	–	–	–	4 1	–	4 1
At 31 March 2006	875 4	1,407 8	(0 3)	5 2	2,523 2	4 811 3
Loss for the year attributable to equity holders	–	–	–	–	(106 7)	(106 7)
Dividends	–	–	–	–	(387 3)	(387 3)
New share capital issued	4 4	14 1	–	–	–	18 5
Post employment benefits – actuarial losses on defined benefit schemes	–	–	–	–	(21 4)	(21 4)
Share-based compensation – charged to the income statement	–	–	–	–	3 9	3 9
Tax on items taken directly to equity	–	–	–	–	6 4	6 4
Exchange adjustments	–	–	–	(6 9)	–	(6 9)
At 31 March 2007	**879 8**	**1,421 9**	**(0 3)**	**(1 7)**	**2,018 1**	**4,317 8**

The authorised ordinary share capital of the company was 1,119,000,000 ordinary shares of £1 each at 31 March 2007 (2006 1,119,000,000) The allotted and fully paid ordinary share capital of the company at 31 March 2007 was 879,812,392 ordinary shares (2006 875,422,577)

4,389,815 (2006 4,563,203) ordinary shares were allotted during the year ended 31 March 2007 for the exercise of options in accordance with the rules of the employee ShareSave schemes and the executive share option scheme for a total consideration of £18 5 million (2006 £20 2 million) The five-for-nine rights issue, structured so that the proceeds were received in two stages, was approved at the Extraordinary General Meeting (EGM) of shareholders on 26 August 2003 The first tranche of the proceeds, received during September 2003, raised £501 2 million (net of costs) from the issuing of 309,286,997 A shares The second tranche of proceeds received in June 2005 raised £508 1 million (net of costs) reflecting the subscription of 309,286,997 further A shares

In July 2005, all A shares were consolidated and reclassified as ordinary shares on the basis of one ordinary share for two A shares The company therefore now has one class of ordinary shares which carry no rights to fixed dividends

As permitted by section 230(4) of the Companies Act 1985, the company has not presented its own income statement The amount of group loss for the financial year dealt with in the company's income statement is £106 7 million (2006 £315 0 million profit) after accounting for dividends received from subsidiary undertakings of £48 1 million (2006 £323 6 million) and a loss on the disposal of the Vertex business of £100 4 million (2006 £nil)

The revaluation reserve represents the uplift to deemed cost of the group's water and wastewater infrastructure assets on transition to IFRS, net of taxation

24 Acquisition of subsidiary undertakings

The group made no material acquisitions during the year ended 31 March 2007

On 12 May 2005, the group acquired 100 per cent of the issued share capital of Vertex Financial Services Holdings Limited (formerly Marlborough Stirling Group plc) for cash consideration of £97 3 million including attributable costs

On 30 March 2006, the group and company acquired 100 per cent of the issued share capital of 1st Software Group Limited for initial cash consideration of £25 3 million and deferred contingent consideration of up to £13 5 million On 26 March 2007, on disposal of the Vertex business, the liability for the deferred contingent consideration was assumed by United Utilities PLC

The transactions have been accounted for by the purchase method of accounting The net assets acquired in the transactions, and the goodwill arising, are as follows

	Vertex Financial Services Holdings Limited			1st Software Group Limited		
	Book value £m	Fair value adjustments £m	Fair value £m	Book value £m	Fair value adjustments £m	Fair value £m
Property, plant and equipment	16 8	(12 3)	4 5	0 2	(0 1)	0 1
Other intangible assets	–	77 0	77 0	–	22 1	22 1
Trade and other receivables	18 1	–	18 1	0 5	–	0 5
Cash and cash equivalents	20 8	–	20 8	1 9	–	1 9
Trade and other payables	(32 6)	–	(32 6)	(7 2)	–	(7 2)
Provisions	(3 9)	(34 3)	(38 2)	–	(1 6)	(1 6)
Deferred tax assets	3 1	4 0	7 1	–	–	–
Deferred tax liabilities	–	(9 0)	(9 0)	–	(6 1)	(6 1)
	22 3	25 4	47 7	(4 6)	14 3	9 7
Goodwill			49 6			25 0
Total consideration satisfied by cash and contingent consideration			97 3			34 7
Net cashflows arising on acquisition						
Cash consideration			(95 3)			(32 9)
Attributable costs			(2 0)			(1 8)
			(97 3)			(34 7)
Cash and cash equivalents acquired			20 8			1 9
Contingent consideration less amounts receivable			–			7 5
			(76 5)			(25 3)

