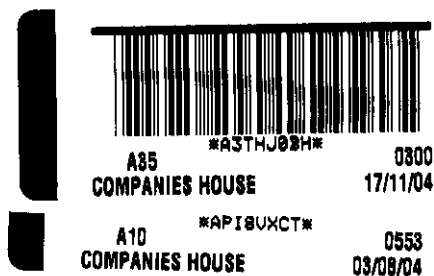


# ANGLIAN WATER SERVICES LIMITED

## ANNUAL REPORT AND ACCOUNTS 2004

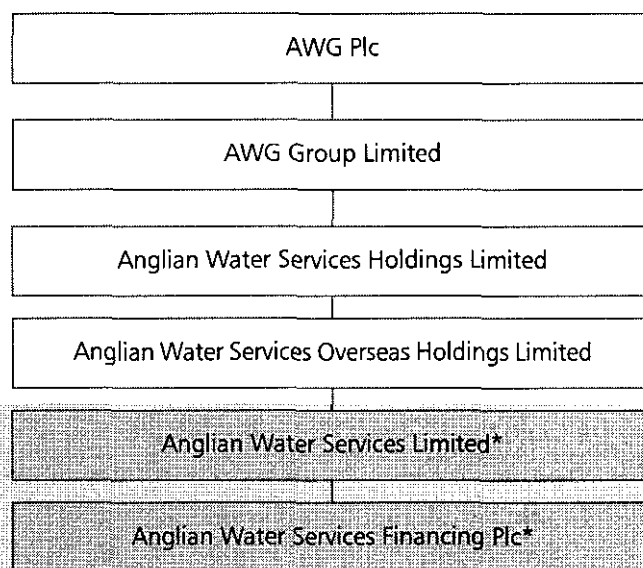
Company Number: 2366656



## financial highlights

	2004	2003	change
turnover	£766.6m	£726.8m	5.5%
operating costs	£447.7m	£458.0m	(2.2)%
operating profit	£318.9m	£268.8m	18.6%
profit before tax	£269.2m	£166.9m	61.3%

## legal structure



The legal structure of Anglian Water Services Limited, its parent companies and subsidiary company is shown opposite:

\* These two companies are collectively known as the Anglian Water Services group and the Statutory Accounts in this document have been prepared for this group.

Under the Common Terms Agreement (see page 2) the four Anglian Water Services companies are collectively known as the Anglian Water Services Financing group.

## directors' report

Anglian Water Services Limited (the company) serves the people of the Anglian Water region, an area stretching from the Humber to the Thames, as well as customers in the Hartlepool Water region. The company aims to provide a high quality, cost effective service to all customers, whilst ensuring compliance with environmental and public health standards.

### Anglian Water Services group

The company and Anglian Water Services Financing Plc are collectively known as Anglian Water Services group (the group) and are part of the AWG Plc group. The group operates on an arms-length basis from other companies within AWG Plc group.

### common terms agreement

On 30 July 2002 the group entered into a Common Terms Agreement (CTA) with its debt investors as part of a financial restructuring. The CTA sets out the terms and conditions of the group's borrowing and the on-going management of its Global Secured Medium Term Note (GSMTN) programme. The CTA also sets out the financial and non-financial covenants that must be complied with in relation to the GSMTN.

Under the CTA the four Anglian Water Services companies (see 'legal structure' on page 1) are collectively known as the Anglian Water Services Financing group.

### corporate governance

The corporate governance measures put in place at the time of the financial restructuring are designed to ensure that the company has the means to conduct its regulated business separately from AWG Plc group, and that all dealings between AWG Plc group and the group are on an arms-length basis.

Each company within the group is required to maintain at least three independent Non-Executive Directors. Further, the board of directors of each group company may comprise directors who are also directors of other AWG Plc group companies provided that the Executive Directors in this category do not constitute a majority of the Executive Directors. The constitutional documents of each company provide that all conflicts of interest of directors must be disclosed and that no director may vote on any contracts or arrangement between a group company and any other AWG Plc group company if he/she is also a director of the AWG Plc group company.

The processes for identifying, evaluating and managing the significant risks to the company and the company's internal control systems are regularly reviewed by the Audit Committee which reports its findings for consideration by the board.

The Audit Committee, which meets three times a year, comprises Non-Executive Directors of the company and has written terms of reference. The terms of reference deal clearly with the committee's authority and duties. The processes used by the committee to carry out its review include:

- the review of plans prepared by internal and external auditors;
- the review of reports arising from the work of the risk management committee on the effectiveness of risk management across the company;
- discussions with management on significant risk areas; and
- the review of significant issues highlighted by the Executive Directors, internal and external auditors.

### principal activities and business review

The group's principal activities during the year were the provision of drinking water and the treatment of wastewater in a region approximately one-fifth the area of England and Wales. The group provides drinking water to more than 4.2 million customers, and more than 5.4 million customers benefit from our wastewater services.

A review of the group's performance during the year, together with comments on the financial results, is contained on pages 4 and 5.

### results and dividends

The profit and loss account on page 7 shows the group's results, dividends and profit for the year.

### health and safety

Health and safety is a key priority for the company which is seeking to achieve high standards for the wellbeing of its employees, contractors and customers. It encourages ownership of health and safety by all its employees, contractors, visitors and anyone else affected by its activities. The company strives to achieve an incident- and injury-free environment wherever it operates.

The company has operational procedures for each business area. These procedures take account of good management practice and specific business, statutory and legal requirements. Business heads are charged with the implementation of these procedures within their respective units.

### regulation

The company's activities are regulated by the Water Industry Act 1991 (which consolidated that part of the Water Act 1989 relating to water supply and sewerage) and the conditions of an Instrument of Appointment (the licence) granted to the company by the Secretary of State for the Environment on 1 September 1989.

With certain exceptions, the regulatory provisions do not apply to business activities which are not connected with the carrying out of the water and sewerage functions.

Under Condition F of the licence the company is obliged to provide the Director General of Water Services (DG) with additional accounting information to that contained in the historical cost financial statements. This information is presented in the regulatory accounts (see pages 31 to 47).

### directors and directors' interests

During the year ended 31 March 2004 there were two changes in the directors of the company:

Peter Hickson (Chairman of AWG Plc) was appointed Non-Executive Chairman on 17 April 2003 and Jonson Cox (Chief Executive of AWG Plc) was appointed as a Non-Executive Director on 29 January 2004.

The directors at 31 March 2004 were:

Peter Hickson – Non-Executive Chairman  
Roy Pointer – Chief Executive  
Colin Brown – Executive Director  
David Hipple – Executive Director  
Jonson Cox – Non-Executive Director  
Richard Jewson – Non-Executive Director<sup>1</sup>  
Robert Napier – Non-Executive Director<sup>1</sup>  
Roger Witcomb – Non-Executive Director<sup>1</sup>

<sup>1</sup> Independent Non-Executive Director

In addition, Jean Spencer was appointed as an Executive Director on 20 May 2004.

Details of the directors' interests in the shares of AWG Plc, and in options over such shares, are shown on pages 17 and 18.

### charitable and political donations

During the year the group made a payment of £1.0 million (2003: £1.0 million) to the Anglian Water Trust Fund.

The AWG Community Investment Programme, which is predominantly based on employees' participation in community activities during working hours, saw 322 employees joining up for the 'give me five' matching hours scheme.

The 'give me five' scheme allows employees to take up to 30 work hours, matched by their own time, to get involved in community activities.

Financially through charitable donations, educational, regeneration and recreation projects the company contributed £0.1 million (2003: £0.1 million) to other charitable causes.

No political donations were made.

### research and development

The company has a continuing policy of undertaking market-focused research and development on process plant, biosolids treatment and other water and wastewater-related matters.

### employees

Employees are kept informed of changes in the business and general financial and economic factors influencing the company. This is done through a systematic approach to employee communication through regular briefings, presentations, electronic mailings and the wide circulation of the AWG magazine. The AWG Intranet is also widely used as a source of information.

The company has introduced an Ethics Policy, which informs all employees on the group's approach to a range of ethical issues. 'Whistle-blowing' procedures are in place to deal with allegations of harassment, bullying and other inappropriate behaviour.

## statement of directors' responsibilities

The company has also introduced a series of 'family friendly' policies including such initiatives as flexible working hours, home working, sabbaticals and career breaks.

A Sharesave Scheme is in place to encourage participation in the AWG Plc group's performance.

The company is an equal opportunities employer and job applications from disabled persons are fully and fairly considered, having regard to the aptitudes and abilities of the applicant. In the event of disability, every effort is made to ensure that employment continues and appropriate training is given. Career development and promotion of disabled people is, as far as possible, identical to that of other employees.

### policy on the payment of creditors

It is the company's policy to provide suppliers of goods and services with a statement of general conditions of contract. This document is available from the company's Supply Chain Management department. In general, regional purchasing agreements are in place with preferred suppliers and the terms will apply to all transactions. The company abides by the terms of payment. The company's average creditor payment period at 31 March 2004 was 36 days (2003: 35 days).

### auditors

PricewaterhouseCoopers LLP has indicated its willingness to continue in office and a resolution proposing its re-appointment will be put to the Annual General Meeting.

By order of the board



Juana Tinn  
Company Secretary  
2 June 2004

Registered Office: Henderson House,  
Lancaster Way, Huntington,  
Cambridgeshire PE29 6XQ  
Registered in England and Wales No. 2366656

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

The directors confirm that suitable accounting policies have been used and applied consistently as set out in note 1 to the financial statements (Accounting policies). They also confirm that reasonable and prudent judgements and estimates have been made in preparing the financial statements for the year ended 31 March 2004 and the applicable accounting standards have been followed.

The directors are responsible for ensuring that the Annual Report and Accounts are published and where they are published on the Internet, for the maintenance and integrity of the website. Uncertainty regarding legal requirements is compounded as information published on the Internet is accessible in many countries with different legal requirements relating to the preparation and dissemination of financial statements.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the company and the group 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 the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

## performance review

### operating results

The group's turnover increased 5.5 per cent in the period to £766.6 million (2003: £726.8 million), while operating profit after exceptional items was up 18.6 per cent to £318.9 million (2003: £268.8 million). The additional revenue arose principally from the regulatory pricing formula of Retail Price Index (RPI) + K<sup>1</sup>, together with £8 million extra turnover generated in the first half as a result of additional demand from metered customers during the exceptionally dry summer. Despite the extreme conditions and the region's low rainfall, the group's resources remained satisfactory throughout the period and have recharged to normal levels during the wet winter months.

The dry summer conditions demonstrated the benefit of a customer base where more than half the domestic customers are metered. At a local level, however, it also highlighted 'hot spot' growth areas where further investment is required in the supply network over the next five years. These issues are being addressed with Ofwat, the industry regulator, as part of the price review process.

Operating expenditure (excluding depreciation) for the full year was £291.7 million (2003: £282.5 million) before exceptional charges of £18.6 million, £10 million above the regulatory determination, reflecting £4.7 million of redundancy costs and additional costs on sludge.

The depreciation charge has reduced from £156.9 million to £156.0 million largely reflecting the fact that some shorter life assets were fully depreciated in the prior year offset by depreciation on new additions.

There are no exceptional operating costs in the current year. In the prior year the exceptional operating costs of £18.6 million related to restructuring (£2.9 million) and refinancing project costs (£15.7 million).

Net interest payable includes £193.6 million (2003: £129.6 million) receivable from Anglian Water Services Holdings Limited in relation to an inter-company loan. Excluding this inter-company interest receivable and, in the prior year, the exceptional interest charge, the interest charge has increased by 30.9 per cent from £185.8 million to £243.3 million. This increase reflects the fact that the prior year charge included only a part year impact of the financial restructuring which took place in July 2002, whereas there is a full year impact in the current year.

<sup>1</sup> Ofwat defines K as the amount by which a company can increase, or must decrease, its average charge above or below inflation each year to finance its services and meet its legal obligations. When inflation is included, this is commonly referred to as the 'price limit'.

### financial needs and resources

At 31 March 2004 the company had net borrowings of £3,450.9 million, an increase of £161.5 million over the year. Net borrowings are a mixture of fixed, index linked and variable rate debt of £3,922.6 million and cash and deposits of £471.7 million. The increased net borrowings have been financed by a net increase of £456.3 million in loans and associated costs and a net increase of £294.8 million in cash and deposits. The business generated a net cash inflow from operating activities of £484.0 million in 2004 (2003: £415.9 million).

Capital expenditure for the full year continued to show outperformance against the determination at £276.9 million (2003: £263.3 million). Over the current five-year plan period (2000/01 to 2004/05) the group will be investing approximately £1.6 billion on further improvements to drinking water, bathing and river water quality, as well as network improvements to maintain serviceability and meet new demands.

### shareholder's return

Dividends have been declared at 29.14 pence per share (2003: 33.56 pence per share). The total cost of the dividend amounts to £250.6 million (2003: £288.6 million).

Of the above, £193.6 million (2003: £129.6 million) is payable to Anglian Water Services Holdings Limited in order for it to service the interest payable to the company on the inter-company loan of £1,609.1 million and £57.0 million (2003: 159.0 million) is payable outside the Anglian Water Services Financing group. The dividend payable outside the Anglian Water Services Financing group equates to 6.63 pence per share (2003: 18.49 pence per share).

### liquidity

The group's objective is to maintain flexibility, diversification and continuity of funding through access to different markets and debt instruments. At the year-end the group held cash, deposits and current asset investments of £471.7 million (2003: £176.9 million) and had undrawn committed facilities of £225.0 million (2003: £225.0 million). These resources are maintained to ensure liquidity and the continuation of the investment programme of the company. The maturity profile of the group's borrowings is set out in note 19 on pages 20 to 24 of the accounts. In addition the group has access to £304.0 million of 'liquidity facilities', consisting of, £241.0 million to finance debt service costs and £63.0 million to finance operating expenditure and maintenance capital expenditure in the event that the group was in default on its debt obligations.

### interest rates

The group's policy as agreed by the board is to achieve an optimum mix of funding at indexed, fixed and floating rates of interest, including the use of interest rate swaps, to manage the group's exposure to interest rate fluctuations. At the year-end, taking into account interest rate swaps, 32.4 per cent (2003: 28.3 per cent) of the group's borrowings were at rates indexed to inflation, 62.6 per cent (2003: 71.5 per cent) were at fixed rates and 5.0 per cent (2003: 0.2 per cent) were at floating rates. The percentages quoted are net of financial assets on which no interest is paid. See note 19 for further details.

Following the restructuring in July 2002, the group moved to a higher proportion of fixed and index linked interest loans for the remainder of the current regulatory period ending 31 March 2005.

### service quality

The company continued to perform well against service and water quality standards. Drinking water quality remained high, with 99.7 per cent of all water quality tests performed in the 2003 calendar year complying with the regulatory standards (2002: 99.6 per cent). Overall microbiological compliance for the period is at its highest-ever level.

In addition to delivering a quality product, the company has further improved the quality of its service delivery. The number of properties experiencing low water pressure has been reduced, as have interruptions to supply. The company has also reduced the proportion of customers experiencing sewage flooding. Serious pollution incidents have been reduced and sewage treatment compliance with the Office of Water Services (Ofwat) key criteria improved.

All 46 designated bathing waters in the company's region passed the mandatory coliform standards of the Bathing Water Directive. This is the fifth time in the past seven years that 100 per cent compliance has been achieved. In addition, 35 of the region's bathing waters (76 per cent) also passed the guideline standard of the Directive. River water quality in the region remains the best it has been since records began.

Ofwat's report shows that in 2002/03 the company had the lowest water leakage rate in England and Wales. Its leakage of five cubic metres per kilometre of water pipe per day is less than half the industry average of 11 cubic metres. Combined with the proportion of our customers on metered supplies at 54 per cent, the low leakage rate was a significant factor in preserving water resources while a very high level of demand was experienced in the hot summer. The company met Ofwat's leakage target for 2003/04.

#### regulation

As part of the regulatory review process the company submitted its final regulatory business plan for the review period 2005 to 2010 to Ofwat in April 2004. The final business plan's capital investment programme was significantly reduced from the draft submission in August 2003.

In preparing the plan, the company confronted the hard choices that needed to be made between investment, service and quality improvements and the impact that these have on prices.

The plan proposes a capital investment programme of £1.8 billion over the five-year period, which would result in lower bill increases for Anglian Water customers than for any other water and sewerage company in England and Wales.

If accepted, this plan would see the average customer bill rise by £47 over the five years (at 2002/03 prices), or an average of 3.3 per cent each year. The average K factor over the period would be 4.6 per cent. Recognising the concerns of customers, the company has evened out price increases across the new Asset Management Plan period.

Ofwat plans to publish its draft determination in August 2004. This will be followed by a further period of consultation before a final determination in December 2004.

#### pensions

The group continues to account for pensions in accordance with Statement of Standard Accounting Practice (SSAP) 24. Applying SSAP 24 results in the group having a net pension prepayment at 31 March 2004 of £53.5 million. This compares with the Financial Reporting Standard (FRS) 17 pension deficit of £143.6 million. One of the reasons for the difference is that SSAP 24 recommends that the pension scheme is valued at least once every three years, with the last valuation for the scheme at 31 March 2002. Under FRS 17 the valuation is updated every year. In addition, the assumptions used under FRS 17 are different from those in SSAP 24. Under FRS 17 the discount rate used for calculating scheme liabilities is the yield on AA corporate bonds, whereas SSAP 24 uses a higher discount based on the expected return on scheme assets.

The group made additional pension contributions totalling £9.1 million in the year (2003: £6.3 million). Future contributions to the AWG Pension Scheme (AWGPS) will continue to be made in line with actuarial advice.

During the year, an approximate funding update was carried out for the purposes of assessing the cash requirements of the AWGPS for the regulatory periodic review. Although not a full actuarial valuation and not constituting a 'later formal review' (as defined by SSAP 24), this indicated an actuarial deficit (after tax) of £138 million at 31 March 2003. It is anticipated that the appropriate level of pensions costs will be an important part of the forthcoming regulatory settlement.

