

Glas Cymru Cyfyngedig
Company No 3975719

Report & Accounts 2007

THURSDAY



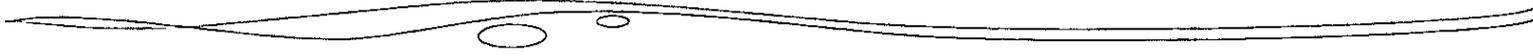
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Newport

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Chairman's statement



It has been another year of satisfactory progress for the Company, not only on the majority of key measures that matter most for our customers and the environment but also in terms of our financial performance. The latter has allowed a further improvement in our credit rating and an increase in our annual 'customer dividend' to £20 per customer.

Last summer saw only 60% of long term average rainfall, but reaching our leakage targets and having reduced our water abstractions by some 25% over the last decade meant we were able to avoid any restrictions on supply. The high level of compliance on key water quality measures was maintained and for the first time we achieved 100% compliance with the bacteriological standards for samples taken at our water treatment works.

During the year we also passed an important milestone with 3,000km of unlined iron water mains refurbished under our 10 year programme, improving water quality and reducing the risk of discoloured water – a major cause of complaints.

Following last year's serious cryptosporidium outbreak in North Wales, the Outbreak Control Team issued its final report which concluded that our water treatment works at Cwellyn was the likely source of the outbreak. The Drinking Water Inspectorate is still to publish its assessment of this incident.

On the wastewater treatment side of our business, we achieved close to our best ever performance – only just falling short of our 100% compliance target at wastewater treatment works – and a record number of Blue Flag awards for Welsh beaches. A further step change in coastal water quality is being delivered by the £35 million Holyhead treatment works that was officially opened during the year, contributing to the first ever Blue Flag for Holyhead Marina.

However, there remains much to be done to improve the performance of our sewer network where last year there was an increase in flooding incidents, mostly caused by sewer blockages, and no reduction in serious pollution incidents caused by sewer problems. Improving the performance of our sewer network is a priority for us.

Our overall financial position strengthened and gearing at the year end was down to 74% of regulatory capital value. This has prompted a further improvement in our credit rating that will help us to raise funds for our future capital investment programme at attractive rates of interest.

Further improvements in customer service were achieved following the opening of our new Operational Activity Centre – which now deals with around 25,000 customer service calls every month – and more will derive from our current £75 million 'IT enabled change' programme to replace legacy systems and processes.

Looking ahead, our single purpose corporate structure means that we are able to plan for the long term. We are working closely with other stakeholders to develop plans that will reflect the priorities of our region for the next 25 years.

Our aim is always to provide a first class service to our customers. We have some challenging times ahead in maintaining the highest standards, in tackling those areas where we currently fall short, in completing the AMP4 capital investment programme on time and within budget, and in developing our long term plans. I remain confident that we have the right team in place, and I would like to thank all the staff who work for Welsh Water and its contract partners for the effort and commitment they continue to make in looking after the water industry in Wales.

And finally, I am very pleased to welcome James Strachan to the Board as a Non Executive Director. He brings with him a rich and distinctive blend of experience from the private, public and voluntary sectors.

Lord Burns, Chairman

Our key performance at a glance

The Board has identified eight key performance indicators (KPI's) to monitor the success of the business, seven of which reflect our key financing and customer service strategies, i.e. reducing long term financing costs and improving customer service. The eighth addresses occupational health and safety and the fundamental right of all those who work on our behalf, or are affected by our undertaking, to return home safely at the end of each day.

Financial KPI's cover (i) Bond credit rating, (ii) Gearing, (iii) Interest cover, and (iv) 'Customer dividend' **1 2 3 4**

Customer service KPI's cover Ofwat's assessment of Overall Performance Assessment (OPA), customer satisfaction and overall bacteriological water quality. For occupational health and safety we monitor the Accident Incidence Rate (AIR) **5 6 7 8**

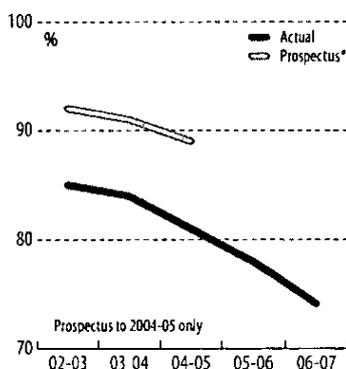
Further information regarding the definition, purpose and target for each of these KPI's can be found on page 30 of this report.

In addition to these KPI's we also report key performance measures for Welsh Water that we have published each year since Glas Cymru acquired Welsh Water in 2001. Further information regarding the definition of these indicators can also be found on page 30 **9**

1 Credit ratings of Glas Cymru bonds

	Standard & Poor's	Moody's	Fitch Ratings
Class A Bonds	AAA	Aaa	AAA
Class B Bonds	A-	A3	A
Class C Bonds	BBB	Baa2	BBB+

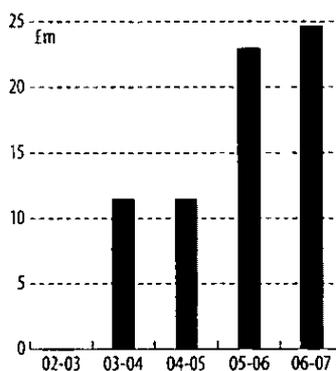
2 Gearing (net debt/RCV)



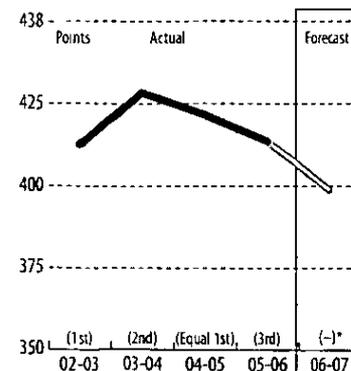
3 Interest cover

	2007	2006
Year to 31 March	£m	£m
EBITDA (pre-'customer dividend')	374	363
Interest payable (excluding indexation and amortisation of issue costs)		
Senior debt	115	114
Senior debt + class C bonds	125	127
Total debt	127	130
Interest cover (EBITDA/Net interest)		
Senior debt	3.3x	3.1x
Senior debt + class C bonds	3.0x	2.9x
Total debt	2.9x	2.8x

4 'Customer dividend'

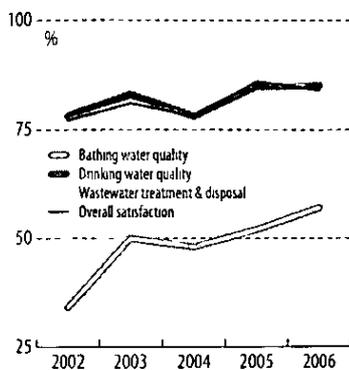


5 Overall Performance Assessment

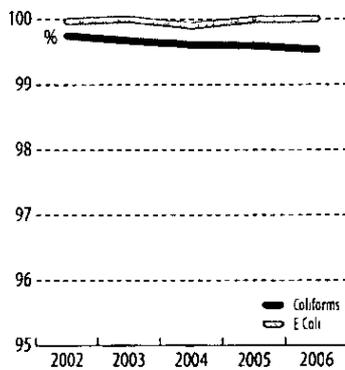


* OPA score and ranking in 2006-07 will be disclosed in Ofwat's Levels of Service Report published in Autumn 2007

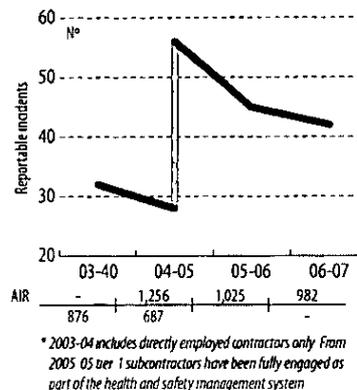
6 Customer satisfaction



7 Bacteriological compliance 'at the tap'



8 Health and safety



9 Key performance measures

Year to 31 March 2007	Monitoring Plan target ¹	Previous performance 2005-06	Actual performance 2006-07	At or ahead of target	At or better than previous year
Customer service					
Properties 'at risk' of receiving low pressure	242	221	221	✓	✓
Unplanned water supply interruptions	1,080	454	313	✓	✓
Properties 'at risk' of sewer flooding	432	514	484	✗	✓
Properties flooded due to hydraulic overload	122	81	96	✓	✗
Properties flooded due to other causes	120	150	203	✗	✗
Billing enquiries answered within 5 days	100%	100%	100%	✓	✓
Written complaints answered within 10 days	99.9%	99.4%	99.7%	✗	✓
Number of written complaints received	n/a	9,948	10,348	n/a	✗
Customer meters read within year	99.9%	99.9%	99.9%	✓	✓
Telephone calls abandoned	1.3%	1.6%	1.7%	✗	✗
Telephone calls receiving engaged tone	0%	0.3%	0.4%	✗	✗
Call handling satisfaction ¹	n/a	4.6	4.6	n/a	✓
Water quality					
Overall water quality compliance 'at the tap' ^{2 c}	n/a	99.9%	99.9%	n/a	✓
Bacteriological compliance 'at the tap' ^c	n/a	99.6%	99.5%	n/a	✗
Iron compliance 'at the tap' ^c	98.9%	99.2%	99.1%	✓	✗
Operational Performance Index ^c	n/a	99.8%	99.8%	n/a	✓
Operational Performance Index (TIM) ^{1 c}	n/a	99.7%	99.7%	n/a	✓
Environment					
Leakage (m ³ /km/day)	7.7	8.2	7.7	✓	✓
Number of 'category 1 and 2' pollution incidents ^{3 c}	n/a	17	17	n/a	✓
Number of 'category 3' pollution incidents ^c	n/a	194	208	n/a	✗
Wastewater treatment works complying with (LUT) consents ^{6 c}	99.7%	99.6%	99.7%	✓	✓
Sewage sludge recycled satisfactorily ^c	100%	100%	100%	✓	✓
'Mandatory' coastal bathing water compliance at EU designated bathing beaches ^c	100%	100%	99%	✗	✗
'Guideline' coastal bathing water compliance at EU designated bathing beaches ^c	'Stable'	91%	89%	n/a	✗