The goodwill arising on the acquisitions represents the excess of consideration over the fair value of the net assets and liabilities acquired

In addition to the cashflows above, £0 6 million deferred consideration was paid during the year ended 31 March 2006 in relation to the acquisition of First Revenue Assurance LLC on 31 March 2004

The activities of Vertex Financial Services Holdings Limited, 1st Software Group Limited and First Revenue Assurance LLC have been classified within discontinued operations as they are included in the disposal of Vertex as at 26 March 2007 (see note 7)

25 Operating lease commitments

Group	2007 Property £m	2007 Plant and equipment £m	2006 Property £m	2006 Plant and equipment £m
Commitments under non-cancellable operating leases due				
Within one year	**3 8**	**1 7**	0 1	0 1
In the second to fifth years inclusive	**12 3**	**2 0**	12 2	0 8
After five years	**180 3**	**–**	233 4	2 8
	196 4	**3 7**	245 7	3 7

In respect of the group's commitment to significant property leases, there are no contingent rentals payable, or restrictions on dividends, debt or further leasing imposed by these lease arrangements The group has the right to renew such leases and escalation of rents is via rent reviews over a minimum five-year period

26 Share-based payments

The company operates several share option schemes Options are exercisable at a price equal to the average quoted market price of the company's shares on the date of grant Options are forfeited if the employee leaves the group through resignation or dismissal before the options vest

Equity-settled share-based payments are measured at fair value at the date of grant The fair value determined at the date of grant of equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the group's estimate of shares that will eventually vest

Fair value is measured by use of both simulation and binomial models according to the relevant measures of performance The models include adjustments, based on management's best estimate, for the effects of exercise restrictions, behavioural considerations and expected dividend payments The option life is derived by the models based on these assumptions and other assumptions identified below

The total expense included within operating profit from continuing operations in respect of share-based payments was £4 0 million (2006 £2 6 million)

The United Utilities Employee Share Trust was established by a trust deed executed on 21 August 1996 The Trustees hold the trust fund for the benefit of the beneficiaries (being employees or former employees of the group's companies and their relatives) to the extent determined by the rules of the share schemes As at 31 March 2007, the Trust held 53,601 (2006 52,500) shares on trust and these shares will be used to satisfy awards payable under the group's performance share plan All dividends payable on the shares during the current and prior years were waived

Further details of the different types of share-based payments are as follows

Continuing operations

Company share option scheme 1999

The company share option scheme 1999 is for senior executives (excluding, with effect from the introduction of the group's long-term incentive plan, executive directors and other executives participating in that plan and its successor, the performance share plan)

Options under the company share option scheme 1999 are exercisable in a period beginning no earlier than three years (five years for discounted options under the former executive share option scheme, which are no longer granted) and ending no later than ten years from the date of grant

Employee ShareSave scheme

The employee ShareSave scheme is available to all eligible employees and is based on SAYE savings contracts with options exercisable within a six-month period from the conclusion of a three or five-year period as appropriate from the date of grant Under the terms and conditions of this scheme, for every month (up to no more than six months) an employee fails to contribute the agreed monthly amount determined under the rules of the scheme the last date exercisable will be delayed by one month

Performance share plan

The performance share plan (PSP) is for senior executives of the group Options under the performance share plan are exercisable no earlier than three years from the 31 March preceding the grant and have an exercise period of three months PSP awards are subject to a total shareholder return (TSR) performance condition (a market-based measure of performance)

Cash-settled share-based payments

The group issued to certain employees share appreciation rights (SARs) that require the group to pay the intrinsic value of the SAR to the employee at the date of exercise At 31 March 2007, the group has recorded liabilities of £0 4 million (2006 £0 3 million) in respect of SARs The fair value of the SARs is determined using the Black-Scholes pricing model using the assumptions detailed below The group recorded total expenses of £0 1 million (2006 £0 3 million) during the year in respect of SARs At 31 March 2007, the total intrinsic value of the vested SARs was £nil (2006 £nil)

Other share-based payment plan

The main all-employee scheme is the Inland Revenue approved share incentive plan, 'ShareBuy' This is a flexible way for employees to acquire shares in the company by buying 'partnership' shares up to the lower of £1,500 or ten per cent of taxable pay each year The funds are deducted from pre-tax pay and passed to an independent trustee who makes a monthly purchase of shares at full market price Employees can reinvest the dividends on partnership shares to buy more shares under the plan In 2004, the group introduced 'matching' shares It gives one free share for every five partnership shares bought The shares need to be held in trust for a five-year term in order to retain the maximum tax advantages