## independent auditors' report

We have audited the statutory financial statements which comprise the profit and loss account, the balance sheet, the cash flow statement and the related notes which have been prepared under the historical cost convention and the accounting policies set out in the accounting policy note.

### respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable United Kingdom law and accounting standards are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board. This report, including the opinion, has been prepared for, and only for, the company's member in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the directors' report and the performance review.

### basis of audit opinion

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

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

### opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the company and the group at 31 March 2004 and of the profit and cash flows of the group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.



PricewaterhouseCoopers LLP  
Chartered Accountants and Registered Auditors  
Birmingham  
2 June 2004

PRICEWATERHOUSECOOPERS 

# group profit and loss account

for the year ended 31 March

Notes	2004			2003	
	Total £m	Before exceptional items £m	Exceptional items £m	Total £m	
2	Turnover – continuing operations	766.6	726.8	--	726.8
	Operating costs:				
3, 4	Operating costs before depreciation	(291.7)	(282.5)	(18.6)	(301.1)
3	Depreciation net of amortisation of grants and contributions	(156.0)	(156.9)	--	(156.9)
3, 4	Total operating costs	(447.7)	(439.4)	(18.6)	(458.0)
5	Operating profit – continuing operations	318.9	287.4	(18.6)	268.8
4	Profit on disposal of businesses	--	--	3.3	3.3
4	Profit on sale of fixed assets	--	--	0.6	0.6
	Profit on ordinary activities before interest	318.9	287.4	(14.7)	272.7
4, 6	Net interest payable	(49.7)	(56.2)	(49.6)	(105.8)
	Profit on ordinary activities before taxation	269.2	231.2	(64.3)	166.9
4, 7	Tax on profit on ordinary activities	33.5	(75.2)	17.5	(57.7)
	Profit on ordinary activities after taxation for the financial year	302.7	156.0	(46.8)	109.2
8	Dividends				
	– paid / payable	(250.6)	(288.6)	--	(288.6)
	– part of 2001 final dividend waived by AWG Group Limited	--	799.2	--	799.2
25	Retained profit	52.1	666.6	(46.8)	619.8

The notes on pages 11 to 30 form part of these financial statements.

No statement of total recognised gains and losses has been presented, as all gains and losses have been included in the profit and loss account.



# group and company balance sheets

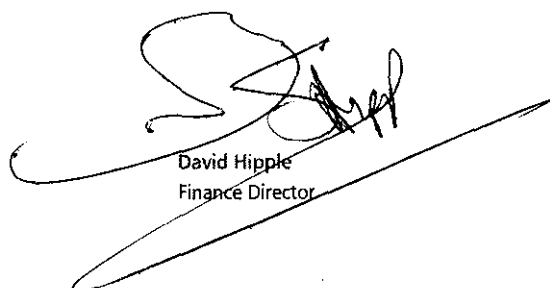
at 31 March

Notes	Group		Company		
	2004 £m	2003 £m	2004 £m	2003 £m	
	<b>Fixed assets</b>				
14	Tangible assets	3,801.5	3,696.7	3,801.5	3,696.7
15	Investments	1,609.3	1,609.3	1,609.3	1,609.3
		<b>5,410.8</b>	<b>5,306.0</b>	<b>5,410.8</b>	<b>5,306.0</b>
	<b>Current assets</b>				
16	Stocks	6.6	4.6	6.6	4.6
17	Debtors	253.0	264.2	290.2	279.2
	Cash at bank and in hand	471.7	176.9	431.4	161.3
		<b>731.3</b>	<b>445.7</b>	<b>728.2</b>	<b>445.1</b>
	<b>Creditors: amounts falling due within one year</b>				
18,19	Short-term borrowings	(22.0)	(27.4)	(22.0)	(27.4)
18	Other creditors	(344.1)	(449.7)	(343.3)	(448.6)
		<b>(366.1)</b>	<b>(477.1)</b>	<b>(365.3)</b>	<b>(476.0)</b>
	<b>Net current assets / (liabilities)</b>	<b>365.2</b>	<b>(31.4)</b>	<b>362.9</b>	<b>(30.9)</b>
	<b>Total assets less current liabilities</b>	<b>5,776.0</b>	<b>5,274.6</b>	<b>5,773.7</b>	<b>5,275.1</b>
	<b>Creditors: amounts falling due after more than one year</b>				
19	Loans and other borrowings	(3,900.6)	(3,438.9)	(3,900.6)	(3,438.9)
20	Other creditors	(90.0)	(87.4)	(90.0)	(87.4)
		<b>(3,990.6)</b>	<b>(3,526.3)</b>	<b>(3,990.6)</b>	<b>(3,526.3)</b>
21	Provisions for liabilities and charges	(149.0)	(164.0)	(149.0)	(164.0)
		<b>1,636.4</b>	<b>1,584.3</b>	<b>1,634.1</b>	<b>1,584.8</b>
	<b>Capital and reserves</b>				
24, 25	Called up equity share capital	860.0	860.0	860.0	860.0
25	Profit and loss reserve	776.4	724.3	774.1	724.8
25	<b>Total shareholder's funds (all equity)</b>	<b>1,636.4</b>	<b>1,584.3</b>	<b>1,634.1</b>	<b>1,584.8</b>

The notes on pages 11 to 30 form part of these financial statements.

Approved by the board on 2 June 2004.

  
Roy Pointer  
Chief Executive

  
David Hipple  
Finance Director

# group cash flow statement

for the year ended 31 March

Notes	2004 £m	2003 £m
(a) Net cash inflow from operating activities	484.0	415.9
>Returns on investments and servicing of finance		
Interest received	206.5	95.5
Interest paid	(211.7)	(126.6)
(d) Cash flows treated as finance costs under Financial Reporting Standard (FRS) 4	(1.3)	(23.8)
Interest element of finance lease rental payments	(9.1)	(9.7)
Net cash outflow for returns on investments and servicing of finance	(15.6)	(64.6)
Taxation		
Corporation Tax received	0.3	0.5
Capital expenditure and financial investment		
Purchase of tangible fixed assets	(276.6)	(261.7)
Grants and contributions received	18.6	17.0
Short-term loan to group company, AWG Group Limited	–	309.5
Loan to group company, Anglian Water Services Holdings Limited	–	(1,609.1)
Disposal of tangible fixed assets	1.1	1.3
Net cash outflow for capital expenditure and financial investment	(256.9)	(1,543.0)
Acquisitions and disposals		
Acquisition of trade and certain assets of a group company, Geodesys Limited (net of cash acquired)	–	1.7
Equity dividends paid	(345.1)	(136.0)
Net cash outflow before management of liquid resources and financing	(133.3)	(1,325.5)
(c) Management of liquid resources		
(d) Increase in short-term deposits and investments	(180.8)	(88.2)
(d) Financing		
Increase in loans	453.2	1,947.3
Repayment of amounts borrowed	(0.7)	(255.1)
Capital element of finance lease rental payments	(24.4)	(21.7)
Net cash inflow from financing	428.1	1,670.5
(d) Increase in cash	114.0	256.8

The notes on page 10 form part of this cash flow statement.

## notes to the group cash flow statement

	2004 £m	2003 £m
(a) Reconciliation of operating profit to net cash inflow from operating activities		
Operating profit	318.9	268.8
Depreciation (net of amortisation of deferred grants and contributions)	156.0	156.9
Profit on disposal of fixed assets	(0.8)	–
Sale of businesses	–	(3.3)
Net movement in prepaid pension contributions	(14.6)	(14.6)
Net movement on provisions	(2.1)	(1.9)
	<u>457.4</u>	<u>405.9</u>
Working capital:		
Increase in stocks	(2.0)	(0.5)
Decrease in debtors	28.9	46.9
Decrease in creditors	(0.3)	(36.4)
	<u>26.6</u>	<u>10.0</u>
<b>Net cash inflow from operating activities</b>	<b><u>484.0</u></b>	<b><u>415.9</u></b>

The cash flow statement for the year ended 31 March 2004 includes £7.7 million in respect of prior year exceptional charges. The prior year comparative includes cash outflows of £39.1 million in respect of prior year exceptional costs.

	1 April 2003 £m	Cash flows £m	Non-cash movements £m	31 March 2004 £m
(b) Analysis of net debt				
Cash	88.7	114.0	–	202.7
Deposits and investments	88.2	180.8	–	269.0
Debt due within one year	(27.4)	27.4	(22.0)	(22.0)
Debt due after one year	(3,438.9)	(454.2)	(7.5)	(3,900.6)
	<u>(3,289.4)</u>	<u>(132.0)</u>	<u>(29.5)</u>	<u>(3,450.9)</u>

Non-cash movements comprise indexation of index linked loan stock, indexation of Retail Price Index (RPI) swaps, transfers between categories of debt, amortisation of debt issue costs and amortisation of 'mark to market' adjustments.

The deposits and investments of £269.0 million (2003: £88.2 million) are short-term deposits maturing within three months, these are included in the heading 'cash at bank and in hand' in the Balance Sheet.

(c) Management of liquid resources is comprised of movements in short-term deposits which have maturity dates of up to one year.

	2004 £m	2003 £m
(d) Movement in net debt		
At beginning of year	(3,289.4)	(1,970.9)
Increase in cash	114.0	256.8
Increase in short-term deposits and investments	180.8	88.2
Increase in loans	(453.2)	(1,947.3)
Repayment of amounts borrowed	0.7	255.1
Finance costs capitalised under FRS 4	1.3	23.8
Amortisation of debt issue costs and 'mark to market' adjustments	1.4	0.9
Indexation of loan stock and RPI swaps	(30.9)	(17.7)
Capital element of finance lease rental payments	24.4	21.7
<b>At end of year</b>	<b><u>(3,450.9)</u></b>	<b><u>(3,289.4)</u></b>

## notes to the financial statements

### 1 Accounting policies

The financial statements are prepared under the historical cost convention and in accordance with applicable accounting standards and in accordance with the Companies Act 1985, except as disclosed in note 1 (d) below as relating to grants and contributions.

The principal accounting policies are summarised below. They have all been applied consistently throughout the current and preceding year.

#### (a) Basis of consolidation

The Anglian Water Services group (the group) financial statements comprise a consolidation of the financial statements of Anglian Water Services Limited (the company) and its subsidiary, Anglian Water Services Financing Plc, at 31 March. Intra-group sales and profit are eliminated fully on consolidation.

#### (b) Turnover

Turnover represents the income receivable (excluding Value Added Tax) in the ordinary course of business for goods and services provided and, in respect of unbilled charges, includes an accrual for measured income.

The measured income accrual is an estimation of the amount of main water and wastewater charges unbilled at the year end. The accrual is estimated using a defined methodology based upon weighted average water consumption by tariff, which is calculated based upon historical billing information. The calculation is sensitive to estimated consumption for domestic customers (a fall of 1 cubic metre in average annual consumption will reduce turnover by approximately £1.0 million).

#### (c) Tangible fixed assets and depreciation

Tangible fixed assets comprise:

*Infrastructure assets* (being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls) comprise a network of systems. Investment expenditure on infrastructure assets relating to increases in capacity or enhancements of the network and on maintaining the operating capability of the network in accordance with defined standards of service, is treated as an addition and included at cost after deducting grants and contributions. The depreciation charge for infrastructure assets is the estimated level of annual expenditure required to maintain the operating capability of the network which is based on the company's independently certified Asset Management Plan.

*Other assets* (including properties, over-ground plant and equipment) are included at cost less accumulated depreciation. Cost includes own work capitalised which represents the direct cost of materials, labour and applicable overheads. Freehold land is not depreciated. Depreciation of other assets is calculated at rates expected to write off cost less the estimated residual value of the relevant assets on a straight line basis over their estimated economic lives, which are principally as follows:

Operational structures	30 – 80 years
Buildings	30 – 60 years
Fixed plant	12 – 40 years
Vehicles, mobile plant and computers	3 – 10 years

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

Interest costs are not capitalised into the cost of fixed assets.

#### (d) Grants and contributions

Grants and contributions on capital expenditure, other than those relating to infrastructure assets, are credited to a deferral account within creditors and are released to revenue evenly over the expected useful life of the relevant asset in accordance with the provisions of the Companies Act 1985.

Grants and contributions to capital expenditure on infrastructure assets are deducted from the costs of these assets. This policy is not in accordance with Schedule 4 of the Companies Act 1985, which requires grants and contributions to be shown as deferred income, but has been adopted in order to show a true and fair view as, in the opinion of the directors, while a provision is made for depreciation of infrastructure assets, these assets have no determinable finite economic life and hence no basis exists on which to recognise such contributions as deferred income. The financial effect of this departure is disclosed in note 14.

Revenue grants and contributions are credited to the profit and loss account in the year to which they apply.

#### (e) Leased assets

Where assets are financed by leasing arrangements which transfer substantially all the risks and rewards of ownership of an asset to the lessee (finance leases), the assets are treated as if they had been purchased and the corresponding capital cost is shown as an obligation to the lessor. Leasing payments are treated as consisting of a capital element and finance costs, the capital element reducing the obligation to the lessor, and the finance costs being written off to the profit and loss account over the primary period of the lease. The assets are depreciated over the shorter of their estimated useful lives and the lease period.

All other leases are regarded as operating leases. Rental costs arising under operating leases are expensed over the term of the lease.

## notes to the financial statements continued

### 1 Accounting policies (continued)

#### (f) Investments

Investments held as fixed assets are stated at cost less any provision for impairment.

#### (g) Stocks

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

#### (h) Pension costs

Contributions to the AWG Plc group's defined benefit pension scheme are charged to the profit and loss account so as to spread the regular cost of pensions over the average service lives of employees, in accordance with the advice of an independent qualified actuary. Actuarial surpluses and deficits are amortised, where appropriate, over the average remaining service lives of employees. The cost of the defined contribution scheme is charged to the profit and loss account in the year in respect of which the contributions become payable. The notes to the accounts disclose the effect of the transitional provisions of FRS 17 'Retirement Benefits'.

#### (i) Research and development

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

#### (j) Foreign currencies

Transactions in foreign currencies are recorded at the rate of exchange at the date of the transactions or, if hedged forward, at the rate of exchange under the related forward currency contract.

#### (k) Deferred taxation

Deferred taxation is provided on timing differences, arising from the different treatment for accounts and taxation purposes of events and transactions recognised in the financial statements of the current and previous years. Deferred taxation is calculated at the rates at which it is estimated that taxation will arise. The deferred taxation balances are discounted using the post tax yields to maturity that could be obtained at the balance sheet date on Government bonds with maturity dates similar to those of the deferred taxation assets and liabilities. For assets with a life in excess of 30 years, the 30 year bond rate has been used as no other quoted rates are available.

*Deferred taxation is not provided in respect of timing differences arising from the sale or revaluation of fixed assets unless, by the balance sheet date, a binding commitment to sell the asset has been entered into and it is unlikely that any gain will be rolled over.*

Deferred taxation assets are recognised to the extent that it is regarded as more likely than not that there will be suitable taxable profits against which the deferred tax asset can be recoverable in future periods.

#### *Calculation of deferred tax on infrastructure assets:*

Infrastructure assets have an effectively unlimited life and a notional depreciation charge, the infrastructure renewal charge (IRC), is applied to the network (see note 1(c)).

For the purposes of estimating the deferred tax liability in relation to infrastructure assets, the useful life over which the underlying differences reverse is estimated by deflating the current cost based IRC to an appropriate deemed historic cost based depreciation charge.

#### (l) Bad debts

The bad debt provision is calculated based on applying expected recovery rates to an aged debt profile.

#### (m) Related party transactions

The group has taken advantage of the exemption not to disclose transactions with other members of the AWG Plc group under FRS 8 'Related Party Disclosures' as it is a wholly-owned subsidiary.

#### (n) Financial instruments

*Derivative instruments are used for hedging purposes in line with the group's risk management policy and no trading in financial instruments is undertaken.* Loans and other borrowings are recorded using the contracted rates implicit in the financial instruments used to hedge the group's exposure to fluctuations in currency rates. Similarly, interest is charged to the profit and loss account based on the contracted interest rates.

#### (o) Capitalisation of finance costs

Costs that are incurred directly in connection with the issue of a capital instrument are capitalised and amortised at a constant rate over the life of the underlying instruments.

#### (p) Provisions

Provisions of a long-term nature are discounted to reflect the time value of money in the estimated period over which the provision will be utilised. The rate of discount varies according to the nature of the underlying provision and further details are given in note 21. The unwinding of the discount on those provisions (other than deferred tax) is included within net interest payable.

### 2 Segmental analysis

The directors believe that the whole of the group's activities constitute a single class of business.

The group's turnover is wholly generated from within the United Kingdom.

	2004		2003	
	Total £m	Before operating exceptional items £m	Operating exceptional items £m	Total £m
3 Operating costs				
Operating costs before depreciation:				
Raw materials and consumables	21.3	20.9	–	20.9
Other operating costs	200.7	188.9	15.7	204.6
Staff costs (see note 9)	108.5	107.0	2.9	109.9
Own work capitalised	(39.0)	(35.3)	–	(35.3)
Contribution to Anglian Water Trust Fund	1.0	1.0	–	1.0
Profit on sale of fixed assets	(0.8)	–	–	–
Total operating costs before depreciation	291.7	282.5	18.6	301.1
Depreciation of tangible fixed assets	161.9	163.5	–	163.5
Amortisation of deferred grants and contributions	(5.9)	(6.6)	–	(6.6)
Depreciation net of amortisation of deferred grants and contributions	156.0	156.9	–	156.9
Total operating costs	447.7	439.4	18.6	458.0

The profit on sale of fixed assets relates to various sales of surplus land and assets.

	2004 £m	2003 £m
4 Exceptional items		
Operating costs:		
Restructuring costs	–	2.9
Refinancing project costs	–	15.7
	–	18.6
Charged / (credited) after operating profit:		
Profit on disposal of businesses	–	(3.3)
Profit on sale of fixed assets	–	(0.6)
Interest and finance charges	–	49.6
Total exceptional items	–	64.3
Taxation credit thereon	–	(17.5)

The restructuring costs in the prior year relate wholly to a reorganisation undertaken by the company during the year and comprise principally redundancy costs.