¹ New measure introduced in 2005-06. Score out of maximum 5

² This measure is now based on Mean Zonal Compliance

³ New measure introduced in 2005-06 which takes into account performance against turbidity, iron and manganese

⁴ The Monitoring Plan sets out the targets agreed with regulators at the Regulatory Price Review in 2004 and covers the five year period to 31 March 2010

⁵ 2 of these pollution incidents resulted from compliant discharges (2005-06: 8)

⁶ Look up table

^c Calendar year 2006. All other figures are for the year ended 31 March 2007

Our sole purpose is to provide high quality water and sewerage services at least cost to Welsh Water's customers.

Operating and financial review

A single purpose

Glas Cymru is the single purpose company formed in 2000 to own, finance and manage Dŵr Cymru Welsh Water ('Welsh Water'). It is a 'company limited by guarantee' and because it has no shareholders, any financial surpluses are retained for the benefit of Welsh Water's customers.

Under Glas Cymru's ownership, Welsh Water's assets and capital investment are financed by bonds, loans, leases and retained financial surpluses. All day-to-day activities are carried out by specialist contract partners employed by Welsh Water following a competitive procurement process. The Glas Cymru 'not-for-profit' business model aims to reduce Welsh Water's asset financing costs, the water industry's single biggest cost, and improve service delivery by employing the best companies for each distinct activity in the business. 

Financing efficiency savings to date have largely been used to build up reserves to insulate Welsh Water and its customers from any unexpected costs and also to improve credit quality so that Welsh Water's cost of finance can be kept as low as possible in the years ahead. These

savings have also funded additional discretionary investment in service improvements and the annual 'customer dividend', which since its introduction five years ago has returned nearly £100 million to customers.

Company structure and market

Welsh Water is wholly owned by Glas Cymru and is the sixth largest of the ten regulated water and sewerage companies in England and Wales, representing around 8% of the sector when measured by assets employed. It provides an essential public service to more than 3 million people living in Wales and some adjoining parts of England. Its primary responsibility is to operate, maintain and upgrade its assets so as to ensure a safe and reliable supply of drinking water and to deal effectively with wastewater so as to protect public health and the natural environment. Welsh Water was established in 1989, when the water industry in England and Wales was privatised, and is Glas Cymru's principal trading subsidiary.

In delivering these services Welsh Water operates one of the larger networks of infrastructure assets in the UK water industry: 71 impounding reservoirs and 91 water treatment works deliver a

daily average of around 850 million litres of drinking water supplied through a network of 27,000 km of water mains, 532 pumping stations and 557 service reservoirs. Welsh Water also collects wastewater and surface water through a network of 19,000 km of sewers, incorporating 1,700 sewage-pumping stations and 3,300 combined sewer overflows. Treatment is carried out at 850 wastewater treatment works. Welsh Water also owns 35,000 hectares of land, much of which has a high value in terms of nature conservation and recreational use.

Household customers cannot currently choose which company provides their water or wastewater services, but non-household customers who use at least 50 million litres of water a year can take supply from any licensed water supplier. Welsh Water does not have a high concentration of non-household customers, with its 25 largest customers (by volume) accounting for less than 5% of revenue.

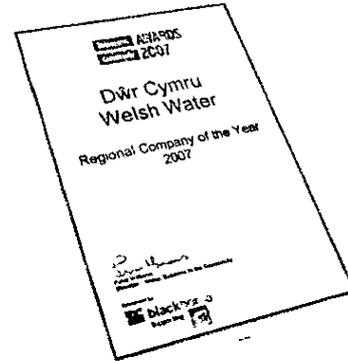
Welsh Water directly employs only 165 staff, but in total around 3,000 people are employed by contract partners in delivering water and sewerage services to its customers.

To ensure that the interests of Glas Cymru and Welsh Water are fully aligned, the Directors of Glas Cymru are also Directors of Welsh Water

The Board is accountable to the Members of the company who are appointed on the recommendation of an Independent Membership Panel. The Members carry out similar corporate governance functions to shareholders in a company limited by shares, by electing the Board and external auditors, and approving the Annual Report and Accounts and the Remuneration Report

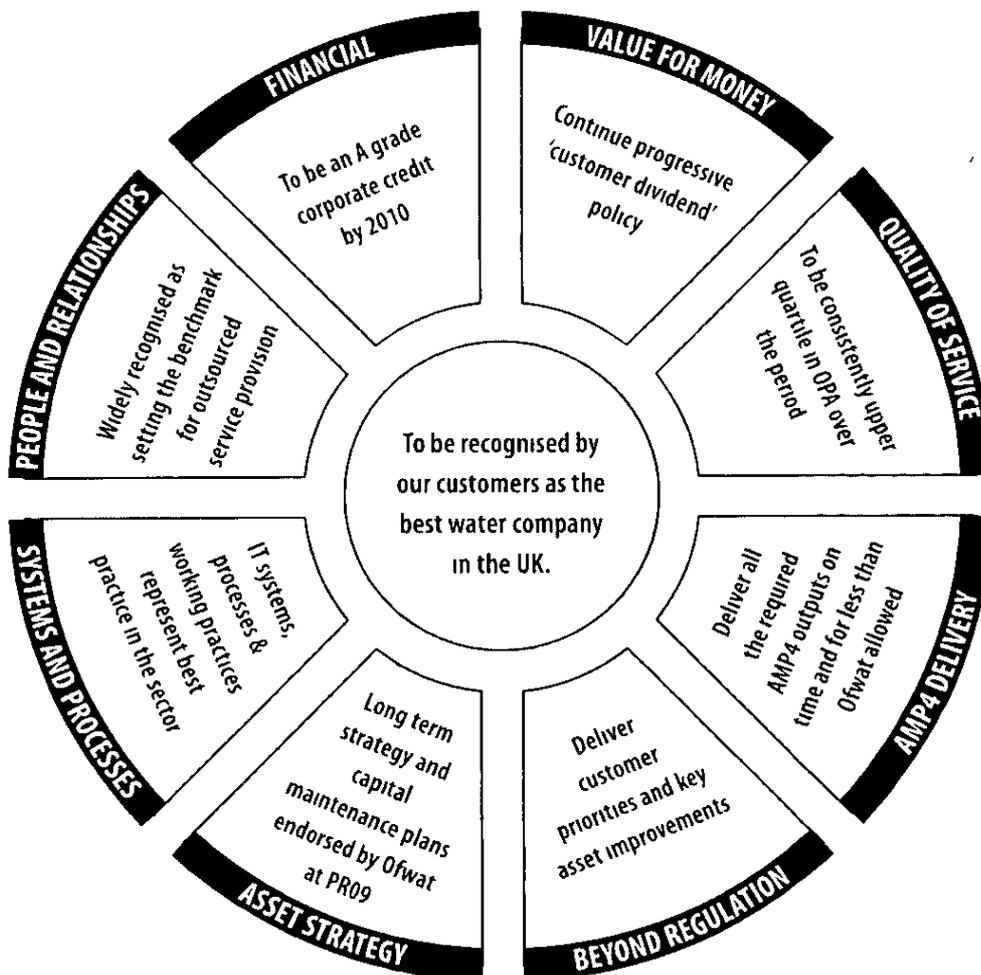
Financing

The group's bonds (further details of which can be found on page 27) are listed on the Luxembourg Stock Exchange in the name of Glas Cymru's wholly owned financing subsidiary, Dŵr Cymru (Financing) Limited. The group's strategy on financing and credit rating is addressed in the Financial Review on page 25. Reporting of performance against the group's financial obligations to bondholders and other financial creditors is disclosed in a quarterly Investor Report available on our website www.dwrcymru.com



Recognised as a valued and trusted partner in the communities we serve

10 Strategic objectives



Procurement

Under Glas Cymru's ownership, the primary objective of Welsh Water is to provide high quality water and sewerage services at least cost to its customers. To this end Welsh Water meets many of its obligations as a regulated water and sewerage service provider through a portfolio of contracts with specialist contractors and service providers.