26 Share-based payments continued

Discontinued operations

Vertex performance share plan (Vertex PSP)

The Vertex PSP is for senior executives of the group Options under the Vertex PSP are exercisable no earlier than three years from the 31 March preceding the grant and have an exercise period of three months Vertex PSP awards are subject to both a TSR performance condition (a market-based measure of performance) and earnings before interest, taxation and amortisation (EBITA) and return on capital employed (ROCE) performance conditions (non-market based measures of performance)

The Vertex PSP scheme has been discontinued in line with the disposal of Vertex on 26 March 2007 (see note 7) Accordingly, all Vertex PSP options will vest no later than 31 March 2009 and the remaining charge is considered to be inconsequential

For those share option awards and SARs granted in the year ended 31 March 2007 and 31 March 2006, the assumptions used in the calculation of the fair values were as follows

2007	Cash-settled share-based payments	Performance share plan	Vertex performance share plan
Weighted average exercise price (£ per share)	–	–	–
Vesting period (years)	3 0	3 0	3 0
Expected volatility (per cent)	14 2	14 2	14 3
Expected option life after adjustment for anticipated forfeiture (years)	2 7	2 7	2 7
Risk free rate (per cent)	4 84	4 85	4 85
Expected dividend yield (per cent)	–	–	–
Fair value (£ per share)	7 55	1 77	4 36

2006	Cash settled share-based payments	Performance share plan	Vertex performance share plan
Weighted average exercise price (£ per share)	–	–	–
Vesting period (years)	3 0	3 0	3 0
Expected volatility (per cent)	14 0	17 6	18 7
Expected option life after adjustment for anticipated forfeiture (years)	1 8	2 8	2 8
Risk free rate (per cent)	4 38	4 12	4 25
Expected dividend yield (per cent)	6 34	8 57	7 37
Fair value (£ per share)	6 24	1 99	7 14

The rules of the cash-settled share-based payment plan, PSP and Vertex PSP were amended in the year ended 31 March 2007 to include dividend reinvestment

The expected volatility is based on the historical volatility of the company's share price over the expected life of the option The movement in total outstanding options in respect of the awards identified above is provided below

					Continuing operations			Discontinued operations	
	Company share option scheme 1999		Employee ShareSave scheme		Performance share plan		Cash-settled share-based payments	Vertex performance share plan	
	Number of options	Weighted average exercise price (£)	Number of options	Weighted average exercise price (£)	Number of options	Weighted average exercise price (£)	Number of SARs	Number of options	Weighted average exercise price (£)
Outstanding at 1 April 2005	755,027	5 44	4,075,497	4 09	2,683,242	–	66,008	457,431	–
Granted	–	–	–	–	1,227,911	–	80 632	551,991	–
Forfeited	–	–	(284 292)	4 06	(280,467)	–	(19,233)	(95,726)	–
Exercised	(313,478)	5 44	(968 228)	4 20	–	–	–	–	–
Expired	(20,596)	5 44	(12,106)	4 06	–	–	–	–	–
Outstanding at 31 March 2006	420,953	5 44	2,810,871	4 05	3,630,686	–	127,407	913,696	–
Granted	–	–	–	–	853,094	–	59 073	463,010	–
Forfeited	–	–	(114,952)	4 06	(317,408)	–	(34,630)	(483,003)	–
Exercised	(131,183)	5 44	(1,696,035)	3 98	(566,620)	–	–	–	–
Expired	(52,698)	5 44	(30,852)	4 15	(816,274)	–	(4,332)	–	–
Outstanding at 31 March 2007	**237,072**	**5 44**	**969,032**	**4 19**	**2,783,478**	**–**	**147,518**	**893,703**	**–**
Range of prices									
31 March 2007		**5 44**		**3 96-4 23**		**–**			**–**
31 March 2006		5 44		3 96-4 23		–			–
Contractual remaining life									
31 March 2007		**5 7 years**		**1 4 years**		**2 3 years**	**2 3 years**		**2 3 years**
31 March 2006		6 7 years		2 4 years		2 3 years	2 3 years		2 3 years

None of the share options identified above as outstanding at 31 March 2007 had vested at that date

26 Share-based payments continued

Options outstanding at 31 March under the share option schemes which are outside the scope of IFRS 2 'Share-based Payment', together with their exercise prices and dates, were