In the prior year the group completed a major refinancing project. The project costs of £15.7 million principally comprises legal and advisers' fees and banking costs incurred in respect of the refinancing of the regulated water business.

The prior year profit on sale of fixed assets relates to various sales of surplus land and assets.

The prior year exceptional interest charge of £49.6 million relates to the debt transfer and termination costs from the refinancing project referred to above. This includes a provision of £32.0 million for coupon enhancement and other related costs incurred on the transfer of debt.

	2004 £m	2003 £m
5 Operating profit		
Operating profit is stated after charging:		
Hire of plant and machinery	1.2	2.0
Other operating lease costs	10.0	9.9
Research and development expenditure	1.7	1.9
Fees paid to the auditors:		
– for statutory audit services (group and company)	0.1	0.1
– for regulatory audit services (company only)	0.1	0.1
– total audit services	0.2	0.2
– for other assurance services (group and company)	0.3	1.2
Total fees paid to the auditors	0.5	1.4

The fees paid to auditors for other assurance work largely relates to work undertaken on the Periodic Review 2004 and the Global Secured Medium Term Note Programme. The fees paid to auditors for other assurance work in the prior year principally relates to work undertaken on the refinancing project mentioned in note 4 above.

## notes to the financial statements continued

	2004 £m	2003 £m
6 Interest payable (net)		
Bank loans and overdrafts	–	1.9
Other loans including financing expenses	217.0	168.0
Indexation	30.9	17.7
Interest and financing charges – exceptional item	–	49.6
Finance leases	9.1	8.7
Unwinding of discount on coupon enhancement provision (see note 21)	0.4	0.7
Unwinding of discount on unfunded pension obligations (see note 21)	2.4	2.4
	<u>259.8</u>	<u>249.0</u>
Interest receivable from Anglian Water Services Holdings Limited	(193.6)	(129.6)
Other interest receivable	(16.5)	(13.6)
<b>Total interest payable (net)</b>	<u>49.7</u>	<u>105.8</u>

In the prior year interest of £23.2 million was payable to AWG Group Limited, a parent undertaking.

In the prior year interest of £7.3 million was receivable from AWG Group Limited, a parent undertaking.

£193.1 million of the interest received per the cash flow statement (see page 9) is from Anglian Water Services Holdings Limited.

	2004 £m	2003 £m
7 Taxation		
(a) <b>Analysis of tax (credit) / charge in the year</b>		
Current tax:		
UK Corporation Tax at 30 per cent (2003: 30 per cent)	–	38.8
Adjustments in respect of previous periods	(22.2)	(1.0)
<b>Total current tax (see note 7(b))</b>	<u>(22.2)</u>	<u>37.8</u>
Deferred tax:		
Charge for timing differences arising in year	23.6	13.2
Impact of discounting on deferred tax liability	(27.2)	(9.1)
Impact of (increase) / decrease in discount rates	(3.7)	17.7
Discounted effect of movements in Advance Corporation Tax	(3.7)	(7.2)
Adjustments in respect of previous periods	(0.3)	5.3
<b>Total deferred tax</b>	<u>(11.3)</u>	<u>19.9</u>
<b>Total tax (credit) / charge on profit on ordinary activities</b>	<u>(33.5)</u>	<u>57.7</u>
Analysed as:		
– before exceptional items	(33.5)	75.2
– exceptional items	–	(17.5)
<b>Total tax (credit) / charge on profit on ordinary activities</b>	<u>(33.5)</u>	<u>57.7</u>

(b) **Factors affecting tax (credit) / charge for the period**

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

	2004 £m	2003 £m
Profit on ordinary activities before tax	<u>269.2</u>	<u>166.9</u>
Profit on ordinary activities at the standard UK rate of tax (30 per cent)	80.7	50.1
Effects of:		
Items not deductible for tax purposes	(0.5)	1.7
Group relief not paid for	(57.1)	–
Accounting for depreciation not eligible for tax purposes	0.4	0.2
Capital allowances for the year in excess of depreciation	(19.4)	(5.6)
Short-term timing differences	(4.1)	(7.6)
Adjustments to tax charge in respect of previous period	(22.2)	(1.0)
<b>Current tax (credit) / charge for the year (see note 7(a))</b>	<u>(22.2)</u>	<u>37.8</u>

Based on capital investment plans for the current regulatory period, the group expects to continue to be able to claim tax relief on capital expenditure in excess of depreciation for the remainder of the regulatory period.

7 Taxation (continued)

The 'impact of (increase) / decrease in discount rates' results from movements in the post tax yield to maturity on UK Government bonds used to discount the gross deferred tax liability. If all UK gilt rates moved by 0.25 per cent a change in the tax charge of between £10.0 million to £15.0 million would occur.

It has been agreed in the current year that the company will not pay for tax losses surrendered to it by Anglian Water Services Holdings Limited. Adjustments in respect of previous periods arise from this agreement not to pay for losses and from the agreement of prior year computations.

	2004	2003
	£m	£m
8 Dividends		
Ordinary:		
Interim paid	47.0	54.0
Interim payable	–	35.0
Dividend paid within the Anglian Water Services Financing group	145.5	82.0
Dividend payable within the Anglian Water Services Financing group	48.1	47.6
Final payable	10.0	70.0
	250.6	288.6
Part of 2001 final dividend waived by AWG Group Limited	–	(799.2)
	250.6	(510.6)

A dividend of £193.6 million (2003: £129.6 million) is ultimately paid and payable to Anglian Water Services Holdings Limited, a parent undertaking, in order for it to service the interest payable to the company on the inter-company loan of £1,609.1 million (see note 15). £193.1 million of the dividend paid per the cash flow statement (see page 9) is ultimately paid to Anglian Water Services Holdings Limited.

	2004			2003
	Total	Before	Operating	Total
	£m	operating	exceptional	£m
		exceptional	items	
		items	£m	
9 Employee information				
Staff costs:				
Wages and salaries	91.3	90.4	1.9	92.3
Social security costs	7.6	8.9	–	8.9
Pension costs (see note 26)	9.6	7.7	1.0	8.7
	108.5	107.0	2.9	109.9

Pension costs are stated after crediting £2.4 million (2003: £2.4 million) in respect of the amortisation of an actuarial surplus in the main UK pension scheme.

Staff costs in the current year include £4.7 million (£2.6 million of wages and salaries and £2.1 million of pension costs) of redundancy costs relating wholly to a reorganisation undertaken by the group.

Average number of full-time equivalent persons employed:

	2004	2003
Number employed	3,492	3,588

10 Profit of parent company

The company has not presented its own profit and loss account as permitted by Section 230 of the Companies Act 1985. Profit for the financial year (see note 25) dealt with in the financial statements of the parent company is £299.9 million (2003: £106.4 million).

11 Non-Executive Directors' fees

The fees for the Non-Executive Directors, other than Peter Hickson and Jonson Cox, are set by the board. These fees are £30,000 per annum (pa) (2003: £25,000 pa).

Richard Jewson receives an additional £10,000 pa (2003: £9,000 pa) for acting as Deputy Chairman and an additional £nil (2003: £6,000 pa) for chairing the Audit Committee.

Robert Napier receives an additional £6,000 pa (2003: £6,000 pa) for chairing the Sustainable Development Committee and an additional £nil (2003: £3,000 pa) for membership of the Audit Committee.

Roger Witcomb receives an additional £3,000 pa (2003: £3,000 pa) for acting as the company's customer service representative at WaterVoice (a customer liaison watchdog) and an additional £nil (2003: £3,000 pa) for membership of the Audit Committee.

The Non-Executive Directors, other than Peter Hickson and Jonson Cox, do not receive benefits or pension contributions from the AWG Plc group, nor do they participate in any of the AWG Plc group's incentive schemes.



## notes to the financial statements continued

### 12 Directors' emoluments

The emoluments of Peter Hickson and Jonson Cox were paid by AWG Group Limited and the following percentages of their total emoluments – Peter Hickson nil per cent (2003: nil per cent) and Jonson Cox 10 per cent (2003: nil per cent) – were charged by AWG Group Limited to the group. All the other directors were paid direct by the group. 10 per cent (2003: nil per cent) of Roy Pointer's emoluments were recharged by the group to AWG Group Limited.

The emoluments of the directors of the group for their services as directors of the group are set out below (rounded to the nearest thousand pounds).

					2004	2003
	Salary £000	Benefits in kind £000	Annual Bonus <sup>(a)</sup> £000	Other £000	Total £000	Total £000
<b>Chairman</b>						
Peter Hickson (appointed 17 April 2003)	–	–	–	–	–	–
<b>Executive Directors</b>						
Roy Pointer	207	22	83	1	313	434
Colin Brown	130	16	37	9	192	238
David Hipple	140	11	43	–	194	224
<b>Non-Executive Directors</b>						
Jonson Cox (appointed 29 January 2004)	9	–	6	2	17	–
Richard Jewson	40	1	–	–	41	41
Robert Napier	36	–	–	–	36	34
Roger Witcomb	33	–	–	–	33	31
	595	50	169	12	826	1,002

(a) The maximum annual bonus is 50 per cent of salary.

The amount of pension entitlements earned, the accrued pension liabilities and the changes therein during the year to 31 March 2004 are summarised below in accordance with the Companies Act 1985 and the Listing Rules of the Financial Services Authority (rounded to the nearest thousand pounds). The table shows the full amounts for each of the directors for their services to the AWG Plc group. The pension liabilities are calculated using the cash equivalent transfer value method, which is the method adopted in the Listing Rules of the Financial Services Authority (rounded to the nearest thousand pounds).

	Accrued pension 2004 £000 <sup>(1)</sup>	Increase in accrued pension 2004 £000	Accrued lump sum 2004 £000 <sup>(2)</sup>	Increase in accrued lump sum 2004 £000	Increase in transfer value less directors contributions 2004 £000 <sup>(3)</sup>	Transfer value at 2004 £000	Transfer value at 2003 £000	Accrued pension 2003 £000 <sup>(1)</sup>	Accrued lump sum 2003 £000 <sup>(2)</sup>
Roy Pointer	118	9	308	32	279	2,388	2,109	109	276
Colin Brown	39	3	–	–	94	482	385	36	–
David Hipple	35	3	–	–	82	400	315	32	–

	Additional accrued pension in year (excluding inflation) £000	Additional accrued lump sum in the year (excluding inflation) £000	Transfer value of the increase in benefits (excluding inflation) £000 <sup>(4)(5)</sup>
Roy Pointer	7	24	149
Colin Brown	2	–	27
David Hipple	2	–	22

(1) The accrued pension entitlement shown is that which is payable at normal retirement age based on service to the end of the respective financial year.

(2) The accrued lump sum shown is that which is payable at normal retirement age based on service to the end of the respective financial year.

(3) The transfer values of increases has been calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11.

(4) The transfer value of the increase in benefits includes adjustment of pensions to reflect salary increases granted on promotion as well as, where relevant, the value of benefits on improvement award.

(5) Excluding directors' contributions.

The emoluments and pension entitlements of Peter Hickson and Jonson Cox in relation to the services rendered in connection with the AWG Plc group are disclosed in the AWG Plc Annual Report and Accounts.

The transfer values disclosed in the two tables above are actuarially determined to provide for pensions liability and not sums paid by the AWG Plc group or the company to the individuals concerned. They cannot meaningfully be added to their annual remuneration.

13 Directors' interests in shares and contracts

The beneficial interests in shares and options for Peter Hickson, Jonson Cox and Roy Pointer are the same as, and not additional to, those disclosed in the AWG Plc Annual Report and Accounts.

Directors have the right to participate in the employee Sharesave Scheme.

Details of directors' options are available in the AWG Plc group's Register of Directors' Interests, which is open to inspection.

The interests of the directors in the shares of AWG Plc and in options over such shares granted under that company's Executive Share Option Scheme, annual bonus scheme, Long-Term Incentive Plan and Sharesave Scheme are set out below.

Throughout this note, all interests in shares as at 31 March 2004 are in relation to AWG Plc ordinary shares of 19<sup>1</sup>/<sub>2</sub> pence each.

Beneficial and family interests in shares:	31 March 2004 No. of shares	31 March 2003 No. of shares
Peter Hickson	54,647	36,875
Roy Pointer	18,147	17,094
Colin Brown	-	-
Jonson Cox	5,000	-
David Hipple	-	-
Richard Jewson	393	490
Robert Napier	-	-
Roger Witcomb	-	-

The figures include ordinary shares held in trust for directors as the share element of the annual bonus scheme, being at 31 March 2004 (with 31 March 2003 figures in brackets), Roy Pointer 4,332 (1,735).

The contingent interests of Roy Pointer (2003: 42,569 shares) and Colin Brown (2003: 15,225 shares) in shares under the AWG Plc group's Long-Term Incentive Plan have lapsed during the year and they now have no contingent interest in any shares under the plan. No other Executive Director has an interest in any shares under the plan.

Roy Pointer holds £30,000 (2003: £30,000) in bonds issued by Anglian Water Services Financing Plc (£275 million class B bond at 7.882 per cent interest until 2012).

The maximum contingent interest of Executive Directors in shares under the matching share element of the AWG Plc group annual retained bonus scheme is as follows:

	1 April 2003	Granted	31 March 2004	Outstanding awards
Roy Pointer	2,716	5,857	8,573	from 9 July 2005

Matching shares were allocated on 11 July 2003 at a share price of £5.61. The release of the matching shares is subject to the achievement of the performance conditions outlined in the AWG Plc Annual Report and Accounts 2004.

Options to subscribe for ordinary shares, under the Sharesave and Executive Share Option Schemes, granted to and exercised by directors during the year, including exercise dates, are summarised below.

	Options outstanding at 1 April 2003	Options granted		Options exercised,		Options outstanding at 31 March 2004	Exercise period for outstanding options		
	Number	Number	Option price (£)	Number	Option price (£)	Number	Weighted average exercise price (£)	From	To
Sharesave Scheme									
Roy Pointer	3,251	1,293	4.28	892	4.34	3,652	4.14	01/04/04	30/09/07
Executive Share Option Scheme <sup>(2)</sup>									
Roy Pointer	243,480 <sup>(1)</sup>	127,777 <sup>(1)</sup>	5.40	-	-	371,257	5.35	15/08/97	31/07/13
Jonson Cox	-	228,136 <sup>(1)</sup>	5.26	-	-	228,136	5.26	16/01/07	16/01/14

(1) Includes 10,418 options granted to Roy Pointer prior to 1996 that are not subject to performance targets.

(2) Under the Scheme, each participant receives annual options grants, equating to a percentage of base salary, which varies according to seniority up to a maximum of 3x basic salary each year. The exercise of options depends on the AWG Plc group's earnings per share growth relative to inflation, which the AWG Remuneration Committee considers to be the most appropriate way of measuring the AWG Plc group's underlying financial performance. To date no options have been exercised under the Scheme.

(3) Jonson Cox was granted 5,703 options under the Executive Share Option Scheme and 222,433 "Phantom Awards" under a schedule (Grants of Phantom Awards) to that scheme.

On 7 July 2003 Roy Pointer exercised 892 Sharesave options at the option price of £4.34. The mid-market closing price at the date of exercise was £5.57.

## notes to the financial statements continued

### 13 Directors' interests in shares and contracts (continued)

On 1 April 2004 Roy Pointer exercised 1,241 Sharesave options at the option price of £4.68. The mid market closing price at the date of exercise was £5.50.

On 2 June 2004 Jonson Cox bought 2,500 ordinary shares at a price of £6.24.

On 2 June 2004 Jonson Cox and Roy Pointer bought 1,927 and 1,220 ordinary shares respectively and were awarded 3,212 and 2,034 matching shares respectively in accordance with the annual retained bonus scheme (ARBS).

On 10 June 2004 Roy Pointer's entitlement under the ARBS was corrected by his purchase of 1,735 shares at £6.17 and the award of a further 2,892 matching shares at the price extant at 2 June 2004 (£6.225).

The market price of shares in AWG Plc at 31 March 2004 was £5.49, and the range during the year was £4.51 to £5.69.

No director has an interest in the shares or debentures of the group or any other AWG Plc group company other than as shown above.

Options granted under the Sharesave Scheme are exercisable within a period of six months after either the third, fifth or seventh anniversary of the date of the savings contract. Options granted under the Executive Share Option Scheme are exercisable during a period commencing on the third anniversary and ending on the tenth anniversary of the date of grant. The outstanding options, dates of grant and the option prices are set out below.

	No. of ordinary shares	Date of grant	Option price
Sharesave Scheme	25,528	12 December 1996	£4.52
Sharesave Scheme	41,769	10 December 1997	£6.19
Sharesave Scheme	66,886	9 December 1998	£7.12
Sharesave Scheme	513,651	12 January 2000	£4.34
Sharesave Scheme	706,213	31 January 2001	£4.68
Sharesave Scheme	897,837	6 February 2002	£4.20
Sharesave Scheme	3,039,404	31 January 2003	£3.38
Sharesave Scheme	1,108,034	5 February 2004	£4.28
Executive Share Option Scheme	17,999	15 August 1994	£5.375
Executive Share Option Scheme	5,253	10 June 1996	£5.71
Executive Share Option Scheme	9,090	7 November 1996	£5.50
Executive Share Option Scheme	1,485,918	21 December 2001	£5.27
Executive Share Option Scheme	1,536,427	9 July 2002	£5.38
Executive Share Option Scheme	1,702,732	31 July 2003	£5.40
Executive Share Option Scheme	5,703	16 January 2004	£5.26
Phantom Executive Share Option Scheme	222,433	16 January 2004	£5.26

No director had during the year, or has, a material interest in any contract of significance to which the group was a party.