Welsh Water has appointed one contract partner to be responsible for clean water delivery 'from source to tap'. The operation of the waste water service is divided geographically, with one contractor responsible for north Wales, and one for south Wales and Herefordshire. Other functions such as capital investment and maintenance and support services, such as billing and income, IT, laboratories and sampling and network development services, are provided through 12 other partners. This outsourcing together covers around 85% of Welsh Water's annual operational and capital costs.

Welsh Water retains ultimate control of all activities carried out under contract and has the ability to exercise that control. Contracts are therefore designed to ensure Welsh Water is not locked-in to any one contract partner or set of working arrangements and that they operate on a transparent basis so that Welsh Water retains access to all staff, information and knowledge required to meet its legal and regulatory obligations. Welsh Water also determines asset strategy and retains final responsibility for decisions regarding key assets.

Contracts are specified and structured to enable contract partners to deliver the best possible combination of quality of service and cost efficiency and partners are incentivised to deliver sector-leading

outcomes. They are also structured to achieve an efficient allocation of risk, with complementary provisions for incentive and reward between Welsh Water and its contract partners. This is built on the essential principles of openness and transparency which allows disclosure of trade offs between cost, risk and service performance, with the aim of securing the best interests of Welsh Water's customers.

Further information on our approach to competitive tendering can be found in Welsh Water's published Procurement Plan, available on our website www.dwcymru.com.

Regulatory environment

Welsh Water operates within a regulatory framework prescribed by the Water Industry Act 1991. The economic regulator is The Water Services Regulation Authority (Ofwat), which is responsible for setting the limits on prices that Welsh Water can charge, and overseeing Welsh Water's overall performance. Ofwat also has a duty to protect the interests of customers, including by promoting competition.

The industry operates on a five-year asset management cycle, and 2006-07 was the second year of the current Asset Management Period (AMP4), which began in April 2005 and ends in March 2010. Welsh Water's settlement for AMP4 is based on a capital expenditure programme costing in total some £1.3 billion, similar to that of the previous five year period, and an assumption that the average Welsh Water customer's bill would increase by no more than 3.6% above retail price inflation each year during the review period, compared to a sector average of 4.3%. In 2005-06 and 2006-07 Welsh Water paid a 'customer dividend' of £19 and £20 respectively per customer (i.e. £9.50 and £10 respectively per service).

The regulator with responsibility for drinking water quality is the Drinking Water Inspectorate (DWI), which is part of the Department of the Environment, Food and Rural Affairs and also acts on behalf of the Welsh Assembly Government in respect of Welsh Water. Under DWI quality monitoring procedures more than 300,000 water supply tests are carried out each year. The results are reported to the DWI, who undertake a series of audits to verify the data provided. The Environment Agency oversees Welsh Water's environmental performance, specifically with regard to the way in which it abstracts water from rivers and reservoirs, and then disposes of wastewater after it has been treated.

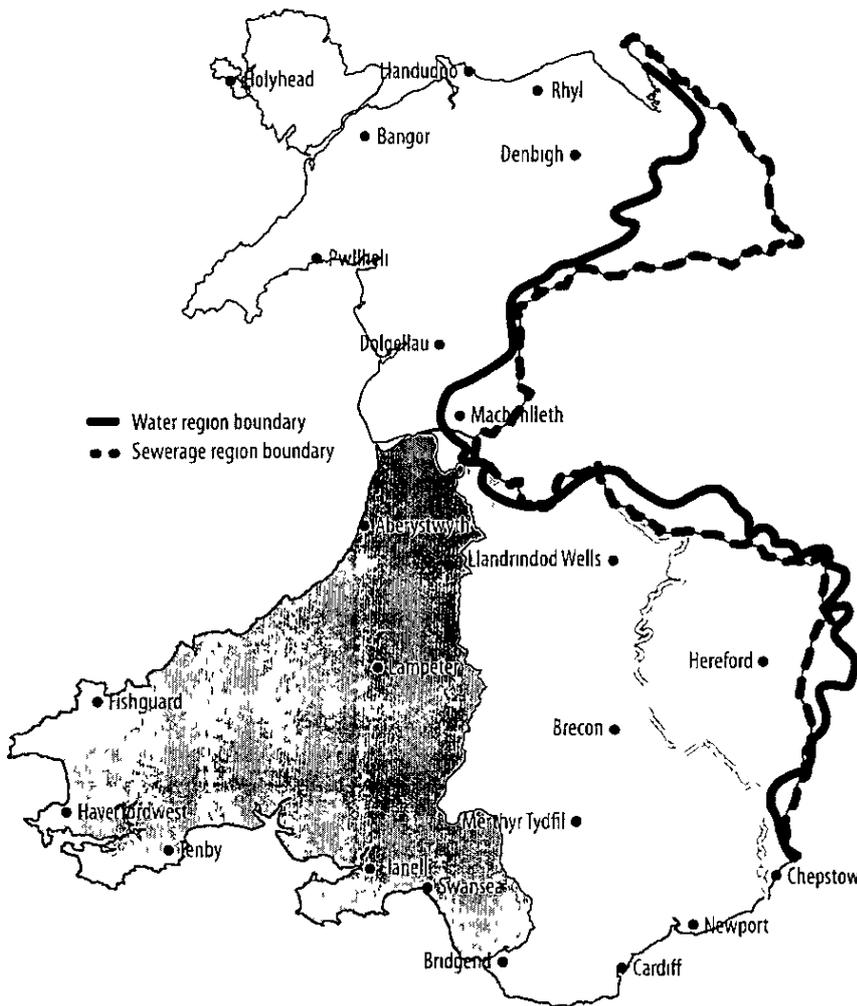
All aspects of Welsh Water's water and wastewater operations are subject to extensive performance monitoring against targets set by regulators and Government. Each year these regulators publish reports commenting on and comparing the performance of water companies across a full range of measures, including cost efficiency, customer service, water quality and environmental quality, and each has powers that can be used in the event that Welsh Water's performance is not up to standard.

The Consumer Council for Water (CC Water) is the independent body established in 2005 to represent the general interests of customers of water companies. CC Water investigates individual concerns and complaints and seeks to influence company policy on issues that customers regard important.

The Welsh Assembly Government also has a role in determining water quality and environmental quality standards, as well as setting the framework for other public policy matters such as social considerations arising from water tariff structures.

'As Glas Cymru is a single purpose business with one principal trading subsidiary (Welsh Water), the remainder of this Operating and Financial Review is structured in the same way as previous annual reports with sections on Water Supply, Wastewater, our approach to Corporate Responsibility (Community, Customers, the Environment, and our People), our Financial Performance and Risk Management'

11 Welsh Water's supply area and outsourced contract partners



Water network & process works

United Utilities
Black and Veatch
Laing O'Rourke

Wastewater (north)

CSO's, Sewerage & process works

United Utilities
Costain
Imtech Process

Wastewater (south west)

CSO's, Sewerage & process works

Kelda Water Services
Imtech Process
Morrison Construction

Wastewater (south east)

CSO's, Sewerage & process works

Kelda Water Services
Amec
Imtech Process

Other partners

Chandlers KBS
Capgemini
EC Harris
Hyder Consulting
Logica CMG
Tata Consulting
Thames Water
Severn Trent Laboratories

Water supply

Our biggest responsibility is to provide a safe and reliable drinking water supply, 24 hours a day - 365 days a year, while ensuring our water abstractions and water supply activities do not damage the environment

In 2006 Welsh Water sustained a high level of performance with compliance on a number of key measures either being maintained at, or improved to, best-ever levels. This improved performance overall reflects continued investment in the distribution system as part of Welsh Water's capital investment programme and continuous improvement in operational practices

Water resources and leakage

Despite summer rainfall being only 60% of the long-term average for Welsh Water's region, which created significant challenges in distribution in some of the more remote parts of the region, we were able to maintain water supplies to customers without imposing restrictions. In such circumstances minimising leakage is a priority and we promote awareness on water efficiency. Key to persuading our customers to use water wisely and avoid waste, is keeping leakage under control and dealing with reported leaks quickly

In 2006-07 we achieved the leakage target agreed with Ofwat by reducing leakage to 209 mega litres a day (Ml/d) 7% below the target we met for 2005-06 of 225Ml/d 

Our leakage performance is in line with the rest of the industry as measured by losses per km of water main. Ofwat is currently reviewing the economic level of leakage (ELL) for each company, i.e. the point at which it would cost more to produce leakage further than to produce water from another source, which may lead to further reduction in regulatory leakage targets. Our current challenge is, by 2010, to reduce leakage to Ofwat's assessed ELL for Welsh Water of 195Ml/d

Around 95% of the water Welsh Water abstracts is taken from rivers and reservoirs, with the remaining 5% of water drawn from the ground through springs, wells and boreholes. As a result of cutting leakage and lower demand from large industrial users, Welsh Water now abstracts for public water supply 25% less water than 10 years ago

Notwithstanding a relatively strong overall water resource position, there are a number of local areas where the balance between supply and demand continues to be tight and where there could be supply or distribution problems during drought conditions. Plans in place to improve the security of supply, especially in Ceredigion, parts of North Wales and parts of rural Herefordshire and Mid Wales, are described in Welsh Water's published Water Resource Plan 