	2007	2006	Exercise price pence	Normal dates of exercise
Employee ShareSave scheme	–	50,575	481 2[1]	2004 or 2006
	74,166	901,517	432 3[1]	2005 or 2007
Executive share option scheme	–	27,475	470 8[2]	1999 to 2006
	–	72 543	543 0[2]	2000 to 2007
	46,965	63,097	546 4[2]	2000 to 2007
	151,364	237 588	664 5[2]	2000 to 2007
	103,083	111,178	766 0[2]	2001 to 2008
	147,123	170,825	750 5[2]	2001 to 2008
	324,683	553 261	664 0[2]	2002 to 2009
Company share option scheme 1999	**69,247**	91,100	532 2[2]	2002 to 2009
	261,989	423,842	587 9[2]	2003 to 2010
	128,446	190,543	575 8[2]	2003 to 2010
	262,755	402,966	563 7[2]	2004 to 2011
	163,313	206,056	509 3[2]	2005 to 2012
	438,894	714 913	528 3[2]	2005 to 2012
	2,172,028	4,217,479		

Notes

(1) The exercise price represents 80 per cent of the market price at the date the option was granted

(2) The exercise price equalled the market price at the date the option was granted

27 Related party transactions

Group

Transactions between the company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note

Trading transactions

The following transactions were carried out with the group's associate and joint ventures

	Sales of services		Purchases of goods and services	
	2007 £m	2006 £m	2007 £m	2006 £m
Joint ventures	**95 3**	80 3	**3 0**	28 1
Associate	**10 2**	1 0	**6 2**	0 5

	Amounts owed by related parties		Amounts owed to related parties	
	2007 £m	2006 £m	2007 £m	2006 £m
Joint ventures	**10 6**	21 7	**–**	3 5
Associate	**1 3**	0 8	**0 3**	1 5

Sales of services to related parties were on the group's normal trading terms

The amounts outstanding are unsecured and will be settled in accordance with normal credit terms No guarantees have been given or received A £0 1 million provision has been made for doubtful debts in respect of the amounts owed by related parties (2006 £nil)

Company

The parent company receives dividend and interest income from, and recharges certain costs to, subsidiary undertakings in the normal course of business

Total income received during the year amounted to £52 8 million (2006 £341 1 million) and total recharges were £28 2 million (2006 £12 1 million) Amounts outstanding at 31 March 2007 and at 31 March 2006 between the parent company and subsidiary undertakings are provided in notes 15 and 22

In addition, the parent company also recharges certain costs to its associate in the normal course of business Total recharges were £8 6 million (2006 £nil) during the year There were no amounts outstanding between the parent company and its associate at 31 March 2007 or 2006

Related party receivables and payables are not secured and no guarantees were issued in respect thereof Balances will be settled in accordance with normal credit terms No provisions have been made for doubtful debts in respect of the amounts owed by related parties

The directors and key management of the company are the same as for the group Information on the remuneration of directors and key management personnel can be found in note 2

28 Cash generated from/(used in) operations

	Group		Company	
	2007 £m	2006 £m	2007 £m	2006 £m
Continuing operations				
Profit/(loss) before taxation	**676 0**	445 1	**(132 6)**	44 5
Adjustment for investment income and finance expense	**170 2**	284 4	**64 8**	(38 1)
Adjustment for share of results of associated company	**(18 7)**	–	**–**	–
Operating profit/(loss)	**827 5**	729 5	**(67 8)**	6 4
Adjustments for				
Depreciation of property, plant and equipment	**277 5**	248 6	**0 2**	–
Amortisation of intangible assets	**11 0**	34 2	**–**	–
Profit on disposal of property plant and equipment	**(5 8)**	(4 7)	**–**	–
Loss on disposal of subsidiaries	**–**	–	**100 4**	–
Changes in working capital				
Decrease in inventories	**3 9**	8 7	**–**	–
(Increase)/decrease in trade and other receivables	**(75 6)**	(166 2)	**78 6**	(7 2)
(Decrease)/increase in provisions and payables	**(2 7)**	147 1	**(49 2)**	(24 5)
Cash generated from/(used in) continuing operations	**1,035 8**	997 2	**62 2**	(25 3)

	2007 £m	2006 £m
Discontinued operations		
Profit/(loss) from operations	**19 2**	(23 4)
Adjustment to value (see note 7)	**–**	(147 7)
Profit/(loss) before taxation	**19 2**	(171 1)
Adjustment for investment income and finance expense	**(4 2)**	12 5
Operating profit/(loss)	**15 0**	(158 6)
Adjustments for		
Depreciation of property, plant and equipment and adjustment to value	**4 3**	135 0
Amortisation of intangible assets and adjustment to value	**9 9**	68 3
Profit on disposal of property, plant and equipment	**–**	(0 1)
Changes in working capital		
Decrease in inventories	**–**	0 2
Decrease in trade and other receivables	**70 3**	23 2
Decrease in payables	**(68 8)**	(72 7)
Interest paid	**(0 1)**	–
Interest received and similar income	**0 3**	0 9
Tax paid	**(2 5)**	(0 7)
Cash generated from/(used in) operating activities – discontinued operations	**28 4**	(4 5)