### 14 Tangible fixed assets

	Group and Company				Total £m
	Land and buildings £m	Infrastructure assets £m	Operational structures £m	Vehicles, plant and equipment £m	
<b>Cost</b>					
At 1 April 2003	59.0	2,055.3	2,255.1	1,115.5	5,484.9
Additions	0.2	91.0	67.6	118.1	276.9
Disposals	(0.1)	(0.9)	(2.0)	(1.2)	(4.2)
<b>At 31 March 2004</b>	<b>59.1</b>	<b>2,145.4</b>	<b>2,320.7</b>	<b>1,232.4</b>	<b>5,757.6</b>
<b>Grants and contributions</b>					
At 1 April 2003	-	162.6	-	-	162.6
Additions	-	9.9	-	-	9.9
<b>At 31 March 2004</b>	<b>-</b>	<b>172.5</b>	<b>-</b>	<b>-</b>	<b>172.5</b>
<b>Depreciation</b>					
At 1 April 2003	26.2	361.0	658.9	579.5	1,625.6
Charge for the year	2.5	27.0	86.0	46.4	161.9
Disposals	-	(0.7)	(2.0)	(1.2)	(3.9)
<b>At 31 March 2004</b>	<b>28.7</b>	<b>387.3</b>	<b>742.9</b>	<b>624.7</b>	<b>1,783.6</b>
<b>Net book amount</b>					
At 31 March 2004	30.4	1,585.6	1,577.8	607.7	3,801.5
At 31 March 2003	32.8	1,531.7	1,596.2	536.0	3,696.7

Tangible fixed assets at 31 March 2004 include £215.4 million of assets in the course of construction (2003: £216.3 million) and also include land of £16.4 million (2003: £16.0 million) which is not subject to depreciation. The group's interests in land and buildings are almost entirely freehold.

The net book value of tangible fixed assets held under finance leases at 31 March 2004 was £136.4 million (2003: £151.8 million). Depreciation charged on assets held under finance leases during the year ended 31 March 2004 amounted to £15.3 million (2003: £18.6 million).

14 Tangible fixed assets (continued)

**Capital commitments**

The group has a substantial long-term investment programme, which includes expenditure to meet regulatory requirements, shortfalls in performance and condition and to provide for new demand and growth. The commitments shown below reflect only the value of orders placed at 31 March 2004.

	2004 £m	2003 £m
Contracted for but not provided in the financial statements	79.7	55.6

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
15 Fixed asset investments				
Shares at cost in participating interests	0.2	0.1	0.2	0.1
Loan to Anglian Water Services Holdings Limited	1,609.1	1,609.1	1,609.1	1,609.1
Other loans	-	0.1	-	0.1
	<b>1,609.3</b>	<b>1,609.3</b>	<b>1,609.3</b>	<b>1,609.3</b>

A loan of £1,609.1 million, made by the company to Anglian Water Services Holdings Limited, is repayable on the later of 30 July 2038 and another date being the next interest payment date following the date which is two years and one day after the final maturity date of the longest dated bond issued from time to time by Anglian Water Services Financing Plc. Interest on the loan is calculated at 12 per cent per annum.

The sole subsidiary, which is 100 per cent owned, and is registered, incorporated and operating in the United Kingdom at 31 March 2004 is Anglian Water Services Financing Plc whose principal activity is that of a financing company.

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
16 Stocks				
Raw materials and consumables	6.6	4.6	6.6	4.6

The current replacement value of stocks does not materially exceed the historical costs stated above.

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
17 Debtors				
<b>Amounts falling due within one year</b>				
Trade debtors	77.1	84.1	77.1	84.1
Amounts owed by other group undertakings	48.6	48.9	87.5	64.1
Other debtors	16.7	12.6	15.0	12.4
Prepayments and accrued income	57.1	79.7	57.1	79.7
	<b>199.5</b>	<b>225.3</b>	<b>236.7</b>	<b>240.3</b>
<b>Amounts falling due after more than one year</b>				
Prepaid pension contributions	53.5	38.9	53.5	38.9
	<b>253.0</b>	<b>264.2</b>	<b>290.2</b>	<b>279.2</b>

Prepayments and accrued income as at 31 March 2004 includes water and wastewater income not yet billed of £51.2 million (2003: £71.7 million).

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
18 Creditors: amounts falling due within one year				
Current portion of long-term loans	4.7	2.2	4.7	2.2
Obligations under finance leases	17.3	25.2	17.3	25.2
Short-term borrowings	22.0	27.4	22.0	27.4
	<b>44.0</b>	<b>54.8</b>	<b>44.0</b>	<b>54.8</b>
Trade creditors	87.4	86.1	87.4	86.1
Amounts owed to other group undertakings	2.1	1.0	2.3	1.1
Receipts in advance	62.0	64.2	62.0	64.2
Corporation tax	25.4	47.2	24.4	46.0
Other taxation and social security	3.0	3.1	3.0	3.1
Deferred grants and contributions	5.8	5.6	5.8	5.6
Accruals	100.3	89.9	100.3	89.9
Dividend payable	58.1	152.6	58.1	152.6
Other creditors	344.1	449.7	343.3	448.6

Receipts in advance includes £49.6 million (2003: £52.2 million) relating to amounts received from customers for water and wastewater charges in respect of the following year.

## notes to the financial statements continued

### 19 Loans, other borrowings and financial instruments

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
<b>Loans and other borrowings</b>				
£150m 8.25% fixed rate 2006 (h)	150.0	150.0	150.0	150.0
£150m 'mark to market' adjustment (e), (h)	8.1	11.2	8.1	11.2
£100m 5.5% index linked 2008 (c), (h)	153.6	149.5	153.6	149.5
£100m 12.375% fixed rate 2014 (h)	100.0	100.0	100.0	100.0
£250m 5.837% fixed rate 2022 (h)	250.0	250.0	250.0	250.0
£200m 6.875% fixed rate 2023 (h)	200.0	200.0	200.0	200.0
£200m 6.625% fixed rate 2029 (h)	200.0	200.0	200.0	200.0
£246m 6.293% fixed rate 2030 (h)	246.0	246.0	246.0	246.0
£275m 7.882% fixed rate 2012/2037 (h), (i)	275.0	275.0	275.0	275.0
£150m 4.125% index linked 2020 (c), (h)	164.9	160.3	164.9	160.3
£75m 3.666% index linked 2024 (c), (h)	78.6	76.4	78.6	76.4
£200m 3.07% index linked 2032 (c), (h)	209.6	203.8	209.6	203.8
£60m 3.07% index linked 2032 (c), (h)	62.8	61.1	62.8	61.1
£50m LIBOR plus 1.2% floating rate 2007/2012 (h), (i)	50.0	50.0	50.0	50.0
£180m LIBOR plus 1.25% floating rate 2009/2014 (h), (i)	180.0	180.0	180.0	180.0
£100m LIBOR plus 2.8% floating rate 2010/2037 (h), (i)	100.0	100.0	100.0	100.0
Finance leases	154.1	178.5	154.1	178.5
Other fixed rate loans	0.1	0.2	0.1	0.2
£150m index linked swap 2024 (f), (h)	6.7	2.6	6.7	2.6
£175m index linked swap 2030 (f), (h)	7.8	3.2	7.8	3.2
£258m index linked swap 2013 (f), (h)	3.8	–	3.8	–
£ loan costs (d)	(18.2)	(19.0)	(18.2)	(19.0)
€350m 5.375% fixed rate 2009 (a), (h)	229.3	229.3	229.3	229.3
€650m 4.625% fixed rate 2013 (a), (h)	453.2	–	453.2	–
€115m EURIBOR plus 2.8% floating rate 2037 (a), (h)	74.0	74.0	74.0	74.0
€ loan costs (d)	(2.1)	(1.0)	(2.1)	(1.0)
US\$40m 6.57% private placements 2005 (a), (h)	28.4	28.4	28.4	28.4
US\$4m 7.21% private placements 2006 (a), (h)	1.6	2.2	1.6	2.2
US\$4m 'mark to market' adjustment (e), (h)	0.1	0.1	0.1	0.1
US\$55m 6.85% private placements 2006 (a), (h)	35.8	35.8	35.8	35.8
US\$35m 6.65% private placements 2006 (a), (h)	24.9	24.9	24.9	24.9
US\$400m LIBOR plus 0.4% floating rate 2007 (a), (h)	254.8	254.8	254.8	254.8
US\$100m 7.01% private placements 2008 (a), (h)	71.0	71.0	71.0	71.0
US\$25m 7.07% private placements 2009 (a), (h)	16.0	16.0	16.0	16.0
US\$25m 'mark to market' adjustment (e), (h)	0.7	0.8	0.7	0.8
US\$23m 7.13% private placements 2009 (a), (h)	16.3	16.3	16.3	16.3
US\$195m 7.23% private placements 2011 (a), (h)	138.5	138.5	138.5	138.5
US\$ loan costs (d)	(2.8)	(3.6)	(2.8)	(3.6)
Total loans and other borrowings	3,922.6	3,466.3	3,922.6	3,466.3
Less amounts included in creditors falling due within one year	(22.0)	(27.4)	(22.0)	(27.4)
Loans and other borrowings due after more than one year	3,900.6	3,438.9	3,900.6	3,438.9

EURIBOR is the 'European Inter Bank Offer Rate'. LIBOR is the 'London Inter Bank Offer Rate'.

- (a) The group has entered into swap agreements which eliminate the risk of currency fluctuations in relation to the US\$ and Euro loans. The adjustment to the US\$ loans is £(111.3) million (2003: £(32.8) million) and the adjustment to the Euro loans is £11.3 million (2003: £17.2 million).
- (b) The group has entered into swap agreements that convert its debt into either floating rate, fixed rate or index linked debt in accordance with the group's hedging policy (see page 22).
- (c) The value of the capital and interest elements of the index linked loans are linked to movements in the Retail Price Index (RPI). The total increase in the capital value of index linked loans during the year of £18.4 million (2003: £11.9 million) has been taken to the profit and loss account as part of interest payable.
- (d) These costs are amortised at a constant rate on the carrying amount of debt over the life of the underlying instruments.
- (e) 'Mark to market' adjustments relate to back-to-back debt reassigned from AWG Group Limited to Anglian Water Services Financing Plc in July 2002 at fair value rather than book value. The difference between the book value and fair value is being amortised at a constant rate on the carrying amount of debt over the remainder of its life.

19 Loans, other borrowings and financial instruments (continued)

- (f) The group has entered into three index linked interest rate swap agreements. The values of the notional capital on these swaps are linked to movements in the RPI. The increase in the notional capital value is payable at the final maturity date of the swaps. The increase for the current year of £12.5 million (2003: £5.8 million) has been taken to the profit and loss account as part of interest payable.
- (g) The group has entered into two forward starting interest rate swaps commencing in 2007 and maturing in 2010 which have the effect of increasing the level of fixed rate debt for that period to a level consistent with the group's hedging policy.
- (h) These loans are 'back-to-back' inter-group loans from Anglian Water Services Financing Plc to the company.  
Under the company / Anglian Water Services Financing Plc loan agreement, Anglian Water Services Financing Plc onlends an equal amount to the sterling equivalent of each bond to the company on identical items. Therefore each individual 'back-to-back' inter-group loan has been separately disclosed. Anglian Water Services Financing Plc charges the company an annual management fee in respect of entering into the company / Anglian Water Services Financing Plc loan agreement.
- (i) Legal maturity of these instruments is the second of the years quoted. Coupons 'step-up' is in the first of the years quoted.
- (j) Under a security agreement dated 30 July 2002 between Anglian Water Services Financing Plc, the company, Anglian Water Services Overseas Holdings Limited, Anglian Water Services Holdings Limited and Deutsche Trustee Company Limited (as Agent and Trustee for itself and each of the Finance Parties to the Global Secured Medium Term Note Programme) creates a fixed and floating charge over the assets of the company to the extent permissible under the Water Industry Act 1991. In addition there is a fixed charge over the issued share capital of Anglian Water Services Financing Plc, the company and Anglian Water Services Overseas Holdings Limited. At 31 March 2004 this charge applies to £3,922.6 million (2003: £3,466.3 million) of the group debt shown on page 20.

For the company the current and long-term borrowings can be analysed as follows:

	2004		2003	
	Creditors < 1 year £m	Creditors > 1 year £m	Creditors < 1 year £m	Creditors > 1 year £m
Amounts owed to group undertakings ('back-to-back' inter-group loans)	6.5	3,785.0	3.9	3,307.3
Debt issue costs	(1.8)	(21.3)	(1.7)	(21.9)
Obligations under finance leases	17.3	136.8	25.2	153.3
Other loans	–	0.1	–	0.2
	22.0	3,900.6	27.4	3,438.9

**Maturity analysis of financial liabilities**

	Group and Company	
	2004 £m	2003 £m
Less than one year	25.9	30.9
Between one and two years	92.6	26.7
Between two and five years	722.0	587.9
After five years	3,107.6	2,850.3
	3,948.1	3,495.8

Included above are amounts due under finance leases of £17.3 million (2003: £25.2 million) payable within one year, £20.5 million (2003: £18.6 million) payable between one and two years, £54.1 million (2003: £73.1 million) payable between two and five years and £62.2 million (2003: £61.6 million) payable after five years. The above maturity profile is determined by reference to the fixed dates on which the liability falls due.

In addition to loans and finance leases the above analysis includes other financial liabilities (including overdrafts, long-term creditors, accruals and provisions) totalling £25.5 million (2003: £29.5 million), of which £3.8 million falls due in less than one year (2003: £3.5 million). This analysis is net of issue costs totalling £23.1 million (2003: £23.6 million).

**Borrowing facilities**

The group has the following unused committed borrowing facilities:

	Group	
	2004 £m	2003 £m
Expiring within one year	304.0	283.0
Expiring between one and two years	225.0	–
Expiring between two and five years	–	225.0
	529.0	508.0

## notes to the financial statements continued

### 19 Loans, other borrowings and financial instruments (continued)

#### Control of treasury

The Treasury Team, who report direct to the group's Finance Director, substantially direct the group financing, including debt, interest costs and foreign exchange. Treasury policy continues to be focused on the efficient and effective management of cash and financial resources within the group. The treasury function will actively endeavour to:

- ensure that lenders covenants are met;
- secure funds through a balanced approach to financial markets and maturities;
- manage interest rates to minimise financial exposures and minimise interest costs;
- invest temporary surplus cash to best advantage at minimal financial risk;
- maintain an excellent reputation with providers of finance and rating agencies;
- promote management techniques and systems; and
- enhance control of financial resources.

#### Management of financial risk

Financial risks faced by the group include funding, interest rate, contractual and currency risks. The board of the group regularly reviews these risks and has approved written policies covering treasury strategy and the use of financial instruments to manage risks. The last review was in May 2003 and treasury matters are reported to the board each month.

During the year a Treasury Advisory Group (TAG) was established comprising the group Finance Director, the group Treasurer and a Non-Executive Director of the company, together with the same position holders at the ultimate shareholder AWG Plc. The TAG meets monthly with the specific remit of reviewing treasury matters.

The group aims to meet its funding requirements primarily through public bond markets, private placements, bank loans and finance leases. Surplus cash is invested in short-term bank deposits and AAA rated money funds.

The group also enters into derivative transactions (principally currency and interest rate swaps) to manage the interest rate and currency risks arising from the treasury policy.

To ensure continued effectiveness and relevance, the board formally review the organisation and reporting annually.

#### Borrowing covenants

With the exception of asset-based funding all the group's borrowings are raised by Anglian Water Services Financing Plc and guaranteed by the Anglian Water Services Financing group. The group treasury function monitors compliance against all financial obligations and it is the group's policy to manage the consolidated balance sheet so as to ensure operation within covenanted restrictions.

#### Foreign currency

The group has currency exposures resulting from debt raised in currencies other than sterling and very small purchases in foreign currencies. The group uses a range of instruments to hedge such exposures. All hedges are undertaken for commercial reasons with the objective of minimising the impact of exchange rate fluctuations on net assets and profits.

#### Financial instruments disclosures

Short-term debtors and creditors have been excluded from this note except for the comments on currency exposures to the financial statements.

#### Currency exposures

The group has no material unhedged monetary assets and liabilities denominated in a currency different from the local currency of the particular operation.

#### Fair value of financial assets and financial liabilities

The fair value of the group's financial instruments at 31 March was:

	2004		2003	
	Book value £m	Fair value £m	Book value £m	Fair value £m
Cash at bank and in hand	471.7	471.7	176.9	176.9
Short-term borrowings	(23.3)	(23.8)	(9.6)	(9.6)
Long-term borrowings	(3,758.1)	(4,087.4)	(3,435.4)	(3,833.7)
Currency and interest rate swaps and forward exchange contracts	(141.2)	(175.6)	(21.3)	(33.2)
Net debt	(3,450.9)	(3,815.1)	(3,289.4)	(3,699.6)
Fixed asset investments	1,609.3	1,930.9	1,609.3	2,145.5
Provisions excluding deferred tax and pension obligations (see note 21)	(25.5)	(25.5)	(29.5)	(29.5)
	(1,867.1)	(1,909.7)	(1,709.6)	(1,583.6)

The fair value of loans and other borrowings represents the market value of publicly traded debt instruments or, if in respect of private debt, the cost which the group would incur if it elected to repay these borrowings before their maturity dates, calculated by discounting future cash flows at prevailing rates. In the fair value table above, the book values assigned to derivative instruments are separately analysed from the book values of the underlying loans.

In accordance with the group's accounting policy, long-term borrowings are recorded using the contracted rates implicit in the financial instruments used to hedge the group's exposure to fluctuations in currency and interest rates.

Interest is charged to the profit and loss account based on the contracted interest rates. To determine the fair value of interest rate swaps for inclusion in the above table, a calculation was made of the net gain or loss which would have arisen if these contracts had been terminated on 31 March 2004. The value at that date was determined by market interest rates, which fluctuate over time. The fair value of the group's fixed asset investments is calculated by discounting cash flows at prevailing rates reflecting the relative risks involved. The group has also entered into swap arrangements to hedge overseas investments.

The fair value of the group's provisions and other financial liabilities has been estimated as not materially different from the book value.