In April 2007 Welsh Water launched its Water Efficiency strategy having previously launched a campaign, Be WaterWise to encourage customers to use water wisely

Looking forward, water resource plans may need to be further modified as a result of the Environment Agency's ongoing review of licensed water abstractions in the context of meeting obligations imposed by the Water Framework Directive and the development of river basin management plans to achieve a healthy aquatic ecosystem

Drinking water quality

Customers rely on Welsh Water to deliver a high quality and consistent supply of wholesome drinking water. How effective we are in this is measured against standards set down and monitored by the DWI. Last year, Welsh Water's quality monitoring procedures involved more than 300,000 individual tests of water quality, the results of which were reported to the DWI

During 2006 Welsh Water sustained a high level of performance for drinking water compliance. In respect of samples taken at water treatment works there was 100% compliance with bacteriological standards for coliforms and E-coli (2005 99.93%) 

A key measure of overall water quality at customer taps is 'mean zonal compliance', which monitors overall compliance against 40 separate parameters, and in

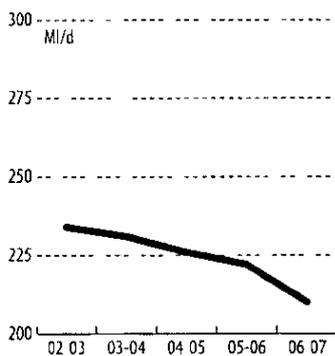
2006 Welsh Water maintained its performance at 99.95% (2005 99.95%) Performance against the 'distribution maintenance index', which takes into account performance against turbidity, iron and manganese - the principal parameters for discolouration problems, was also maintained at 99.7% (2005 99.7%) **13 17**

One initiative we jointly launched in 2006 is the 'Water Health Partnership for Wales', brings together relevant agencies to work more effectively

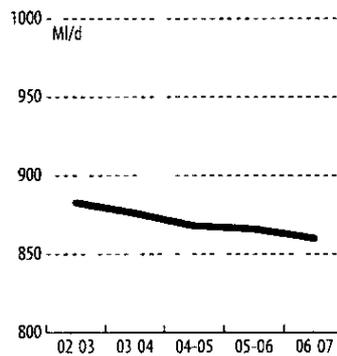
to protect public health This partnership includes the DWI, Welsh Assembly Government, local authority public and environmental health and emergency planning agencies, the Consumer Council for Water Wales and the National Public Health Agency Wales Initial meetings have proved successful in providing opportunities for sharing best practice and benchmarking each organisation's performance Looking forward, the DWI has consulted on proposed changes to the Water Supply (Water Quality)

Regulations These set out the regulatory framework for ensuring the quality of water supplies in England and Wales by specifying requirements for the abstraction, treatment and testing of potable water Proposed changes represent a further move away from reliance on 'end of pipe' testing to monitor water quality, to a risk based approach where the safety of drinking water is protected through a process of comprehensive risk assessment and management at all stages in the water supply chain

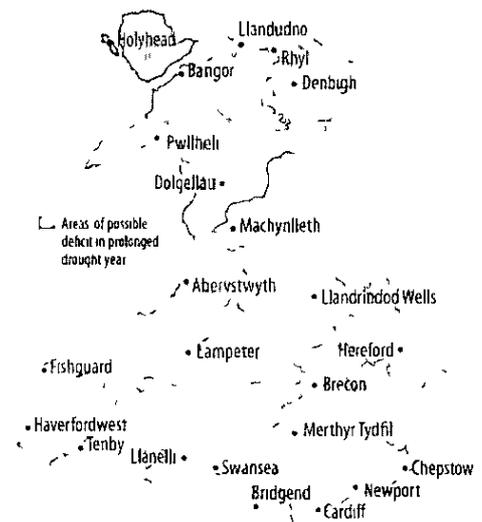
12 Leakage



13 Distribution input



14 Supply and demand

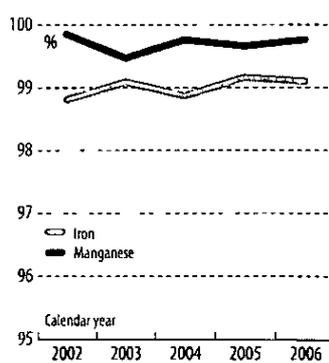


15 Bacteriological compliance

	Compliance 2006	Compliance 2005
Water treatment works		
Coliforms	100%	99.9%
E-Coli	100%	100%
Service reservoirs		
Coliforms	99.9%	99.9%
E-Coli	100%	100%
Compliance in water quality zones		
Coliforms	99.5%	99.6%
E Coli	100%	99.9%

Calendar year

16 Iron and manganese compliance



'Last year we reported that in November 2005 there was a higher than usual number of cases of illness caused by cryptosporidium in North West Wales which was linked to the tap water supplied by Cwellyn water treatment works To date, the DWI has yet to publish its report into this incident'

Reliability of supply

A key measure of customer service is the number of instances where water supplies are cut off without warning because of a burst, third party damage or because we have over-run on planned works. In the last five years we have reduced the number of unplanned supply interruptions, lasting more than six hours, by over 70%. In 2006-07, 313 properties were affected by these unplanned supply interruptions (2005-06 454 properties), a best ever performance for Welsh Water. 

We also monitor pressure in each water distribution zone, which allows us to identify possible problems and upgrade local water supply networks as necessary. Incidence of low pressure can change as new properties are connected to the water supply network and where we rationalise our assets. Last year we removed possible low pressure problems for 1,459 properties and at the end of the year there were 221 properties, or 0.02% of all connected properties, still at risk of having low pressure (2005-06 221), maintaining high performance on this key measure. 

Welsh Water's prioritised programme of work aimed at reducing the frequency of interruption to its worst served customers has helped maintain a reducing trend in burst rates on water mains both in real terms (2006 167 bursts per 1,000km main, 2005 171 bursts) and relative to other companies in the sector.

Capital investment

During the year we invested £132 million to improve or maintain our water assets. We refurbished over 390km of unlined water mains to improve water quality and iron compliance at customers' taps. A further 82km of water mains were replaced that were causing frequent supply interruptions to customers and 20km of mains were relined under maintenance programmes. Major improvement work was also carried out at 55 water treatment works, 52 service reservoirs and 28 water pumping stations. 

During the year we passed an important milestone with 3,000km of unlined iron water mains refurbished under our 10 year programme, improving water quality and reducing the risk of discoloured water – a major cause of complaints. This investment of £264 million between 2000 and 2007 has also delivered a reduced likelihood of leaks and bursts, and associated interruptions to supply.

Quality management systems

Quality Management Systems (QMS) are essential to the effective management and operation of our daily activities. They provide reassurance that risk is minimised, ensure that customer service is prioritised, that regulatory requirements are achieved and that everyone in the relevant organisations operate to the same exacting standards.

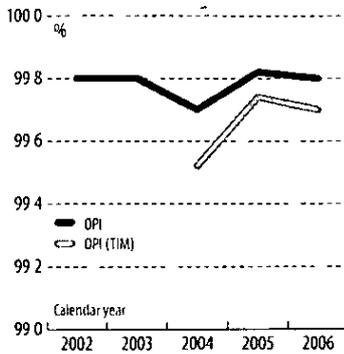
QMS systems play a major role across our business:

- United Utilities Operating Services – Potable Water
- United Utilities Operating Services – Waste Water (North Wales)
- Kelda Water Wales – Waste Water (South Wales)
- Thames Water – Customer Services
- Severn Trent Laboratories – Sampling and Laboratory Services

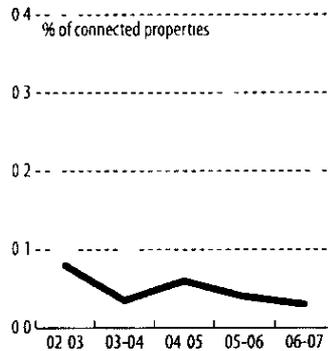
All the above systems have been certified to the ISO 9001 2000 standard and are subject to routine audit and review. In addition, UUOS also operate an Environmental Management System (EMS) and currently hold certification to the ISO 14001 2004 standard for two of DCWW's wastewater treatment works. UUOS have a programme in place to extend this registration on a 'site-by-site' basis.

The monitoring of quality performance at Board level is led by the Quality and Environment Committee, chaired by Dame Deirdre Hine. This Committee meets monthly and reports directly to each Board meeting.

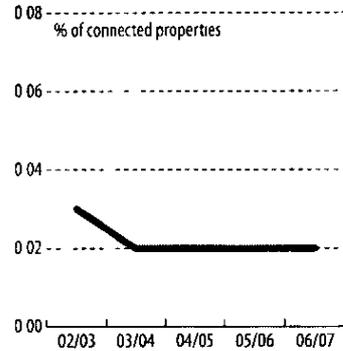
17 Operational performance index



18 Unplanned interruptions to supply



19 Risk of low pressure



20 Water investment in the year

Type of work	Spend
Water treatment works improvements	£12.0m
Water mains refurbishment	£49.4m
Meter installations	£5.0m
Leakage prevention	£6.2m
New developments	£7.0m
Asset maintenance	£42.3m
Other	£10.0m
Total	£131.9m

Further information about Welsh Water's water supply performance in 2006 can be found in the published report of the Quality and Environment Committee which, with the company's Water Resource Plan, is available on our website www.dwrcymru.com

Wastewater

It is our responsibility to collect and treat customers' wastewater – together in many places with highway and surface water that drains into the public sewer – in a way that safeguards public health and protects the environment. In 2006-07 we maintained our good standard of wastewater treatment works and bathing water compliance. However, the performance of our sewerage network is not yet satisfactory as the number of pollution incidents has remained at a similar level to 2005 and we have seen an increase in incidents of sewer flooding, particularly as a result of incidents caused other than by hydraulic overload.