Non-cash transactions

During the period, the retained pension balances (£26 8 million) in respect of businesses disposed have been transferred to the company's share of the defined benefit pension schemes (see note 19)

There were no material non-cash transactions during the year affecting the group

As described in note 7, on 26 February 2006 the group disposed of its interest in the Your Communications' business The total fair value of consideration of £68 1 million was satisfied by the issue of ordinary shares and contingent share options

Disposal of subsidiary

The company cashflow statement includes additional proceeds in relation to the intra-group disposal of 1st Software Group Limited of £21 2 million

29 Contingent liabilities

The company guaranteed loans of group undertakings up to a maximum amount of £703 7 million (2006 £519 5 million), including £613 7 million (2006 £429 5 million) relating to United Utilities Water PLC's loans from European Investment Bank and £90 0 million (2006 £90 0 million) relating to United Utilities Electricity PLC's loans from European Investment Bank

The company has entered into performance guarantees as at 31 March 2007, where a financial limit has been specified of £134 1 million (2006 £124 3 million)

30 Events after the balance sheet date

On 4 June 2007, the board took the decision to initiate a sale process for the group's electricity distribution assets This is as a result of the board's view that shareholders' interests are best served by the group focusing its capital on the much larger water asset base, which offers significantly more growth potential than the electricity assets The group intends to retain the operation of its electricity distribution assets, going forward, consistent with its strategy of focusing on core skills

As there is an expectation that a transaction will qualify for recognition as a completed sale within one year, United Utilities' electricity distribution assets meet the definition of a disposal group in accordance with IFRS 5 'Non-current Assets held for Sale and Discontinued Operations' as at 4 June 2007

The net asset value of the group's electricity distribution assets included within the United Utilities North West segment as at 31 March 2007 was £640 1 million

In this report, references to 'company' or 'United Utilities' are to United Utilities PLC, either alone or together with its consolidated subsidiaries, as the context requires References to 'group' are to United Utilities PLC together with its consolidated subsidiaries References to 'UUE' and to 'United Utilities Electricity' are to United Utilities Electricity PLC, to 'Contract Solutions' and to 'United Utilities Contract Solutions' are to United Utilities Contract Solutions Holdings Limited and subsidiaries, to 'United Utilities Industrial' are to United Utilities Industrial Limited and subsidiaries, to 'United Utilities Networks' are to United Utilities Networks Limited, to 'UUNW' and to 'United Utilities North West' are to United Utilities North West PLC and to the asset management activities of the wastewate, water and electricity network assets owned by United Utilities Water and United Utilities Electricity, to 'UUW' and to 'United Utilities Water' are to United Utilities Water PLC, to 'United Utilities Property' are to United Utilities Property Solutions Limited, which are all wholly owned subsidiaries of the company References to 'Your Communications' are to Your Communications Group Limited and its subsidiaries which were sold to THUS Group PLC on 26 February 2006 References to 'Vertex' are to Vertex Data Science Limited and its subsidiaries which were sold to VTX Bidco Limited on 26 March 2007

References are also made to specific terms which bear the following meanings

– 'Megawatt' (MW)	– a megawatt is a unit of power equal to one million watts
– 'Gigawatt' (GW)	– a gigawatt is a unit of power equal to one billion (one thousand million) watts
– 'Gigawatt-hour' (GWh)	– one gigawatt-hour represents one hour of electricity consumption at a constant rate of 1GW
– 'Kilowatt' (kW)	– a kilowatt is a unit of power equal to one thousand watts
– 'Kilovolt' (kV)	– a kilovolt is a unit of electrical potential equal to one thousand volts
– 'Megalitre' (Ml)	– one megalitre equals one million litres

The company's registered office is located at Haweswater House, Lingley Mere Business Park, Lingley Green Avenue, Great Sankey, Warrington, WA5 3LP, England and its telephone number is +44 (0)1925 237000 The company is registered in England number 2366616 The website address is www unitedutilities com

The company's financial year ends on 31 March of each year Unless the context otherwise requires, references in this report to 'financial year' or to a particular year (e g 2006/07) are to the 12 months ended on 31 March of that year

Within this report we have worked to reduce our impact on the environment and have offset emissions that cannot be eliminated

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