Unrecognised gains and losses on hedges	2004 Gains	2004 Losses	2004 Net	2003 Gains	2003 Losses	2003 Net
	£m	£m	£m	£m	£m	£m
Unrecognised at 1 April	13.6	(61.8)	(48.2)	22.4	(8.2)	14.2
Reversal of items unrecognised at 1 April	(0.2)	18.5	18.3	(22.4)	4.4	(18.0)
Recognised during the year	(0.1)	–	(0.1)	(6.4)	3.8	(2.6)
Arising during the year	18.6	(23.0)	(4.4)	20.0	(61.8)	(41.8)
Unrecognised at 31 March	31.9	(66.3)	(34.4)	13.6	(61.8)	(48.2)

Gains and losses on instruments used for hedging are not recognised until the exposure that is being hedged is itself recognised. The total net unrecognised loss of £34.4 million (2003: net loss £48.2 million) principally represents the opportunity cost of protecting the group charge against movements in interest rates at a time when interest rates were higher than at 31 March 2004.

Of the unrecognised gains and losses at 31 March 2004, a net gain of £3.2 million (2003: loss of £3.3 million) is expected to be included in the profit and loss account for the year ended 31 March 2005 and the balance in future years.

#### Currency and interest rate analysis of net financial assets / (liabilities) at 31 March 2004

	Total £m	Index linked £m	Floating rate £m	Fixed rate £m	Financial assets on which no interest is paid £m	Fixed Rate	
						Weighted average interest rate %	Weighted average years to maturity
Sterling	(3,922.6)	(1,270.8)	(200.4)	(2,465.7)	14.3	6.9	11.2
US Dollar	–	–	–	–	–	–	–
Euro	–	–	–	–	–	–	–
Total borrowings	(3,922.6)	(1,270.8)	(200.4)	(2,465.7)	14.3	–	–
Sterling	471.7	–	471.7	–	–	–	–
US Dollar	–	–	–	–	–	–	–
Euro	–	–	–	–	–	–	–
Cash, deposits and current asset investments	471.7	–	471.7	–	–	–	–
Net debt	(3,450.9)	(1,270.8)	271.3	(2,465.7)	14.3	–	–
Fixed asset investments	1,609.3	–	–	1,609.1	0.2	–	–
Provisions	(25.5)	–	–	–	(25.5)	–	–
Net financial liabilities	(1,867.1)	(1,270.8)	271.3	(856.6)	(11.0)	–	–



## notes to the financial statements continued

### 19 Loans, other borrowings and financial instruments (continued)

#### Currency and interest rate analysis of net financial assets / (liabilities) at 31 March 2003

	Total £m	Index linked £m	Floating rate £m	Fixed rate £m	Financial assets on which no interest is paid £m	Fixed rate	
						Weighted average interest rate %	Weighted average years to maturity
Sterling	(3,466.3)	(981.9)	(5.2)	(2,490.8)	11.6	6.9	12.1
US Dollar	-	-	-	-	-		
Euro	-	-	-	-	-		
<b>Total borrowings</b>	<b>(3,466.3)</b>	<b>(981.9)</b>	<b>(5.2)</b>	<b>(2,490.8)</b>	<b>11.6</b>		
Sterling	176.9	-	176.9	-	-		
US Dollar	-	-	-	-	-		
Euro	-	-	-	-	-		
<b>Cash, deposits and current asset investments</b>	<b>176.9</b>	<b>-</b>	<b>176.9</b>	<b>-</b>	<b>-</b>		
<b>Net debt</b>	<b>(3,289.4)</b>	<b>(981.9)</b>	<b>171.7</b>	<b>(2,490.8)</b>	<b>11.6</b>		
Fixed asset investments	1,609.3	-	-	1,609.2	0.1		
Provisions	(29.5)	-	-	-	(29.5)		
<b>Net financial liabilities</b>	<b>(1,709.6)</b>	<b>(981.9)</b>	<b>171.7</b>	<b>(881.6)</b>	<b>(17.8)</b>		

The above tables reflect the net position after swap arrangements, the most significant effect of which is to swap US\$877 million (2003: US\$877 million) and €1,115 million (2003: €465 million) into sterling. Fixed rate loans are those for which the interest rate was fixed for more than 12 months at 31 March 2004 and 31 March 2003.

Floating rate cash and investments earn interest based on the London Inter Bank Bid rate (LIBID) for the relevant currency. Floating rate borrowings incur interest based on LIBOR.

### 20 Other creditors falling due after more than one year

Deferred grants and contributions

	Group		Company	
	2004 £m	2003 £m	2004 £m	2003 £m
	90.0	87.4	90.0	87.4

### 21 Provisions for liabilities and charges

At 1 April 2003  
Unwinding of discount  
Utilised in the year  
At 31 March 2004

	Group and Company			
	Coupon enhancement provision £m	Unfunded pension obligations £m	Deferred tax £m	Total £m
At 1 April 2003	29.5	26.2	108.3	164.0
Unwinding of discount	0.4	2.4	-	2.8
Utilised in the year	(4.4)	(2.1)	(11.3)	(17.8)
At 31 March 2004	25.5	26.5	97.0	149.0

The coupon enhancement provision relates to coupon enhancement and other related costs incurred on the transfer of debt from AWG Group Limited to Anglian Water Services Financing Plc at the end of the refinancing exercise. The provision is expected to be utilised over the next 25 years and has been discounted at 6.1 per cent which represents the adjusted credit risk of additional coupon payments following the transfer of debt from AWG Group Limited.

The provision for pension obligations relates to the cost of unfunded pension enhancements. These pension payments are expected to be made over several future accounting periods. The provision is determined using actuarial assumptions based on those used for the valuation of the AWG Pension Scheme (AWGPS) and has been discounted at a rate of 9.0 per cent (2003: 9.0 per cent).

The deferred tax provision is analysed in note 22. The effect of discounting on deferred tax is shown in note 7.

22 **Deferred taxation**

The total tax charge or credit in the current year includes provisions for discounted deferred taxation. Consequently, changes in the medium-term and long-term interest rates used to discount deferred taxation assets and liabilities can affect the amount of deferred taxation charged or credited in the profit and loss account.

The deferred tax liability is stated net of Advance Corporation Tax (ACT) recoverable. If changes in the tax legislation were introduced which restricted the ability of companies to use ACT, this asset may no longer be recoverable and in this event, an additional tax charge would arise in the profit and loss account of £64.8 million.

	Group and Company	
	£m	
At 1 April 2003	108.3	
Deferred tax credited to the profit and loss account (see note 7)	(11.3)	
At 31 March 2004	97.0	

	Group and Company	
	2004	2003
	£m	£m
Accelerated capital allowances	742.2	727.1
Short-term timing differences	(6.6)	(10.7)
Surplus ACT asset	(144.0)	(119.9)
Undiscounted provision for deferred tax	591.6	596.5
Discount	(494.6)	(488.2)
Discounted provision for deferred tax	97.0	108.3

23 **Commitments under operating leases**

At 31 March 2004 the group and the company had commitments to make payments during the next 12 months under non-cancellable operating leases which expire as follows:

	Group and Company			
	2004		2003	
	Land and buildings	Other	Land and buildings	Other
	£m	£m	£m	£m
Within one year	–	1.3	–	1.1
Between one and five years	–	3.5	–	5.0
After five years	3.4	1.9	3.2	0.5
	3.4	6.7	3.2	6.6

24 **Share capital – equity shares**

**Authorised**

Ordinary shares of £1 each

**Allotted, issued and fully paid**

Ordinary shares of £1 each

	Group and Company	
	2004	2003
	£m	£m
Ordinary shares of £1 each	860.0	860.0
Ordinary shares of £1 each	860.0	860.0

	Group				Company			
	Share capital	Profit and loss reserve	2004 Total	2003 Total	Share capital	Profit and loss reserve	2004 Total	2003 Total
	£m	£m	£m	£m	£m	£m	£m	£m
25 <b>Movement in shareholder's funds</b>								
At beginning of year	860.0	724.3	1,584.3	964.5	860.0	724.8	1,584.8	967.8
Profit for the financial year	–	302.7	302.7	109.2	–	299.9	299.9	106.4
Dividends	–	(250.6)	(250.6)	510.6	–	(250.6)	(250.6)	510.6
At end of year	860.0	776.4	1,636.4	1,584.3	860.0	774.1	1,634.1	1,584.8

## notes to the financial statements continued

### 26 Pension commitments

- (a) Pension arrangements for the majority of the group's employees are of the funded defined benefit type through the AWG Pension Scheme (AWGPS). The group's actuaries are AON Limited.

The defined benefit arrangements are closed to new employees, who are eligible instead for entry to AWG's defined contribution scheme which started on 1 April 2002. Contributions to the defined contribution scheme amounted to £1.0 million (2003: £0.2 million).

The administration and investment of the AWGPS is maintained separately from the finances of the AWG Plc group.

The accounting pension costs have been prepared under SSAP 24 'Accounting for Pension Costs', based on the most recent full actuarial valuation. Details of the most recent actuarial valuation of the scheme are summarised below:

<b>Scheme</b>	
Date of most recent valuation	31 March 2002
Actuarial method	projected unit
Main assumptions:	
Excess of investment returns over:	
– general salary increases	1.9% pa
– annual increases in pensions	3.8% pa
Results:	
– market value of assets	£518.1 million
– funding level	109%
Due date of next full actuarial valuation	31 March 2005

The net pension cost for the year ended 31 March 2004 was £6.5 million (2003: £7.1 million). The net pension cost includes a credit of £2.4 million (2003: £2.4 million) in respect of the amortisation of actuarial surpluses. At 31 March 2004 there was a prepayment in respect of pensions of £53.5 million (2003: £38.9 million).

- (b) In November 2000 the Accounting Standards Board issued FRS 17 'Retirement Benefits'. The group is making use of the transitional arrangements regarding the adoption of FRS 17. Disclosures are included below as if FRS 17 had been applied from 1 April 2001.

The valuation used for FRS 17 disclosures has been based on the most recent full actuarial valuation for AWGPS (summarised above), updated by independent actuaries to take account of the requirements of FRS 17 in order to assess the liabilities of the scheme at 31 March 2004. The group is contributing 20.1 per cent of pensionable pay plus £9.1 million per annum to the AWGPS. The group also manages an unfunded pension arrangement (see note 21), which has been valued by independent actuaries to take account of the requirements of FRS 17 as at 31 March 2004.

In addition, the group operates a defined benefit scheme for the employees of the former Hartlepool Water Limited acquired on 1 April 2000. The assets and liabilities of this arrangement are not material to the group financial statements and have been excluded from the following disclosures.

The liabilities of the schemes have been valued using the projected unit method and using the following assumptions:

	2004 % pa	2003 % pa	2002 % pa
Discount rate	5.5	5.4	6.0
Inflation rate	2.9	2.6	2.8
Increase to deferred benefits during deferment	2.9	2.6	2.8
Increases to inflation related pensions in payment	2.9	2.7	2.9
Salary increases	4.4	4.6	4.8

The long-term expected rate of return and the assets in the scheme relating to the company at 31 March 2004 are:

	Expected rate of return % pa	AWGPS	Unfunded pensions	Total
		Fair value of scheme assets £m	Fair value of scheme assets £m	Fair value of scheme assets £m
Equities	7.8	333.0	N/A	333.0
Corporate bonds	5.2	23.1	N/A	23.1
Gilts	4.8	113.6	N/A	113.6
Property	6.8	13.4	N/A	13.4
Other	4.0	32.1	N/A	32.1
<b>Total assets</b>		<b>515.2</b>	<b>N/A</b>	<b>515.2</b>
Fair value of scheme liabilities		(658.8)	(39.7)	(698.5)
Deficit in the scheme		(143.6)	(39.7)	(183.3)
Related deferred tax asset		43.4	11.9	55.3
<b>Net pension liability</b>		<b>(100.2)</b>	<b>(27.8)</b>	<b>(128.0)</b>

The long-term expected rate of return and the assets in the scheme relating to the company at 31 March 2003 were:

	Expected rate of return % pa	AWGPS	Unfunded pensions	Total
		Fair value of scheme assets £m	Fair value of scheme assets £m	Fair value of scheme assets £m
Equities	7.6	279.7	N/A	279.7
Corporate bonds	4.9	22.8	N/A	22.8
Gilts	4.6	65.3	N/A	65.3
Property	6.6	13.0	N/A	13.0
Other	4.0	23.3	N/A	23.3
<b>Total assets</b>		<b>404.1</b>	<b>N/A</b>	<b>404.1</b>
Fair value of scheme liabilities		(599.9)	(37.6)	(637.5)
Deficit in the scheme		(195.8)	(37.6)	(233.4)
Related deferred tax asset		58.7	11.3	70.0
<b>Net pension liability</b>		<b>(137.1)</b>	<b>(26.3)</b>	<b>(163.4)</b>

The long-term expected rate of return and the assets in the scheme relating to the company at 31 March 2002 were:

	Expected rate of return % pa	AWGPS	Unfunded pensions	Total
		Fair value of scheme assets £m	Fair value of scheme assets £m	Fair value of scheme assets £m
Equities	8.0	389.1	N/A	389.1
Corporate bonds	6.0	28.0	N/A	28.0
Gilts	5.0	63.3	N/A	63.3
Property	8.0	15.7	N/A	15.7
Other	4.0	13.7	N/A	13.7
<b>Total assets</b>		<b>509.8</b>	<b>N/A</b>	<b>509.8</b>
Fair value of scheme liabilities		(519.8)	(36.7)	(556.5)
Deficit in the scheme		(10.0)	(36.7)	(46.7)
Related deferred tax asset		3.0	8.0	11.0
<b>Net pension liability</b>		<b>(7.0)</b>	<b>(28.7)</b>	<b>(35.7)</b>

## notes to the financial statements continued

### 26 Pension commitments (continued)

The deferred tax attributable to pension scheme deficits is not discounted because the related deficits are themselves determined on a discounted basis.

If the above net pension liabilities had been recognised in the financial statements, the group's net assets and the profit and loss reserve at 31 March 2004 would be as follows:

	2004 £m	2003 £m
<b>Net assets</b>		
Net assets	1,636.4	1,584.3
Exclude existing post tax net pension prepayment (under SSAP 24)	(27.0)	(9.4)
	1,609.4	1,574.9
FRS 17 pension liability net of deferred tax	(128.0)	(163.4)
Net assets including FRS 17 pension liability	1,481.4	1,411.5
<b>Profit and loss reserve</b>		
Profit and loss reserve	776.4	724.3
Exclude existing post tax net pension prepayment (under SSAP 24)	(27.0)	(9.4)
	749.4	714.9
FRS 17 pension liability net of deferred tax	(128.0)	(163.4)
Profit and loss reserve including FRS 17 pension liability	621.4	551.5

The group's pension expense for its defined benefit schemes, in accordance with FRS 17, would have been as set out below.

	AWGPS £m	Unfunded Pensions £m	Total £m
<b>2004 Profit and loss account</b>			
Current service cost	(16.3)	–	(16.3)
Past service cost	(2.0)	–	(2.0)
Charge to operating profit	(18.3)	–	(18.3)
Expected return on pension scheme assets	27.4	–	27.4
Interest on pension scheme liabilities	(32.5)	(2.0)	(34.5)
Amount charged to other finance income	(5.1)	(2.0)	(7.1)
Charge to profit on ordinary activities before taxation	(23.4)	(2.0)	(25.4)
<b>2003 Profit and loss account</b>			
Current service cost	(15.7)	–	(15.7)
Past service cost	–	–	–
Charge to operating profit	(15.7)	–	(15.7)
Expected return on pension scheme assets	39.0	–	39.0
Interest on pension scheme liabilities	(31.3)	(2.0)	(33.3)
Amount credited to other finance income	7.7	(2.0)	5.7
Charge to profit on ordinary activities before taxation	(8.0)	(2.0)	(10.0)

	AWGPS £m	Unfunded Pensions £m	Total £m
<b>2004 Statement of total recognised gains and losses</b>			
Actual return on pension scheme assets less expected return	75.5	–	75.5
Experience gains and losses arising on the scheme liabilities	–	–	–
Changes in assumptions underlying the present value of the scheme liabilities	(22.2)	(2.2)	(24.4)
<b>Gain / (loss) recognised</b>	<b>53.3</b>	<b>(2.2)</b>	<b>51.1</b>
<b>2003 Statement of total recognised gains and losses</b>			
Actual return on pension scheme assets less expected return	(160.4)	–	(160.4)
Experience gains and losses arising on the scheme liabilities	–	0.9	0.9
Changes in assumptions underlying the present value of the scheme liabilities	(41.2)	(1.8)	(43.0)
<b>Loss recognised</b>	<b>(201.6)</b>	<b>(0.9)</b>	<b>(202.5)</b>
<b>2004 Movement in scheme deficit (before related deferred tax asset)</b>			
Deficit at 1 April 2003	(195.8)	(37.6)	(233.4)
Current service costs	(16.3)	–	(16.3)
Contributions	22.3	2.1	24.4
Past service costs	(2.0)	–	(2.0)
Net interest	(5.1)	(2.0)	(7.1)
Actuarial gain / (loss)	53.3	(2.2)	51.1
<b>Deficit at 31 March 2004</b>	<b>(143.6)</b>	<b>(39.7)</b>	<b>(183.3)</b>
<b>2003 Movement in scheme deficit (before related deferred tax asset)</b>			
Deficit at 1 April 2002	(10.0)	(36.7)	(46.7)
Current service costs	(15.7)	–	(15.7)
Contributions	23.8	2.0	25.8
Net interest	7.7	(2.0)	5.7
Actuarial loss	(201.6)	(0.9)	(202.5)
<b>Deficit at 31 March 2003</b>	<b>(195.8)</b>	<b>(37.6)</b>	<b>(233.4)</b>
<b>2004 Details of experience gains and losses</b>			
Difference between expected and actual returns on scheme assets:			
Amount (£m)	75.5	–	75.5
Percentage of scheme assets	14.7%	–	14.7%
Experience gains and losses on scheme liabilities:			
Amount (£m)	–	–	–
Percentage of present value of scheme liabilities	–	–	–
Amount in group statement of total recognised gains and losses:			
Amount (£m)	53.3	(2.2)	51.1
Percentage of present value of scheme liabilities	8.1%	5.5%	7.3%

## notes to the financial statements continued

### 26 Pension commitments (continued)

2003 Details of experience gains and losses	Unfunded		Total
	AWGPS	Pensions	
Difference between expected and actual returns on scheme assets:			
Amount (£m)	(160.4)	–	(160.4)
Percentage of scheme assets	39.7%	–	39.7%
Experience gains and losses on scheme liabilities:			
Amount (£m)	–	0.9	0.9
Percentage of present value of scheme liabilities	–	2.4%	0.1%
Amount in group statement of total recognised gains and losses:			
Amount (£m)	(201.6)	(0.9)	(202.5)
Percentage of present value of scheme liabilities	33.6%	2.4%	31.8%

### 27 Contingent liabilities

At 31 March 2004 £144.0 million of Advance Corporation Tax (ACT) has been surrendered to the company by AWG Group Limited but remains unutilised. As part of the financial restructuring the company is required to pay AWG Group Limited on utilisation of the ACT. A provision has not been recognised in the group accounts as it is uncertain whether the ACT will be utilised (i.e. it is not probable that a transfer of economic benefits will be required to settle the obligation) and it is not possible to make a reliable estimate of the amount of the obligation.