Wastewater treatment

Notwithstanding that Welsh Water operates 850 wastewater treatment works, proportionately more than most companies in the sector, only three small works failed to meet the required standard of performance. This means that 99.97% of our customers (2005-06 99.91%) are served by works that met the required consent standard, making last year the best for wastewater treatment works compliance under Glas Cymru ownership and only marginally short of our target of 100% compliance, which Welsh Water last achieved in 1997. 

Coastal and river water quality

Welsh Water has one of the longest coastlines of any water and sewerage company in the sector – and since privatisation we have invested over £1 billion on upgrading or building new wastewater treatment works and

improving the sewer network. This has led to a significant and substantial improvement in both coastal water and river water quality. Our role in delivering high quality coastal water is especially important for the Welsh tourism industry, which employs around 100,000 people and makes a significant contribution to the Welsh economy.

In 2006, 79 of the 80 EU designated bathing beaches around the coast of Wales achieved the mandatory bathing water standard required by legislation (2005/80). In addition a record 75 beaches (2005/73) achieved the much higher 'guideline' standard. These results have secured 44 'Blue Flag' beach awards and five marina awards for the 2007 season (2006/47 awards in total), which once again means that Wales has secured around one third of the UK's total Blue Flag awards. 

Similarly the quality of rivers in Wales continues to be amongst the best in the UK. The last survey of river water quality published by the Environment Agency confirmed that over 98% of rivers in Wales were good or fair on the assessment of chemical quality and over 99% were good or fair on the assessment for biological quality. Notwithstanding this background, the required treatment standards continue to rise to meet obligations set by the Habitats and Water Framework Directives. Looking ahead, and working with its regulators, Welsh Water's challenge is to meet these rising standards in an environmentally

sustainable way, where the cost of meeting new treatment standards do not outweigh the environmental benefits.

Reliability of sewer network

Maintaining high standards of environmental performance in the sewerage network is one of Welsh Water's major challenges – the average age of our 19,000km of sewer network is 60 years, with around a third being more than 100 years old. The network was also designed to carry away surface water as well as wastewater from households and businesses, which means that at times, and especially after heavy rainfall, the sewer network cannot cope and overloaded sewers can cause flooding at customers' properties.

We measure the risk of this happening and also report actual sewer flooding incidents caused by hydraulically overloaded sewers or other causes, such as blockages and sewer collapses.  Despite significant investment and critical management focus on this key issue, our performance on sewer flooding deteriorated in 2006-07, when 335 properties experienced internal flooding by sewage (2005-06 268). Of these, 132 properties were flooded as a result of hydraulic overload of sewers following heavy rainfall and 203 properties were flooded by other causes, including blockages and sewer collapses. At the year-end 484 properties remained on the 'at risk register', a slight improvement on last year (2005-06 514). 

Reducing the risk of sewer flooding remains a top priority for Welsh Water, and we will continue to focus investment at properties where flooding has occurred most frequently. However, each year new incidents occur where flooding has not been experienced before. Re-examination of historical incident data in the light of changing weather patterns in the last few years has also

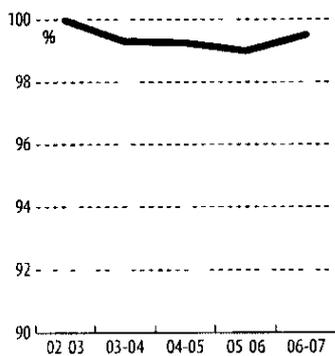
identified some 300 locations at risk of a pollution incident, which we are now addressing in our investment programme.

Where we have 'hot-spot' flooding areas, we may provide a flood forum as a means of communicating Welsh Water's plan to the community affected, and to determine joint solutions to prevent repeat flooding.

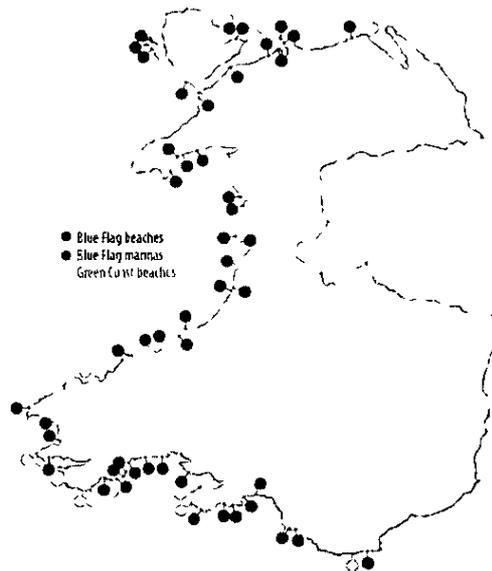
problems with other authorities who have responsibilities for drainage.

Looking forward, we recognise the benefit of government proposals to transfer responsibility for private sewers and drains to statutory undertakers, however this brings with it a number of significant challenges as the number and current condition of these private

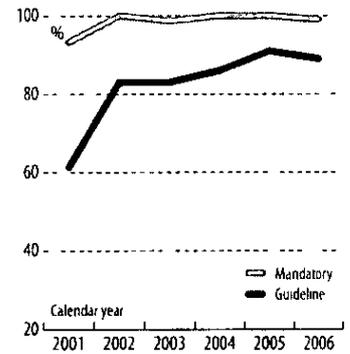
21 Wastewater treatment works (LUT) compliance



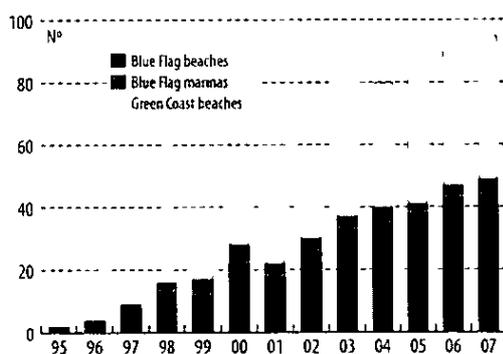
22 Location of award winning beaches



23 Bathing water quality compliance



24 Award winning beaches



Beaches are judged against 29 criteria, which include, in addition to water quality, good litter management, provision of information, strict dog controls and sustainable environmental management.

"When the awards were introduced to Wales in the early nineties only two beaches met the strict criteria, but this year we are celebrating the news that 44 of our beaches and 5 marinas have made the list. Much has been achieved by local authorities and Welsh Water in driving up the quality of our bathing water and land based infrastructure. We now call upon the beach visitor to play their part by ensuring they respect our national treasures."

Tegryn Jones, Chief Executive, Keep Wales Tidy

sewers are as yet largely unknown. It will significantly increase the number of assets Welsh Water owns and we will need time to assess and deliver any investment necessary to bring these assets up and maintain them to regulatory standards. It is important therefore that private sewers are transferred in a way that does not increase customer bills disproportionately.

Intermittent discharges

Our investment to improve storm water overflows will reduce the amount of sewage and associated debris discharged to watercourses when, as a result of combined surface water and domestic wastewater, sewer capacity is exceeded during heavy rainfall. We have nearly 3,300 storm water overflows on Welsh Water's sewer network and by 2010 we will have improved around 460 unsatisfactory overflows under a prioritised programme agreed with the Environment Agency Wales. In 2006-07 we improved 87 storm overflows, bringing the AMP4 total to 155 during the first two years.

Notwithstanding this investment, the number of 'category 1' and 'category 2' pollution incidents in 2006-07 remained at the same level as 2005-06 with 17, and the number of 'category 3' incidents, which cause relatively minor environmental damage, rose slightly to 208 (2005-06 194), although it still remains more than 30% lower than in 2001. 

Improving the performance of our sewerage network is both a priority and a challenge for the business. Following a zero-pollution pilot study in one poor performing catchment Welsh Water has approved a £5 million programme to install additional telemetry alarm devices at key points of the network, and a prioritised programme of sewer desilting, cleaning and CCTV inspection. Together, these give Welsh Water a better understanding of the condition of its sewers and help to direct investment appropriately, which will increasingly enable network operators to react quickly to potential problems before any sewer escape has any environmental impact.

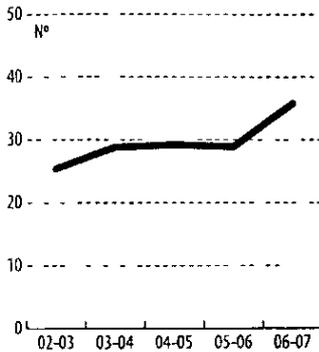
Capital investment

During the year we invested £130 million to improve or maintain our wastewater assets. In all, we completed quality improvement schemes at 188 different locations and significant maintenance schemes at 63 sites. In addition, 35km of new sewers were laid and 26km of sewers were refurbished. 