The company, as part of the Anglian Water Services Financing group, guarantees unconditionally and irrevocably all the borrowings of Anglian Water Services Financing Plc, which at 31 March 2004 amounted to £3,791.5 million (2003: £3,311.2 million). The borrowings of Anglian Water Services Holdings Limited and Anglian Water Services Overseas Holdings Limited are also guaranteed unconditionally and irrevocably by the company. Excluding the £1,609.1 million loan made by the company to Anglian Water Services Holdings Limited, Anglian Water Services Holdings Limited and Anglian Water Services Overseas Holdings Limited had no outstanding indebtedness at 31 March 2004.

There are no other material contingent liabilities at 31 March 2004 for which provision has not been made in these financial statements.

### 28 Ultimate parent company

Anglian Water Services Overseas Holdings Limited, a company registered in the Cayman Islands, is the immediate parent company of the company.

AWG Group Limited, a company registered in England and Wales, is the parent company of the smallest group to consolidate the accounts of the group.

AWG Plc, a company registered in England and Wales, is the parent company of the largest group to consolidate the accounts of the group. The directors consider AWG Plc to be the ultimate parent company.

Copies of the accounts of Anglian Water Services Overseas Holdings Limited, Anglian Water Services Holdings Limited and Anglian Water Services Financing Plc can be obtained from the Company Secretary, Henderson House, Lancaster Way, Huntingdon, Cambridgeshire PE29 6XQ or the company website at [www.anglianwater.co.uk](http://www.anglianwater.co.uk).

Copies of the group accounts of AWG Group Limited and AWG Plc can be obtained from the Company Secretary, Anglian House, Ambury Road, Huntingdon, Cambridgeshire PE29 3NZ.

## regulatory accounts and required regulatory information

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The regulatory accounts and required regulatory information for Anglian Water Services Limited (the company or the appointee) are shown on pages 31 to 47.

## statement of directors' responsibilities for regulatory information

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

This additionally requires the directors to:

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

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

## notes on regulatory information

### 1 general

As discussed in the directors' report in the statutory financial statements, the company's activities are regulated by the conditions of a licence granted to the company by the Secretary of State for the Environment. With certain exceptions, the regulatory provisions do not apply to business activities which are not connected with the carrying out of the water and sewerage function, these business activities are referred to as non-appointed business (see note 2 on page 35).

An analysis of the regulatory historical cost profit and loss account and regulatory historical cost balance sheet between appointed and non-appointed business is set out on pages 33 and 34. A current cost profit and loss account and current cost balance sheet are shown on pages 37 and 38. Other current cost disclosures appear on pages 39 to 47. Additional information required by the licence is shown on pages 35 and 36.

Under the RAGs the treatment of certain turnover and expenditure items differs from that disclosed in the statutory financial statements.

### 2 protection of the regulated business

- (a) In the opinion of the directors the company will have available to it sufficient financial resources and facilities to enable it to carry out, for at least the next 12 months, the regulated activities (including the investment programme necessary to fulfil its obligations under the appointment).
- (b) In the opinion of the directors the company will, for at least the next 12 months, have available to it management resources and methods of planning and internal control which are sufficient to carry out the regulated activities (including the investment programme necessary to fulfil the company's obligations under the Instrument of Appointment).
- (c) In the opinion of the directors all contracts entered into with any associate company include all necessary provisions and requirements concerning the standard of service to be supplied to the company to ensure that it is able to meet all its obligations as a water and sewerage undertaker.

### 3 arms-length trading

In the opinion of the directors, the company was in compliance with paragraph 3.1 of Condition K of the licence throughout the year.



## current cost five year performance review

This relates to the five-year profit and loss accounts and balance sheets on page 47 prepared using current cost accounting principles and should be read in conjunction with the performance review set out in the statutory financial statements. The prior year figures are those reported in the regulatory accounts for that particular year and inflated to a common price base with figures reported in the current year. This is done by multiplying the numbers in prior years by the Retail Price Index (RPI) at 31 March 2004 divided by the RPI at 31 March in the relevant prior year.

In operating costs there was a year on year reduction of £18.0 million between 2003 and 2004. Operating costs in the prior year included £19.1 million of exceptional costs which did not recur in the current period.

Movements between 2003 and 2004 were as follows:

- a) The working capital adjustment which arises through the indexation of the 2003 balance sheet working capital adjustment (comprising short-term debtors, creditors and cash but excluding debt) by the RPI movement in the current year. This results in a credit to the balance sheet and an offsetting debit to the profit and loss of £3.2 million in the current year.
- b) The financing adjustment was £51.2 million in 2004 compared with £63.4 million in 2003 and is calculated as the indexation of the 2003 balance sheet net assets employed less net operating assets. The movement is due to a reduction in other trade creditors from 31 March 2002 to 31 March 2003. Net assets employed are lower than net operating assets as net assets include the impact of long-term debt and dividends payable. This results in a credit balance sheet movement and an offsetting debit profit and loss account movement in the current year.
- c) The increase in working capital in the balance sheet of £234.9 million between 2003 and 2004 is due primarily to an increase in cash balances of £267.8 million. This was due to new borrowings in the year and net cash inflow from operating activities less cash utilised on capital enhancements and dividend payments.

Over the five year period the major notable movements are as follows

- a) Turnover reduced from 2000 to 2001 by £62.2 million as a result of a negative K<sup>1</sup> of 10 being applied as part of the Asset Management Plan (AMP) 3 regulatory settlement. From 2001 to 2002 there was a positive K of 1 and an increase in revenue of £21.1 million. From 2002 to 2003 there was a reduction in turnover of £13.8 million. This was due to the allowable K increase of 2.2 being offset by negative consumption movements and refinements to the accrual consumption calculation. The movement between 2003 and 2004 is explained in the performance review set out in the statutory financial statements.
- b) Current cost operating costs consist of operating costs, exceptional operating costs and current cost depreciation. Over the five-year period operating costs have started at £286.9 million in 1999 and ended at £288.7 million in 2003 despite continued upward pressure. The regulatory price settlement for AMP 3 held operating costs flat in real terms and to date actuals have been broadly in line with the Determination. Current cost depreciation increased over the five-year period from £173.7 million in 1999 to £226.9 million in 2003. This is in line with the historic cost depreciation (as adjusted for price inflation).
- c) Net interest increased by £22.4 million in 2001 when compared with 2000 due to some atypical costs for early termination of some loans and higher indexation on RPI linked bonds. In 2002 this returned to a more normal base of £107.8 million. Following the financial restructuring completed on 30 July 2002 the composition of the net interest charge has changed and this makes comparability with prior years more difficult. The 2003 charge consists of £191.7 million in underlying interest costs, £51.0 million of exceptional costs associated with refinancing and £133.3 million of interest receivable relating to an inter-company loan with Anglian Water Services Holdings Limited. The underlying interest charge increased compared to 2002 because of the increased gearing of the company. The 2004 charge is discussed in the performance review set out in the statutory financial statements.
- d) Taxation charges in 1999, 2000 and 2001 were restated to include the impact of deferred tax as per Financial Reporting Standard (FRS) 19. In 2002 there was a credit due of £29.2 million due to accrual releases following the settlement of prior year tax assessments plus a negative deferred tax charge due to movements in discount rates. In 2003 there was a charge of £36.8 million on current tax, which was predominantly due to charging tax on the interest receivable of £133.3 million (discussed above). In 2004, following agreement that the company will not pay for the losses surrendered to it by Anglian Water Services Holdings Limited, most of this charge was reversed which gave rise to a credit in 2004.

<sup>1</sup> Ofwat defines K as the amount by which a company can increase, or must decrease, its average charge above or below inflation each year to finance its services and meet its legal obligations. When inflation is included, this is commonly referred to as the 'price limit'.

# regulatory historical cost profit and loss account

of the company for the year ended 31 March

	2004			2003		
	Appointed £m	Non appointed £m	Total £m	Appointed £m	Non appointed £m	Total £m
Turnover	758.6	8.0	766.6	719.3	7.4	726.7
Operating costs	(444.7)	(3.9)	(448.6)	(453.4)	(4.7)	(458.1)
Profit on sale of fixed assets	0.8	–	0.8	0.6	–	0.6
Operating profit*	314.7	4.1	318.8	266.5	2.7	269.2
Other income	–	–	–	0.1	–	0.1
Interest receivable	207.6	–	207.6	142.6	–	142.6
Interest payable	(259.8)	–	(259.8)	(249.0)	–	(249.0)
Profit on ordinary activities before taxation	262.5	4.1	266.6	160.2	2.7	162.9
Taxation:						
– current tax	23.2	(1.2)	22.0	(35.8)	(0.8)	(36.6)
– deferred tax	11.3	–	11.3	(19.9)	–	(19.9)
Profit on ordinary activities after taxation	297.0	2.9	299.9	104.5	1.9	106.4
Dividends	(247.7)	(2.9)	(250.6)	512.9	(2.3)	510.6
Movement in reserves	49.3	–	49.3	617.4	(0.4)	617.0

\* After exceptional items of £18.0 million in the prior year.

# regulatory historical cost balance sheet

of the company at 31 March

	2004			2003		
	Appointed £m	Non appointed £m	Total £m	Appointed £m	Non appointed £m	Total £m
<b>Fixed assets</b>						
Tangible assets	3,767.3	–	3,767.3	3,676.4	–	3,676.4
Investments	1,609.3	–	1,609.3	1,609.3	–	1,609.3
	<b>5,376.6</b>	<b>–</b>	<b>5,376.6</b>	<b>5,285.7</b>	<b>–</b>	<b>5,285.7</b>
<b>Current assets</b>						
Stocks	6.6	–	6.6	4.6	–	4.6
Debtors	324.4	–	324.4	299.5	–	299.5
Cash at bank and in hand	157.5	4.9	162.4	0.6	2.7	3.3
Short-term investments	269.0	–	269.0	158.0	–	158.0
	<b>757.5</b>	<b>4.9</b>	<b>762.4</b>	<b>462.7</b>	<b>2.7</b>	<b>465.4</b>
<b>Creditors: amounts falling due within one year</b>						
Short-term borrowings	(22.0)	–	(22.0)	(27.4)	–	(27.4)
Dividends payable	(55.2)	(2.9)	(58.1)	(150.7)	(1.9)	(152.6)
Other creditors	(283.2)	(2.0)	(285.2)	(295.2)	(0.8)	(296.0)
Net current assets / (liabilities)	<b>397.1</b>	<b>–</b>	<b>397.1</b>	<b>(10.6)</b>	<b>–</b>	<b>(10.6)</b>
<b>Total assets less current liabilities</b>	<b>5,773.7</b>	<b>–</b>	<b>5,773.7</b>	<b>5,275.1</b>	<b>–</b>	<b>5,275.1</b>
<b>Creditors: amounts falling due after more than one year</b>						
Loans and other borrowings	(3,900.6)	–	(3,900.6)	(3,438.9)	–	(3,438.9)
Other creditors	(90.0)	–	(90.0)	(87.4)	–	(87.4)
	<b>(3,990.6)</b>	<b>–</b>	<b>(3,990.6)</b>	<b>(3,526.3)</b>	<b>–</b>	<b>(3,526.3)</b>
<b>Provisions for liabilities and charges</b>						
Deferred tax	(97.0)	–	(97.0)	(108.3)	–	(108.3)
Other provisions	(52.0)	–	(52.0)	(55.7)	–	(55.7)
	<b>(149.0)</b>	<b>–</b>	<b>(149.0)</b>	<b>(164.0)</b>	<b>–</b>	<b>(164.0)</b>
	<b>1,634.1</b>	<b>–</b>	<b>1,634.1</b>	<b>1,584.8</b>	<b>–</b>	<b>1,584.8</b>
<b>Capital and reserves</b>						
Called up equity share capital	860.0	–	860.0	860.0	–	860.0
Profit and loss reserve	774.1	–	774.1	724.8	–	724.8
Total shareholder's funds (all equity)	<b>1,634.1</b>	<b>–</b>	<b>1,634.1</b>	<b>1,584.8</b>	<b>–</b>	<b>1,584.8</b>

## additional information required by the licence

### 1 Accounting policies

The accounting policies are set out in the statutory financial statements, except that, as noted on page 31, under the Regulatory Accounting Guidelines (RAG) certain turnover and expenditure items are treated differently in the regulatory financial statements. In addition, infrastructure renewals accounting has been retained in the regulatory accounts in accordance with the Office of Water Services (Ofwat) requirements.

### 2 Information in relation to allocations and apportionments between the appointed and any other business or activity of the appointee or associated company

The non-appointed business relates mainly to service searches, recreation, leisure and the provision of engineering and consultancy services. The North Tees water supply agreement to the Huntsman Petrochemical site, which is not in the Anglian Water area, has also been treated as non-appointed business.

A proportion of the operating costs relating to these activities is directly incurred and does not require allocation. Other relevant costs have been allocated according to time spent on these activities.

### 3 Allocation to principal service

(a) Operating costs are incurred directly by specific service and have not required allocation. Indirect costs are allocated on either a causal link basis or according to local managers' assessments. The allocation to principal service of the charge for infrastructure renewals is based on the Asset Management Plan.

(b) Capital costs, and hence the related depreciation charges, are incurred directly by specific service and have not required allocation.

### 4 Information in respect of transactions with any other business or activity of the appointee or any associated company

To the best of the directors' knowledge, all appropriate transactions with associated companies have been disclosed in notes (a) to (f) below.

### (a) Borrowings or sums lent

On 30 July 2002 £1,609.1 million was lent by the company to Anglian Water Services Holdings Limited. No other sums were lent by the appointee to associated companies at 31 March 2004.

Sums borrowed by the appointee from Anglian Water Services Financing Plc, its financing subsidiary, were:

Type of loan	Principal amount £m	Repayment date	Interest rate %
Fixed rate	100.0	2014	12.375
Fixed rate	200.0	2023	6.875
Fixed rate	200.0	2029	6.625
Fixed rate	150.0	2006	8.25
'Mark to market' adjustments on £150.0m loan (1)	8.1	2006	
Fixed rate	250.0	2022	5.837
Fixed rate	246.0	2030	6.293
Fixed rate (5)	275.0	2012/2037	7.882
Fixed rate	229.3	2009	5.375
Fixed rate	453.2	2013	4.625
Fixed rate	16.0	2009	7.07
'Mark to market' adjustments on £16.0m loan (1)	0.7	2009	
Fixed rate	1.6	2006	7.21
'Mark to market' adjustments on £1.6m loan (1)	0.1	2006	
Fixed rate	35.8	2006	6.85
Fixed rate	28.4	2005	6.57
Fixed rate	24.9	2006	6.65
Fixed rate	71.0	2008	7.01
Fixed rate	16.3	2009	7.13
Fixed rate	138.5	2011	7.23
Index linked (2)	153.6	2008	5.5
Index linked (2)	164.9	2020	4.125
Index linked (2)	209.6	2032	3.07
Index linked (2)	62.8	2032	3.07
Index linked (2)	78.6	2024	3.666
Floating rate (3)	254.8	2007	LIBOR plus 0.4%
Floating rate (3), (5)	50.0	2007/2012	LIBOR plus 1.2%
Floating rate (3), (5)	180.0	2009/2014	LIBOR plus 1.25%
Floating rate (3)	74.0	2037	EURIBOR plus 2.8%
Floating rate (3), (5)	100.0	2010/2037	LIBOR plus 2.8%
£150m index linked swap (3), (4)	6.7	2024	
£175m index linked swap (3), (4)	7.8	2030	
£258m index linked swap (3), (4)	3.8	2013	

(1) As part of the financial restructuring of the company in 2002/03 back to back loans to the company from AWG Group Limited were reassigned from AWG Group Limited to Anglian Water Services Financing Plc. The 'mark to market' adjustments relate to the reassignment of these loans at fair value rather than book value. The difference between the book value and fair value is being amortised at a constant rate on the carrying amount of the debt over the remainder of its life.

(2) The value of the capital and interest elements of the index linked debt are linked to movements in the Retail Price Index (RPI).

(3) The company has entered into swap agreements that convert 98.5 per cent of its floating rate debt into index linked debt in accordance with the company's hedging policy.

(4) The values of the notional capital on these index linked swaps are linked to movements in RPI. The increase in the notional capital value is payable at the final maturity date of the swaps.

(5) Legal maturity of these instruments is the second of the years quoted. Coupons 'step-up' is in the first of the years quoted.

EURIBOR is the 'European Inter Bank Offer Rate'. LIBOR is the 'London Inter Bank Offer Rate'.

## additional information required by the licence continued

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### 4 Information in respect of transactions with any other business or activity of the appointee or any associated company (continued)

#### (b) Dividends payable

A dividend of £247.7 million is paid and payable for the year (2003: 286.3 million). Of this dividend, £193.6 million (2003: £129.6 million) is ultimately paid and payable to Anglian Water Services Holdings Limited, a parent undertaking, in order for it to service the interest payable to the company on the inter-company loan of £1,609.1 million (see note 4 (a) on page 35). £193.1 million of the dividend paid per the cash flow statement (see page 39) is ultimately paid to Anglian Water Services Holdings Limited.

In 2003 AWG Group Limited waived its right to £786.0 million of the 2001 dividend.

#### (c) Guarantees/securities

The company, as part of the Anglian Water Services Financing group, guarantees unconditionally and irrevocably all the borrowings of Anglian Water Services Financing Plc, its wholly owned subsidiary, which at 31 March 2004 amounted to £3,791.5 million (2003: £3,311.2 million). The borrowings of Anglian Water Services Holdings Limited and Anglian Water Services Overseas Holdings Limited are also guaranteed unconditionally and irrevocably by the company. Excluding the £1,609.1 million loan made by the company to Anglian Water Services Holdings Limited, Anglian Water Services Holdings Limited and Anglian Water Services Overseas Holdings Limited had no outstanding indebtedness at 31 March 2004 (2003: nil).

#### (d) Charitable and political donations

During the year the group made a payment of £1.0 million (2003: £1.0 million) to the Anglian Water Trust Fund.

Financially through charitable donations, educational, regeneration and recreation projects, the group contributed £0.1 million (2003: £0.1 million) to other charitable causes.

No political donations were made.

#### (e) Omissions of rights

No material omissions took place during the year.

#### (f) Waivers

There were no material waivers during the year.

current cost profit and loss account for the appointed business  
of the company for the year ended 31 March

Notes	2004 £m	2003 £m
2 Turnover	758.6	719.3
4 Current cost operating costs	(515.6)	(519.0)
3 Operating income	0.3	0.3
1(e),3 Working capital adjustment	243.3 (3.2)	200.6 (8.9)
Current cost operating profit*	240.1	191.7
Other income	–	0.1
Interest receivable	207.6	142.6
Interest payable	(259.8)	(249.0)
1(e) Financing adjustment	51.2	63.4
Current cost profit before taxation	239.1	148.8
Current tax	23.2	(35.8)
Deferred tax	11.3	(19.9)
Current cost profit attributable to shareholder	273.6	93.1
Dividends	(247.7)	512.9
7 Current cost profit	25.9	606.0

\*After exceptional items of £18.3 million in the prior year.

The notes on pages 40 to 47 form part of these current cost financial statements.

current cost balance sheet for the appointed business  
of the company at 31 March

Notes	2004 £m	2003 £m
<b>Assets employed</b>		
5	19,181.0	18,665.9
	(609.3)	(581.6)
	<u>18,571.7</u>	<u>18,084.3</u>
6	411.2	121.9
	<u>18,982.9</u>	<u>18,206.2</u>
	1,609.3	1,609.3
	68.5	51.3
	(55.2)	(150.7)
	(22.0)	(27.4)
	(3,900.6)	(3,438.9)
	(97.0)	(108.3)
	(52.0)	(55.7)
	<u>16,533.9</u>	<u>16,085.8</u>
<b>Financed by</b>		
	860.0	860.0
7	182.3	156.4
8	15,491.6	15,069.4
	<u>16,533.9</u>	<u>16,085.8</u>

The notes on pages 40 to 47 form part of these current cost financial statements.

Approved by the board on 2 June 2004.

  
Roy Pointer  
Chief Executive

  
David Hipple  
Finance Director

current cost cash flow statement for the appointed business  
of the company for the year ended 31 March

Notes	2004 £m	2003 £m
9(a) Net cash inflow from operating activities	457.5	415.1
Returns on investments and servicing of finance		
Interest received	204.6	94.9
Interest paid	(212.2)	(141.8)
Cash flow treated as finance costs under Financial Reporting Standard (FRS) 4	(1.3)	(23.8)
Interest element of finance lease rental payments	(9.1)	(9.7)
Net cash outflow for returns on investments and servicing of finance	(18.0)	(80.4)
Taxation		
Corporation Tax received	0.3	0.5
Capital expenditure and financial investment		
Gross cost of purchase of fixed assets	(236.1)	(219.1)
Grants and contributions received	18.6	17.0
Infrastructure renewals expenditure	(40.5)	(42.6)
Short-term loan to group company, AWG Group Limited	-	309.5
Loan to group company, Anglian Water Services Holdings Limited	-	(1,609.1)
Disposal of tangible fixed assets	1.1	1.3
Net cash outflow for capital expenditure and financial investment	(256.9)	(1,543.0)
Equity dividends paid	(343.2)	(122.4)
Management of liquid resources		
Increase in short-term deposits and investments	(180.8)	(88.2)
Net cash outflow before financing	(341.1)	(1,418.4)
Financing		
Increase in loans	453.2	1,947.3
Repayments of amounts borrowed	(0.7)	(255.1)
Capital element of finance lease payments	(24.4)	(21.7)
Net cash inflow from financing	428.1	1,670.5
Increase in cash	87.0	252.1

Notes 9a and 9b on page 46 forms part of this current cost cash flow statement.



## notes to the current cost financial statements

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### 1 Accounting policies

#### (a) General

These financial statements have been prepared in accordance with guidance issued by the Director General of Water Services (DG) for modified real terms financial statements suitable for regulation in the water industry.

They measure profitability on the basis of real financial capital maintenance, in the context of assets which are valued at their current cost value to the business, with the exception of assets acquired prior to 31 March 1990.

The accounting policies used are the same as those adopted in the statutory historical cost financial statements, except as set out below:

#### (b) Tangible fixed assets

Assets acquired prior to 31 March 1990 and in operational use are valued at the replacement cost of their operating capability. To the extent that the regulatory regime does not allow such assets to earn a return high enough to justify that value, this represents a modification of the value to the business principle.

No provision is made for possible funding of future replacement of assets by contributions from third parties and, to the extent that some of those assets would on replacement be so funded, replacement cost again differs from value to the business.

Redundant assets are valued at their recoverable amounts.

##### *Land and buildings*

Non-specialised operational properties are valued on the basis of open market value for existing use as part of the periodic Asset Management Plan (AMP) reviews and are expressed in real terms by indexation using the RPI thereafter.

Specialised operational properties acquired since 31 March 1990 are valued at the lower of depreciated replacement cost and recoverable amount, restated annually between periodic AMP reviews by adjusting for inflation as measured by changes in the RPI. The unamortised portion of third party contributions received is deducted in arriving at net operating assets (as described below).

##### *Infrastructure assets*

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

A process of continuing refinement of asset records is expected to produce adjustments to existing values when periodic reviews of the AMP take place. In the intervening years, values are restated to take account of changes in the general level of inflation, as measured by changes in the RPI over the year.

##### *Other fixed assets*

All other fixed assets are valued periodically at depreciated replacement costs. Between periodic AMP reviews, values are restated for inflation as measured by changes in the RPI.

##### *Surplus land*

Surplus land is valued at recoverable amount, taking into account that part of any proceeds to be passed on to customers under Condition B of the licence.

#### (c) Modern equivalent asset (MEA) valuation

A review of the MEA valuation and asset stock is undertaken as part of the last Periodic Review. The revised values arising from this review, once deemed effective by Ofwat, provide the basis for calculating the MEA in the current cost financial statements.

#### (d) Grants and other third party contributions

Grants, infrastructure charges and other third party contributions received since 31 March 1990 are carried forward to the extent that any balance has not been credited to revenue. The balance carried forward is after restatement for the change in the RPI for the year. This balance is treated as deferred income.

1 *Accounting policies (continued)*

(e) **Real financial capital maintenance adjustments**

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

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

Disposal of fixed assets adjustment – the difference between the values of realised assets in these current cost financial statements and in the historical cost financial statements.

The depreciation adjustment is incorporated within operating costs in the profit and loss account. The disposal of fixed assets adjustment is incorporated within operating income in the profit and loss account.

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

Financing adjustment – this is calculated by applying the changes in the RPI over the year to the opening balance of net finance, which comprises all monetary assets and liabilities in the balance sheet apart from those included in working capital and dividends payable.

		2004			2003		
		Water service £m	Sewerage service £m	Appointed business £m	Water service (restated) £m	Sewerage service (restated) £m	Appointed business (restated) £m
2	<b>Turnover for the appointed business</b>						
	Measured	148.6	210.7	359.3	128.8	187.7	316.5
	Unmeasured	113.7	212.5	326.2	115.2	214.2	329.4
	Trade effluent	–	7.4	7.4	–	8.4	8.4
	Large user revenues	21.5	22.8	44.3	20.0	19.8	39.8
	Third party services	16.4	2.1	18.5	20.1	1.3	21.4
	Other sources	2.1	0.8	2.9	1.7	2.1	3.8
	<b>Total turnover</b>	<b>302.3</b>	<b>456.3</b>	<b>758.6</b>	<b>285.8</b>	<b>433.5</b>	<b>719.3</b>

The analysis of 2003 turnover has been restated because:

- (1) Hartlepool Water's measured large user and special agreement revenue was incorrectly listed as unmeasured
- (2) the sewerage and trade effluent large user revenue was not separately analysed
- (3) service charge revenue was incorrectly listed as measured

These adjustments only affect the split of revenue in 2003 and the total turnover of £719.3 million remains unchanged.

		2004			2003		
		Water service £m	Sewerage service £m	Appointed business £m	Water service £m	Sewerage service £m	Appointed business £m
3	<b>Operating income and working capital adjustment for the appointed business</b>						
	Current cost profit on disposal of fixed assets	0.2	0.1	0.3	0.1	0.2	0.3
	Working capital adjustment	(1.6)	(1.6)	(3.2)	(4.4)	(4.5)	(8.9)

## notes to the current cost financial statements continued

### 4 Analysis of operating costs and fixed asset net book values by service

2004

	Service analysis								Business activities		
	Water service			Sewerage service					Customer services	Scientific services	Cost of regulation
	Resources and treatment	Distribution	Water service subtotal	Sewerage treatment	Sewage treatment & disposal	Sludge treatment & disposal	Sewage T&D subtotal	Sewerage service subtotal			
£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	
<b>Direct costs:</b>											
Employment costs	6.0	7.8	13.8	9.6	14.7	7.2	21.9	31.5	10.3	5.1	1.8
Power	5.8	5.5	11.3	2.6	8.4	2.4	10.8	13.4	–	0.1	–
Hired and contracted services	3.2	10.9	14.1	5.0	9.2	12.0	21.2	26.2	7.4	1.2	1.4
Materials and consumables	3.9	1.0	4.9	1.7	5.2	6.9	12.1	13.8	0.3	0.5	–
Service charges	7.6	–	7.6	1.0	4.9	–	4.9	5.9	–	–	–
Bulk supply imports	1.1	–	1.1	–	–	–	–	–	–	–	–
Other direct costs	0.1	0.3	0.4	0.2	0.2	0.1	0.3	0.5	4.6	0.2	1.5
<b>Total direct costs</b>	<b>27.7</b>	<b>25.5</b>	<b>53.2</b>	<b>20.1</b>	<b>42.6</b>	<b>28.6</b>	<b>71.2</b>	<b>91.3</b>	<b>22.6</b>	<b>7.1</b>	<b>4.7</b>
General and support expenditure	9.5	7.0	16.5	7.3	12.0	9.8	21.8	29.1	4.3	1.5	0.8
Functional expenditure	37.2	32.5	69.7	27.4	54.6	38.4	93.0	120.4	26.9	8.6	5.5
<b>Total business activities</b>			<b>20.7</b>					<b>20.3</b>			
Rates			18.7					13.5			
Doubtful debts			5.5					7.2			
Exceptional items			–					–			
<b>Total less third party services</b>			<b>114.6</b>					<b>161.4</b>			
Third party services			12.0					0.7			
<b>Total operating costs</b>			<b>126.6</b>					<b>162.1</b>			
<b>Capital costs:</b>											
Infrastructure renewals expenditure	0.1	17.3	17.4	23.1	–	–	–	23.1			
Movement in infrastructure renewal accrual/prepayment	–	(5.8)	(5.8)	(7.7)	–	–	–	(7.7)			
Depreciation† (allocated)	45.4	17.0	62.4	22.1	95.5	8.3	103.8	125.9			
Amortisation of deferred credits			(2.0)					(3.9)			
Business activities depreciation‡ (non-allocated)			5.4					8.1			
Capital maintenance excluding third party services			77.4					145.5			
Third party services – capital maintenance			3.1					0.9			
<b>Total capital maintenance</b>			<b>80.5</b>					<b>146.4</b>			
<b>Total operating costs<sup>(1)</sup></b>			<b>207.1</b>					<b>308.5</b>			
2003 total operating costs			213.6					305.4			
<b>CCA (MEA) values</b>											
Service activities	1,121.0	4,483.3	5,604.3	11,796.5	1,578.5	88.7	1,667.2	13,463.7			
Business activities			14.1					21.2			
<b>Service totals</b>			<b>5,618.4</b>					<b>13,484.9</b>			
Service assets for third parties			65.3					12.4			
<b>Total MEA values</b>			<b>5,683.7</b>					<b>13,497.3</b>			
2003 total MEA values			5,542.9					13,123.0			

† On a current cost basis.

(1) Included within total operating costs are reactive and planned maintenance expenditure on infrastructure assets of £11.4 million. This is split £7.2 million water distribution and £4.2 million sewerage.

4 Analysis of operating costs and fixed asset net book values by service (continued)

2003	Service analysis								Business activities		
	Water service			Sewerage service					Customer services £m	Scientific services £m	Cost of regulation £m
	Resources and treatment £m	Distribution £m	Water service subtotal £m	Sewerage £m	Sewage treatment £m	Sludge treatment & disposal £m	Sewage T&D subtotal £m	Sewerage service subtotal £m			
<b>Direct costs:</b>											
Employment costs	5.9	7.3	13.2	9.3	13.9	5.2	19.1	28.4	10.6	5.0	1.3
Power	5.0	5.3	10.3	1.9	6.4	2.5	8.9	10.8	–	0.1	–
Hired and contracted services	3.9	10.3	14.2	6.2	9.8	16.7	26.5	32.7	8.0	1.5	0.4
Materials and consumables	4.0	1.2	5.2	1.6	4.9	6.5	11.4	13.0	0.3	0.3	–
Service charges	6.8	–	6.8	0.9	4.6	–	4.6	5.5	–	0.6	–
Bulk supply imports	0.9	–	0.9	–	–	–	–	–	–	–	–
Other direct costs	0.3	0.4	0.7	0.2	0.3	0.2	0.5	0.7	4.9	0.2	1.3
<b>Total direct costs</b>	<b>26.8</b>	<b>24.5</b>	<b>51.3</b>	<b>20.1</b>	<b>39.9</b>	<b>31.1</b>	<b>71.0</b>	<b>91.1</b>	<b>23.8</b>	<b>7.7</b>	<b>3.0</b>
<b>General and support expenditure</b>	<b>8.9</b>	<b>6.3</b>	<b>15.2</b>	<b>6.6</b>	<b>11.3</b>	<b>8.4</b>	<b>19.7</b>	<b>26.3</b>	<b>4.3</b>	<b>1.6</b>	<b>1.2</b>
<b>Functional expenditure</b>	<b>35.7</b>	<b>30.8</b>	<b>66.5</b>	<b>26.7</b>	<b>51.2</b>	<b>39.5</b>	<b>90.7</b>	<b>117.4</b>	<b>28.1</b>	<b>9.3</b>	<b>4.2</b>
<b>Total business activities</b>			<b>22.6</b>					<b>19.0</b>			
Rates			19.7					13.0			
Doubtful debts			3.7					4.3			
Exceptional items			9.3					9.3			
<b>Total less third party services</b>			<b>121.8</b>					<b>163.0</b>			
Third party services			11.0					0.7			
<b>Total operating costs</b>			<b>132.8</b>					<b>163.7</b>			
<b>Capital costs:</b>											
Infrastructure renewals expenditure	–	19.1	19.1	23.4	0.1	–	0.1	23.5			
Movement in infrastructure renewal accrual/prepayment	–	(7.0)	(7.0)	(8.6)	–	–	–	(8.6)			
Depreciation <sup>†</sup> (allocated)	46.0	17.3	63.3	21.5	93.6	8.0	101.6	123.1			
Amortisation of deferred credits			(2.3)					(4.3)			
Business activities depreciation <sup>†</sup> (non-allocated)			4.7					7.1			
Capital maintenance excluding third party services			77.8					140.8			
Third party services – capital maintenance			3.0					0.9			
<b>Total capital maintenance</b>			<b>80.8</b>					<b>141.7</b>			
<b>Total operating costs<sup>(1)</sup></b>			<b>213.6</b>					<b>305.4</b>			
<b>2002 total operating costs</b>			<b>213.9</b>					<b>286.2</b>			
<b>CCA (MEA) values</b>											
Service activities	1,095.9	4,363.7	5,459.6	11,441.2	1,557.5	86.5	1,644.0	13,085.2			
Business activities			16.6					24.9			
<b>Service totals</b>			<b>5,476.2</b>					<b>13,110.1</b>			
Service assets for third parties			66.7					12.9			
<b>Total MEA values</b>			<b>5,542.9</b>					<b>13,123.0</b>			
<b>2002 total MEA values</b>			<b>5,372.1</b>					<b>12,715.5</b>			

<sup>†</sup> On a current cost basis.