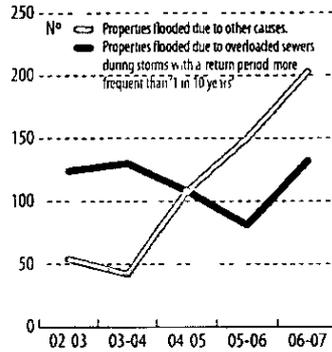
New works opened in 2006-07 included Holyhead wastewater treatment works, following a six-year process of planning, consultation and construction. This scheme which has improved services to customers and delivered environmental benefit to local bathing beaches involved, in addition to the new works, the construction of 16 new pumping stations and associated storm water storage facilities and a new 890 metre marine outfall.

Further information about Welsh Water's wastewater and sewerage performance in 2006-07 can be found in the published report of the Quality and Environment Committee of the Board which is available on our website www.dwrcymru.com.

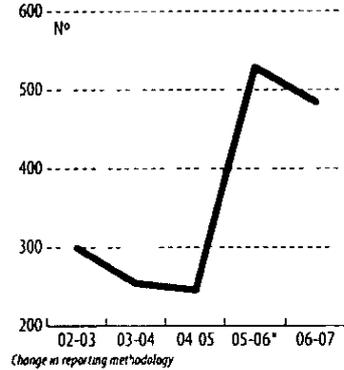
25 Sewer collapses per 1,000km



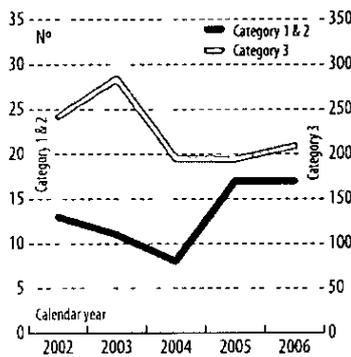
26 Sewer flooding



27 Sewer flooding at risk register



28 Pollution incidents



29 Wastewater investment in the year

Type of work	Spend
Wastewater treatment works improvements	£23.7m
Combined sewer overflows upgrade	£36.6m
First time sewerage provision	£0.9m
Sewer flooding prevention	£6.8m
Sewer maintenance	£17.2m
Sludge treatment	£3.6m
New developments connected	£11.2m
Wastewater asset maintenance	£21.2m
Other	£8.5m
Total	£129.7m

Responsible business

By delivering safe and reliable drinking water and wastewater services we provide an essential public service, but we also have a wider responsibility. Our goal is to be recognised as a valued and trusted partner in the communities we serve.

Education

Since 2001 we have placed considerable emphasis on supporting education and have increased our facilities over this period from one classroom at one environmental education centre to five classrooms at four centres across Wales. In the last academic year almost 12,500 children attended one of Welsh Water's centres and received free curriculum-based lessons, and since our first centre opened in 1997 more than 70,000 children have received lessons designed and led by our seconded teachers. Our approach aims to teach the importance of diverse habitats and nature conservation and promote a better understanding of the importance of water in our everyday lives, as well as communicating key business messages on water conservation and efficiency and public safety.

In the last year we have redesigned our bilingual educational website and associated online interactive resources (www.livingandlearningwithwater.com), and added a new module on water efficiency to our interactive CDROM (Water-World Explorers), all of which are available free to schools in our region. These facilities complement

a website developed with certain other water companies (www.waterintheschool.co.uk), which provides everything required to set up and run a water conservation project.

We also continue to work closely with organisations that have a similar approach to providing education, such as Eco-Schools and our education partners, who include the National Botanic Garden of Wales in Carmarthen, Techniquist in Cardiff, the Hereford Waterworks Museum and The Wildfowl and Wetlands Trust at its National Wetlands Centre at Llanelli. To improve the effectiveness of how we work with our education partners, and to make our education service more accessible to schools located too distant for a day visit to one of our centres, this year we have successfully trialled a new peripatetic teacher role, which will be rolled out in the next academic year.

Associated with our education strategy, for the last three years we have worked in a successful partnership with the Welsh Assembly Government to provide cooled tap water to children in schools across Wales. This recognises that water is beneficial to health (children should drink at least 3-4 glasses of water a day) and can improve concentration and academic performance. Over the same period we have issued more than 70,000 plastic water bottles, which are provided free of charge to children who visit our education centres and are made

available for schools and other youth organisations in Welsh Water's region to purchase 'at cost'.

Sustainability and global citizenship are fairly new subjects in the national curriculum and, in December 2006, 30 teachers received training at a workshop hosted by Welsh Water's teachers. Other participants were Oxfam Cymru, Christian Aid, British Telecom Volunteers, The Riverfront Theatre, Careers Wales and local education business partnerships.

Conservation, heritage and access

Welsh Water's region is rich in both biodiversity and heritage. To ensure our water and sewerage operations do not harm these national assets we continue to develop our conservation consultation database, which holds details of more than 1,100 sites of special scientific interest and more than 4,000 Scheduled Ancient Monuments or other sites of conservation or archaeological interest. This ensures our design teams are aware of such sensitivities at the earliest stage, and that appropriate consultation with conservation and heritage bodies can take place in a timely manner. This process is supported with an annual meeting of senior representatives of both our environmental and heritage stakeholders. We also continue to support the Hereford Waterworks Museum, which collects, restores and displays artefacts associated with the history of water supply in Wales and the adjoining parts of England that we supply.

Healthy living

Welsh Water owns more than 35,000 hectares of land in Wales, much of it both scenic and environmentally sensitive. Access is encouraged at seventeen major reservoir sites, which provide valuable formal, and informal, sporting recreational and leisure resources. Just under a million people visit one of these Welsh Water sites each year, which makes a valuable contribution to tourism and the local economy.

Public safety

Last year we revitalised our reservoir safety campaign with the launch, supported by the Welsh Assembly Government, of a multi-media campaign explaining the dangers of swimming in reservoirs. The campaign ('so you think reservoirs are cool?') targeted all schools in our region via a pod-cast available on our website, posters and fact sheets.

We also work closely with various local community organisations, and for several years we have, in particular, worked with local police forces and other caring organisations to help combat 'distraction burglaries'. In areas where 'Beat the Burglar' partnerships are established, the number of distraction burglaries has fallen.

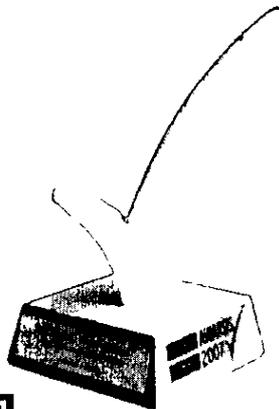
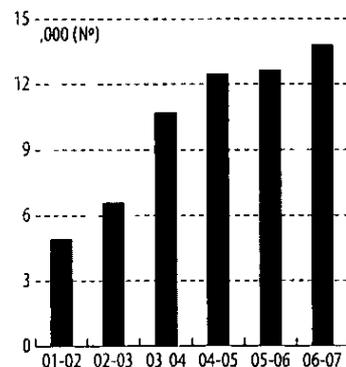
Charity and community projects

Welsh Water is a member of Business in the Community and promotes a community investment scheme for employees who wish to become involved in charitable or other projects within their local communities. Many of our staff, and those of our contract partners, freely give their own time. In 2006-07, 12% of Welsh Water staff signed up to support local schools and participate in a 'World of Work' scheme coordinated by the Mid Glamorgan

Education Business Partnership, which provides business mentoring and mock interview support for 15-16 year olds.

WaterAid is an international charity dedicated to extending access to safe domestic water, sanitation and hygiene education for some of the world's poorest communities. Re-launched in Wales in 2004, the support of our staff and customers means we are well on track to meet the goal of raising £1 million for WaterAid. This is achieved through year-round fund-raising activities, including an annual WaterAid Ball, fun events such as 'It's a Knockout Competitions', a monthly staff lottery and donations from Welsh Water customers.

30 Educational visits

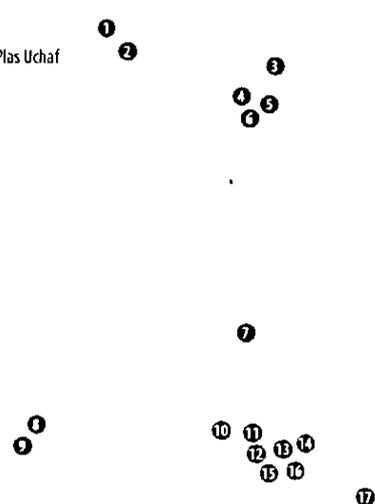


31

Living and Learning with Water
BITC Award for companies who have delivered a long term beneficial impact on communities

32 Main reservoir recreation sites

- 1 Llyn Alaw
- 2 Cefni
- 3 Dotwen and Plas Uchaf
- 4 Llyn Aled
- 5 Llyn Brenig
- 6 Alwen
- 7 Eilan Valley
- 8 Rosebush
- 9 Llys y Fran
- 10 Usk
- 11 Beacons
- 12 Cantref
- 13 Pentwyn
- 14 Talybont
- 15 Llwyn On
- 16 Pontsticill
- 17 Llandegfedd



Our customers

We aim to deliver the best possible service to our customers, and we know that customer recognition of this will be judged on the standards and efficiency of the service our customers receive. So we aim to get things right first time, every time, and always deal with customers in a prompt, courteous and professional manner. 

Improving customer service

Welsh Water has a strong track record of bringing innovation into the water sector to improve efficiency and performance for customers. To ensure this continues into the future, Welsh Water has commenced a £75 million four year programme of IT Enabled Change, which through improved IT systems and streamlined business processes will deliver improvements across our business. Our new Operational Activity Centre, which we opened this year alongside our Billing and Income Contact Centre in Cardiff, now receives and directs response to all customer contacts on matters of operational service or quality for both our water and sewerage services. This has already reduced unnecessary, repeat and abortive calls and seen significantly more customer calls resolved on first contact.

We are also investing in new systems to manage our assets real-time and in the most effective manner, with enhanced capability to support remote diagnosis and operation of assets, and in systems to enhance our capability in terms of work scheduling and mobile working. Key to this is a system to capture

information about the configuration and performance of over 500,000 assets, held in a single database, which essential information is available to Welsh Water and its contract partners as and when it is required. Only by improving our understanding of how our assets perform, can we tailor capital investment and maintenance expenditure more effectively to deliver the best possible value for money for Welsh Water's customers.

Customer contact

The majority of customers prefer to contact us by telephone and last year we received 1.2 million calls to our customer billing or operational contact centres (up 9.4% from 2005-06). We also know that customers prefer not to have to deal with automated telephone response systems, which we use only where necessary, preferring the phone to be answered by a person straight away. In Ofwat's latest reported assessment for 2005-06 of call handling customer satisfaction Welsh Water was rated 4.57 out of a possible score of 5 (2006: 4.59).

In 2005-06 we reported the number of written complaints we received had risen due to the overall price increase at the start of the 2005-10 investment period, changes to our tariff structure, sewer flooding and especially the cryptosporidium outbreak in late 2005. This increase reversed a falling trend, which had seen complaints more than halved in five years. In 2006-07 the total number of complaints was 10,348 (2005-06: 9,948) but 80% of these

related to disputed bills, charging policy or debt collection activity. 

Supported by the Welsh Language Board and Welsh Assembly, we also recently launched an initiative 'Mae gen ti ddewis' (You have a choice) to draw customer attention to the fact that they have a choice over whether to use Welsh or English when they contact Welsh Water with an enquiry.

Keeping customers informed

Before starting any major investment scheme we liaise closely with the local communities that are affected. If water supplies are going to be interrupted, or if access to customer's premises will be required, then information is provided to those customers directly affected by the work and a 24 hour contact telephone number is provided. If required, customers can request a home visit to discuss how the works will impact on them, and we also keep the relevant local authority, community council and Assembly Member informed about major schemes of work.

A new initiative last year was the introduction of a 'Floodcare Plan' to improve communication with customers when they have experienced an incident of either internal or external sewer flooding. Under this new procedure we give a firm commitment to customers in relation to the immediate support we will provide and our longer-term investment plans to avoid reoccurrence of such events.

Additional services

We make extra effort to support our vulnerable, disabled and elderly customers, who at times need a little extra help. Among our additional services we offer large print or Braille bills, bottled water during emergencies, a password scheme for home visits and a 'knock and wait' service for customers who need a little more time to answer the door to callers. Over 3,000 customers are registered to receive one or more of these additional services.

Aided by the Citizens Advice Bureau, we also offer a Customer Assistance Fund which is designed to help customers who have fallen into

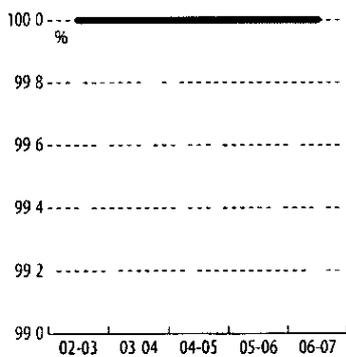
arrears with their bill to return to paying current charges on a regular basis. Last year 1,080 customers benefited from this scheme (2005-06 550).

Customer research

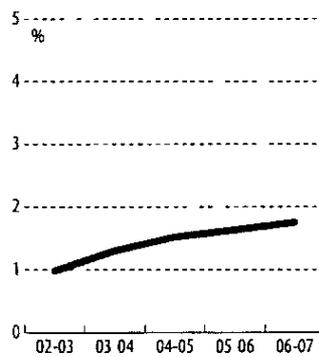
Every six months independent market research tracks customer views on a range of issues, including satisfaction with the service customers receive from Welsh Water, drinking water quality, river and coastal environmental quality and how customers perceive our service on value for money compared to other utilities. The latest research shows a relatively stable position following good improvement made in previous years. **33**

In addition to this general research, independent surveys are undertaken, to monitor the views of customers who have contacted us. This shows that more than 70% of customers are very or fairly satisfied with our overall level of service. We also employ independent researchers as 'mystery shoppers' to assess the quality of our telephone contact service. Each of Welsh Water's contact centres continues to perform well, consistently beating industry benchmarks with satisfaction ratings in excess of 90%. This research is routinely shared with the Consumer Council for Water (Wales) and is used to inform an annual customer service improvement plan.

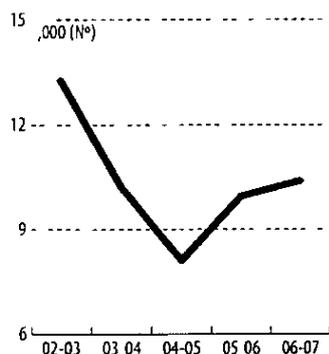
33 Billing contacts dealt with within 5 working days



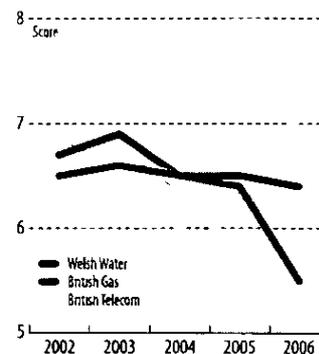
34 Calls abandoned



35 Written complaints received



36 Value for money score (0-10)



Our impact on the environment

Our role in providing good quality and efficient drinking water and wastewater services means that, by the nature of our business, we are a major contributor to the quality of the environment in our region. We seek to operate in a sustainable way that minimises or, where an impact is unavoidable, mitigates any adverse environmental impact from our business activities. Our work programmes are designed to minimise the extent and duration of construction and, wherever possible, to achieve positive benefits for conservation and the wider community.

Climate change

We are addressing the longer-term environmental impacts associated with changing climate conditions, as greater variability in climate (wetter winters, drier summers) introduces new challenges for managing water resources and water quality, the sewer network and storm drainage. Welsh Water emits a significant quantity of greenhouse gases, and in the last three years we have worked in partnership with the Carbon Trust in Wales to develop our knowledge of our carbon footprint, and to identify sustainable opportunities to reduce our emissions. To date our focus has been on local schemes to increase renewable energy capacity and to improve energy efficiency.

We have identified that energy use is responsible for 60% of our carbon footprint, with our process emissions accounting for 35% and transport for the remaining 5%.

Since 2001 the footprint of Welsh Water has grown by some 30%, mainly due to a small number of large new works, including major new wastewater treatment works at Cardiff, Aberystwyth and more recently Holyhead. In 2006-07 our business generated some 284,000 tonnes of carbon emissions, which is broadly similar to the previous year (277,000 tonnes) **17**

Our carbon management programme has helped mitigate the sharp increase in energy costs in the last two years, as well as highlighting the increased energy requirements likely to arise in future years from new quality standards. In particular, with the Carbon Trust, we are trialling a business tool that will reliably calculate the net carbon cost of alternative capital investment solutions required to meet increasing treatment and environmental standards.

Looking forward, work has commenced on a long term plan for Welsh Water – looking 25 years ahead which is to be published during 2007-08. This will set out for consultation our ambition for Welsh Water in respect of its long term approach to climate change mitigation (what we will do to reduce our carbon emissions) and adaptation (how we need to adapt our operations and assets to ensure continued service to customers during more extreme adverse weather conditions). We are determined our proposals, which are still being developed, will deliver a

significant reduction in our current level of carbon emissions.

Energy management

Welsh Water is one of the top ten energy users in Wales, so promoting energy efficiency and awareness is important for our business and for the environment. In 2006-07 we used almost 565Gwh of energy, which is 3% higher than the previous year primarily due to increased pumping across the water network during the dry summer months **18**

Looking forward, we are continuing to target key works and treatment processes to receive additional sub-meter monitoring to identify further opportunity for energy efficiency, as well as increased use of energy efficient electrical motors and initiatives to encourage staff to use energy wisely.