(1) Included within total operating costs are reactive and planned maintenance expenditure on infrastructure assets of £43.1 million. This is split £10.2 million water distribution and £32.9 million sewerage.

notes to the current cost financial statements continued

	Specialised operational assets £m	Non-specialised operational properties £m	Infrastructure assets £m	Other tangible assets £m	Total £m
5 Fixed assets					
(a) Fixed assets by type – water service					
Gross replacement cost					
At 1 April 2003	1,465.0	9.7	4,893.9	274.9	6,643.5
RPI adjustment	38.1	0.3	127.2	7.1	172.7
Disposals	(1.7)	–	–	(0.7)	(2.4)
Additions	42.8	0.1	15.5	9.9	68.3
At 31 March 2004	1,544.2	10.1	5,036.6	291.2	6,882.1
Depreciation					
At 1 April 2003	905.0	2.8	–	192.8	1,100.6
RPI adjustment	23.5	0.1	–	5.0	28.6
Disposals	(1.0)	–	–	(0.7)	(1.7)
Charge for the year	48.9	0.1	–	21.9	70.9
At 31 March 2004	976.4	3.0	–	219.0	1,198.4
Net book amount at 31 March 2004	567.8	7.1	5,036.6	72.2	5,683.7
Net book amount at 31 March 2003	560.0	6.9	4,893.9	82.1	5,542.9
(b) Fixed assets by type – sewerage service					
Gross replacement cost					
At 1 April 2003	3,598.8	10.0	11,496.5	283.8	15,389.1
RPI adjustment	93.6	0.1	299.0	7.4	400.1
Disposals	(1.3)	–	(0.1)	(0.7)	(2.1)
Additions	118.2	0.1	35.0	14.9	168.2
At 31 March 2004	3,809.3	10.2	11,830.4	305.4	15,955.3
Depreciation					
At 1 April 2003	2,015.2	2.4	–	248.5	2,266.1
RPI adjustment	52.3	0.1	–	6.5	58.9
Disposals	(1.3)	–	–	(0.6)	(1.9)
Charge for the year	92.3	0.2	–	42.4	134.9
At 31 March 2004	2,158.5	2.7	–	296.8	2,458.0
Net book amount at 31 March 2004	1,650.8	7.5	11,830.4	8.6	13,497.3
Net book amount at 31 March 2003	1,583.6	7.6	11,496.5	35.3	13,123.0
(c) Fixed assets by type – total					
Gross replacement cost					
At 1 April 2003	5,063.8	19.7	16,390.4	558.7	22,032.6
RPI adjustment	131.7	0.4	426.2	14.5	572.8
Disposals	(3.0)	–	(0.1)	(1.4)	(4.5)
Additions	161.0	0.2	50.5	24.8	236.5
At 31 March 2004	5,353.5	20.3	16,867.0	596.6	22,837.4
Depreciation					
At 1 April 2003	2,920.2	5.2	–	441.3	3,366.7
RPI adjustment	75.8	0.2	–	11.5	87.5
Disposals	(2.3)	–	–	(1.3)	(3.6)
Charge for the year	141.2	0.3	–	64.3	205.8
At 31 March 2004	3,134.9	5.7	–	515.8	3,656.4
Net book amount at 31 March 2004	2,218.6	14.6	16,867.0	80.8	19,181.0
Net book amount at 31 March 2003	2,143.6	14.5	16,390.4	117.4	18,665.9

5 Fixed assets (continued)

(6) In the preparation of its statutory financial statements, the company has followed common industry practice and adopted the infrastructure renewals accounting basis as required by FRS 15 'Tangible Fixed Assets'. However, for the purposes of the regulatory financial statements, Ofwat has requested that FRS 15 is not applied for infrastructure renewals accounting, thereby providing a basis consistent with prior years. A reconciliation to the tangible fixed assets shown in the statutory financial statements is set out below:

	infrastructure assets £m
<b>Cost</b>	
At 31 March 2004 per regulatory financial statements	16,867.0
Adjustment to opening balance at 31 March	(14,762.3)
Infrastructure renewals expenditure related to the prior year	0.2
Infrastructure renewals expenditure capitalised in the year	40.5
At 31 March 2004 per statutory financial statements	<u>2,145.4</u>
<b>Grants and contributions</b>	
At 31 March 2004 per regulatory financial statements	-
Adjustment to opening balance at 31 March	(172.5)
At 31 March 2004 per statutory financial statements	<u>(172.5)</u>
<b>Depreciation</b>	
At 31 March 2004 per regulatory financial statements	-
Adjustment to opening balance at 31 March	(360.3)
Depreciation charge for infrastructure renewal expenditure	(27.0)
At 31 March 2004 per statutory financial statements	<u>(387.3)</u>
<b>Net book value</b>	
At 31 March 2004 per regulatory financial statements	16,867.0
Adjustment to opening balance at 31 March	(15,295.1)
Infrastructure renewals expenditure related to the prior year	0.2
Infrastructure renewals expenditure capitalised in the year	40.5
Depreciation charge for infrastructure renewal expenditure	(27.0)
At 31 March 2004 per statutory financial statements	<u>1,585.6</u>
<b>Working capital</b>	
At 31 March 2004 per regulatory financial statements	34.1
Less infrastructure renewals prepayment	(34.1)
At 31 March 2004 per statutory financial statements	<u>-</u>

	2004 £m	2003 £m
6 Working capital		
Cash	426.4	158.6
Stocks	6.6	4.6
Trade debtors	77.1	84.1
Trade creditors	(62.1)	(60.8)
Short-term capital creditors	(25.3)	(25.3)
Infrastructure renewals prepayment	34.1	20.4
Other trade accruals	(162.8)	(154.2)
Corporation Tax	(22.3)	(45.2)
Payroll related taxes and social security contributions	(3.0)	(3.1)
Group trade debtors (net)	85.4	63.1
Prepayments	57.1	79.7
Total working capital	<u>411.2</u>	<u>121.9</u>

	2004 £m	2003 £m
7 Current cost profit and loss reserve		
At beginning of year	156.4	(449.6)
Retained profit for the year for the appointed business	25.9	606.0
At end of year	<u>182.3</u>	<u>156.4</u>

## notes to the current cost financial statements continued

	2004 £m	2003 £m
8 Current cost reserve		
At beginning of year	15,069.4	14,580.4
RPI adjustments:		
Fixed assets	485.3	560.7
Working capital	3.2	8.9
Financing	(51.2)	(63.4)
Deferred grants and contributions	(15.1)	(17.2)
At end of year	15,491.6	15,069.4

The company has revalued its current cost asset base as part of the 2004 periodic review process. In accordance with RD10/04 published by Ofwat the revised amounts have not been reflected in the regulatory accounts this year, but will be reflected in the 2004/05 regulatory accounts on finalisation of the periodic review process.

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

	2004 £m	2003 £m
Current cost operating profit*	240.1	191.7
Working capital adjustment	3.2	8.9
Increase in stocks	(2.0)	(0.5)
Other income received	0.1	0.2
Current cost depreciation	205.8	202.1
Current cost profit on sale of fixed assets	(0.3)	(0.3)
Decrease in debtors and prepaid expenses	6.6	31.9
Decrease in creditors and accrued expenses	(0.4)	(22.8)
Provision for infrastructure renewals	27.0	27.0
Net movement in restructuring provision	(2.1)	(1.9)
Amortisation of deferred grants and contributions	(5.9)	(6.6)
Net movement in prepaid pension contributions	(14.6)	(14.6)
Net cash inflow from operating activities	457.5	415.1

\*After exceptional items of £18.3 million in the prior year.

	1 April 2003 £m	Cash flows £m	Non-cash movements £m	31 March 2004 £m
9(b) Analysis of net debt				
Cash	70.4	87.0	-	157.4
Deposits and investments	88.2	180.8	-	269.0
Finance leases due within one year	(25.2)	25.2	(17.3)	(17.3)
Finance leases due after one year	(153.3)	(0.8)	17.3	(136.8)
Other debt due within one year	(2.2)	2.2	(4.7)	(4.7)
Other debt due after one year	(3,285.6)	(453.4)	(24.8)	(3,763.8)
	(3,307.7)	(159.0)	(29.5)	(3,496.2)

Non-cash movements comprise indexation of index linked loan stock, indexation of RPI swaps, transfers between categories of debt, amortisation of debt issue costs and amortisation of 'mark to market' adjustments.

### 10 Regulatory capital value (RCV)

	2004 £m	2003 £m
Opening RCV for the year	4,032.6	3,945.4
Indexation of opening RCV	105.3	-
Capital expenditure	270.9	274.0
Infrastructure renewals expenditure	34.9	33.9
Grants and contributions	(16.4)	(15.5)
Depreciation	(138.5)	(131.0)
Infrastructure renewals charge	(23.6)	(22.7)
Outperformance of regulatory assumptions (5 years in arrears)	(13.3)	(51.5)
Closing RCV carried forward	4,251.9	4,032.6
Average RCV	4,146.6	3,935.8

10 Regulatory capital value (RCV) (continued)

RCV figures are extracted from those published by Ofwat on 10 March 2004 in their RD05/04 letter at 2002/03 prices. These have been indexed upwards to 2003/04 prices using an RPI factor of 184.6 / 179.9 (RPI at 31 March 2004 / RPI at 31 March 2003) to give all figures in the table excluding average RCV. The average RCV is derived by indexing the average RCV published on 10 March 2004 by the RPI factor of 182.5 / 177.5 (average RPI for year ended 31 March 2004 / average RPI for the year ended 31 March 2003).

The company intends to log up and down additional items at the forthcoming periodic review. This will be subject to agreement by Ofwat.

11 Current cost profit and loss account for the appointed business	2004	2003	2002	2001 restated	2000 restated
	£m	£m	£m	£m	£m
<b>Turnover</b>	758.6	739.6	753.4	732.3	794.5
Current cost operating costs	(515.6)	(533.6)	(524.9)	(511.6)	(523.9)
Operating income	0.3	0.3	1.9	(0.6)	(2.3)
Working capital adjustment	(3.2)	(9.2)	1.4	2.1	1.1
<b>Current cost operating profit*</b>	240.1	197.1	231.8	222.2	269.4
Other income	–	0.1	1.2	0.6	0.2
Interest (net)	(52.2)	(109.4)	(107.8)	(128.0)	(105.7)
Financing adjustment	51.2	65.2	23.0	36.3	34.8
<b>Current cost profit before taxation</b>	239.1	153.0	148.2	131.1	198.7
Taxation – current tax	23.2	(36.8)	30.0	(37.9)	(44.2)
Taxation – deferred tax	11.3	(20.5)	–	–	–
<b>Current cost profit attributable to shareholder</b>	273.6	95.7	178.2	93.2	154.5
Dividends	(247.7)	527.3	–	(969.6)	(163.3)
<b>Current cost profit / (loss)</b>	25.9	623.0	178.2	(876.4)	(8.8)

\* After historical exceptional charges in 2003 (£18.8 million), 2002 (£26.3 million), 2001 (£13.6 million) and 2000 (£48.8 million).

Current cost balance sheet for the appointed business	2004	2003	2002	2001 restated	2000 restated
	£m	£m	£m	£m	£m
<b>Assets employed</b>					
Fixed assets	19,181.0	19,153.6	19,134.5	19,106.5	18,904.6
Third party contributions since 31 March 1990	(609.3)	(596.8)	(586.1)	(573.6)	(563.9)
Working capital	360.0	125.1	304.5	(108.1)	(94.5)
<b>Net operating assets</b>	18,931.7	18,681.8	18,852.9	18,424.8	18,246.2
Cash and investments	1,609.3	1,651.3	0.2	0.2	0.3
Non-trade debtors	119.7	52.6	43.4	33.1	30.9
Dividends payable	(55.2)	(154.6)	(831.5)	(935.8)	(113.3)
Other non-trade creditors due within one year	(22.0)	(28.1)	(271.9)	(103.9)	(351.9)
Creditors due after one year	(3,900.6)	(3,528.7)	(1,813.9)	(1,600.9)	(1,264.8)
Provisions for liabilities and charges	(149.0)	(168.3)	(120.7)	(145.3)	(129.8)
<b>Net assets employed</b>	16,533.9	16,506.1	15,858.5	15,672.2	16,417.6
<b>Financed by</b>					
Called up share capital	860.0	882.5	909.8	921.9	942.7
Profit and loss reserve	182.3	160.5	(475.6)	(664.0)	222.6
Current cost reserve	15,491.6	15,463.1	15,424.3	15,414.3	15,252.3
<b>Total capital and reserves</b>	16,533.9	16,506.1	15,858.5	15,672.2	16,417.6

The financial information set out above for the four years ended 31 March 2003 is based on the audited current cost financial statements for those years, as adjusted to 2003/04 prices for changes in the RPI. The comparatives for 2000 and 2001 have been restated in respect of the adoption of FRS 19 'Deferred Tax' in 2002.

On 1 April 2000 the company acquired the trade and certain assets and liabilities from Hartlepool Water Limited. The trading results and balance sheet figures for the years ending 31 March 2004, 31 March 2003 and 31 March 2002 reflect this acquisition and are therefore not strictly comparable to previous years.

On 1 April 2002 the company acquired part of the business and certain assets and liabilities of Geodesys Limited. The trading results and balance sheet figures for the years ending 31 March 2004 and 31 March 2003 reflect this acquisition and are therefore not strictly comparable to previous years.



# independent auditors' report

## to the Director General of Water Services and the Directors of Anglian Water Services Limited

We have audited the Regulatory Accounts of Anglian Water Services Limited (referred to as the company) on pages 33 to 47 which comprise:

- the regulatory historical cost accounting statements comprising the regulatory historical cost profit and loss account and the regulatory historical cost balance sheet; and
- the regulatory current cost accounting statements for the appointed business comprising the current cost profit and loss account, the current cost balance sheet, the current cost cash flow statement and the related notes to the current cost financial statements including the statement of accounting policies.

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

### basis of preparation

The Regulatory Accounts have been prepared in accordance with Condition F of the Appointment and the Regulatory Accounting Guidelines, the accounting policies set out in the statement of accounting policies and, in the case of the regulatory historical cost accounting statements, under the historical cost convention.

The Regulatory Accounts are separate from the statutory financial statements of the company and have not been prepared under the basis of Generally Accepted Accounting Principles in the United Kingdom (UK GAAP). Financial information other than that prepared on the basis of UK GAAP does not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in financial statements prepared in accordance with the Companies Act 1985.

### respective responsibilities of the Regulator, the Directors and Auditors

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

The Directors' responsibilities for preparing the Regulatory Accounts in accordance with Regulatory Accounting Guidelines are set out in the statement of directors' responsibilities for regulatory information on page 31.

Our responsibility is to audit the Regulatory Accounts in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board, except as stated in the "Basis of audit opinion", below and having regard to the guidance contained in Audit 05/03 'Reporting to Regulators of Regulated Entities'.

We report to you our opinion as to whether the regulatory historical cost accounting statements present fairly, under the historical cost convention, the revenues and costs, assets and liabilities of the appointee and its appointed business in accordance with the company's Instrument of Appointment and Regulatory Accounting Guideline 2.03 (Guideline for classification of expenditure), Regulatory Accounting Guideline 3.05 (Guideline for the contents of regulatory accounts) and Regulatory Accounting Guideline 4.02 (Guideline for the analysis of operating costs and assets); and whether the regulatory current cost accounting statements on pages 37 to 47 have been properly prepared in accordance with Regulatory Accounting Guideline 1.03 (Guideline for accounting for current costs and regulatory capital values), Regulatory Accounting Guideline 3.05 and Regulatory Accounting Guideline 4.02. We also report to you if, in our opinion, the company has not kept proper accounting records as required by paragraph 3 of Condition F and whether the information is in agreement with the appointee's accounting records and has been properly prepared in accordance with the requirements of Condition F and, as appropriate, Regulatory Accounting Guideline 1.03, Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.05 and Regulatory Accounting Guideline 4.02.

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

#### basis of audit opinion

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

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

Our opinion on the Regulatory Accounts is separate from our opinion on the statutory financial statements of the company on which we reported on 2 June 2004, which are prepared for a different purpose. Our audit report in relation to the statutory accounts of the company (our "Statutory" audit) was made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our Statutory audit work was undertaken so that we might state to the company's members those matters we are required to state to them in a Statutory auditors' report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume any responsibility to anyone other than the company and the company's members as a body, for our Statutory audit work, for our Statutory audit report, or for the opinions we have formed in respect of that Statutory audit.

The regulatory historical cost accounting statements on pages 33 and 34 have been drawn up in accordance with Regulatory Accounting Guideline 3.05 in that infrastructure renewals accounting as applied in previous years should continue to be applied and accordingly that the relevant sections of Financial Reporting Standards 12 and 15 be disapplied. The effect of this departure from Generally Accepted Accounting Principles, and a reconciliation of the balance sheet drawn up on this basis with that drawn up under Companies Act 1985 is given on page 45.

#### opinion

In our opinion the Regulatory Accounts of the company contain the information for the year ended 31 March 2004 to comply with Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the company as a water and sewerage undertaker under the Water Industry Act 1991.

In respect of this information we report that in our opinion:

- (a) proper accounting records have been kept by the appointee as required by paragraph 3 of Condition F of the instrument;
- (b) the information is in agreement with the appointee's accounting records and has been properly prepared in accordance with the requirements of Condition F and, as appropriate, Regulatory Accounting Guideline 1.03, Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.05 and Regulatory Accounting Guideline 4.02 issued by the Regulator;
- (c) the regulatory historical cost accounting statements on pages 33 to 34 present fairly, under the historical cost convention, the revenues and costs, assets and liabilities of the appointee and its appointed business in accordance with the company's Instrument of Appointment and Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.05 and Regulatory Accounting Guideline 4.02 issued by the Regulator;

- (d) the regulatory current cost accounting statements on pages 37 to 47 have been properly prepared in accordance with Regulatory Accounting Guideline 1.03, Regulatory Accounting Guideline 3.05 and Regulatory Accounting Guideline 4.02 issued by the Regulator.

*PricewaterhouseCoopers LLP*

PricewaterhouseCoopers LLP  
Chartered Accountants and Registered Auditors  
Birmingham  
2 June 2004

*1. The maintenance and integrity of the company web site is the responsibility of the Directors and the maintenance and integrity of the Regulator's web site is the responsibility of the Regulator; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the Regulatory Accounts since they were initially presented on the web sites.*

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