The generation of renewable energy from our resources and business processes is important for climate change mitigation. In 2006-07 combined heat and power (CHP) plants operated to capture and burn 'waste' methane gas generated from eight wastewater treatment sites. This included, as part of our expansion of self-generated electricity, two new CHP plants, at Kinnel Bay and Chester, and a refurbished plant at Penybont that were commissioned towards the end of last year. When fully operational these new works will have doubled renewable energy capacity on our sites, within two years **19**

In addition, in partnership with the Carbon Trust Wales, we are testing the robustness of various on site micro generation technologies, with promising results. Our goal is to set up more sites such as that at Eithinfynydd on the Cardigan Bay coast, which this year has started to generate more power than used at the works making it both energy and carbon neutral.

Our landholdings

We encourage conservation best practice and each of our major reservoir landholdings has a site-specific habitat and species plan. At locations such as Llandegfedd and Brenig Reservoirs we show how, by careful zoning, conservation can be managed alongside popular recreational activities such as fishing and sailing. We also encourage simple but effective measures, such as grassland management, that can make a difference to the

conservation value of some of our operational sites. Our conservation manual and guidance on 'How to make the most of your site' is available to all staff and contract partners.

Working with the Environment Agency in Wales, at Llandegfedd Reservoir Welsh Water has created a system of ditches and reed beds that will ensure a constant area of standing water, even when water levels drop. This has established a new habitat for invertebrates, which are an important source of food for visiting birds, and shelter for nesting wildfowl.

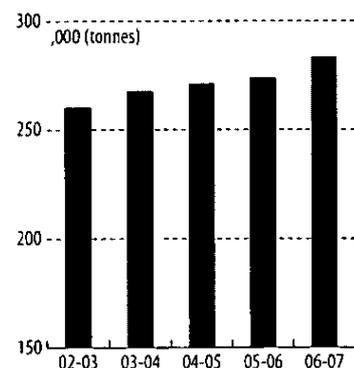
Independent studies on the impact of climate change have reported, for example, that mountain heath land habitats and wildlife in Snowdonia are expected to be under serious threat by 2050, and similar studies report threats to wetland habitats and species. In response we are re-evaluating the habitat value of

Welsh Water's 'green corridor' of landholdings if, as expected over time, wildlife starts to migrate northwards.

Environmental procurement

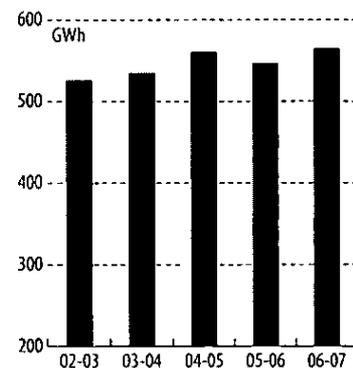
When selecting contract partners we pay significant attention to an assessment of a prospective partner's environmental credentials and track record in showing environmental awareness, responsibility and best practice. Through the procurement chain we also seek, wherever possible, to procure energy and water efficient plant and machinery, thereby maximising environmental and financial benefit. We also pursue opportunities for resource optimisation and waste minimisation and for giving preference to efficient and sustainable waste management options, with landfill as the last option.

37 Total Emissions tCO₂e/year

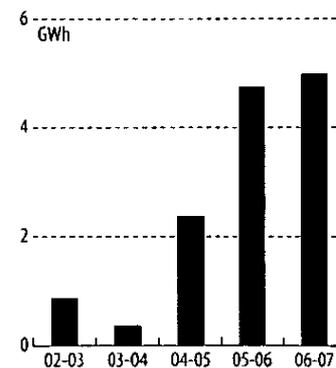


We currently deduct the carbon savings made from using self-generated renewable energy from our total emissions.

38 Energy use



39 Renewable energy capacity



People and partners

Welsh Water has established an 'Asset Management Alliance' (AMA), comprising 3,000 people from 14 different organisations, who work together to look after the water industry in Welsh Water's region and to deliver a reliable and efficient high quality service to Welsh Water's 3 million customers. Our contract partners provide wide experience of best practice from some of the UK's leading utility, construction and infrastructure companies and share Welsh Water's commitment to progressive employee relations.

This alliance of Welsh Water and its contract partners operates on the basis of openness and transparency and aims to ensure a seamless approach to the delivery of all our services and programmes. Its ambition is to set new standards in partnership working. A Principals Leadership Team, comprising the heads of each contract partner in Wales, meets monthly to optimise the way we do business across the AMA.

Staff turnover in our business is only 4%, well below the national average. This has benefits for our business, from staff stability and knowledge of and commitment to the company, but it also provides some major challenges, particularly as regards succession planning and career development. Our HR team works closely with partner organisations in meeting these challenges and on such issues as organisational

design, change management, and the optimisation of partnering and performance management. 

All Welsh Water employees have a 'Personal Development Plan', which each year translates company objectives into personal objectives against which individual performance can be evaluated. In this way, a 'golden thread' is established through the business with the company business plan disseminated into individual sets of objectives.

New initiatives in 2006-07 include the introduction of an assessment centre approach to aid recruitment of senior roles and the development, with the University of Wales Institute, Cardiff, of a knowledge transfer partnership which will provide technical graduates with high calibre placements, while also developing expert knowledge in the business for our programme of IT enabled change.

The views of our staff are important and these are independently tested through an annual employee satisfaction survey. Evidence from our latest survey (January 2007) shows a continuing high general level of satisfaction. The full results of the survey are shared with all employees, together with the resulting action plan that management considers appropriate. 

Keeping staff informed on company performance and key business issues is important. We achieve this via monthly local team meetings, an annual staff forum, to which all Welsh Water staff are invited and a quarterly magazine - 'The Link'. We also provide regular opportunity for all staff, in small groups, to meet the Managing Director and ask questions directly. Emails and the employee intranet are also used to communicate immediate news and announcements, and, working with staff, the intranet has been redesigned this year, to improve its effectiveness and use.

Employee reward and recognition is closely aligned to business performance, with an annual cash bonus linked to Welsh Water's relative ranking in Ofwat's annual Overall Performance Assessment league table and financial performance. Compensation and Benefit packages are regularly benchmarked against the Welsh Employment market and the UK Industrial and Services market.

This year we offered all staff the opportunity to attend a pensions surgery with a qualified financial advisor and access to the company's pension scheme actuary. Some 20% of staff attended, and all staff received a 'total reward statement' for the first time.

Occupational health and safety

The health, safety and welfare of our employees and all those who work with us, is of the utmost importance, and we operate a proactive health and safety management system which applies to all contract partners and their first tier suppliers. In 2006-07 the number of health and safety reportable incidents fell by 6.7%, continuing the trend of the last five years. Regrettably, against this backdrop of continuous improvement, in May 2006 a colleague employed by a contractor experienced a fatal accident, which is still being investigated by the police and Health and Safety Executive.

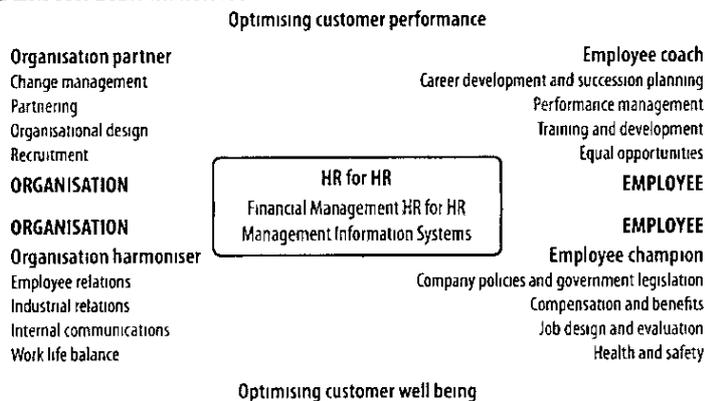
During the year our partners implemented 172 risk based improvement plans, which were 96% complete during the year, focusing on improvements in occupational health as well as managing risks to safety. We promote health and safety best practice and shared learning through an AMA steering group and a process of 'cross partner' audits, which we also verify through independent external audit.

During 2006-07 Welsh Water embarked on a review of occupational health and safety procedures with a view to securing certification to OHSAS 18001 by April 2008. We also enhanced our

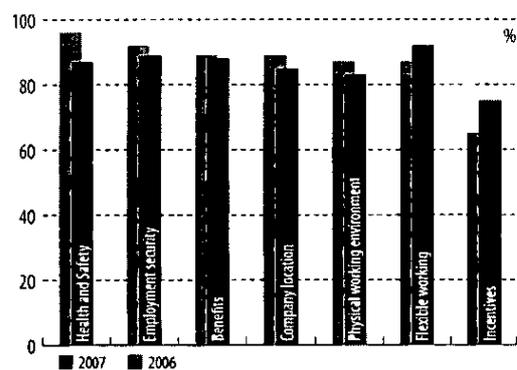
on-line reporting of health and safety performance and document management, and extended training initiatives to increase staff competency in investigating health and safety incidents.

In March 2007 Welsh Water held its first Occupational Health and Safety Conference, sponsored by Mitsui Sumitomo Insurance, which brought together health and safety professionals from Welsh Water and its major partners. The conference also introduced a new award to recognise contract partners demonstrating best practice in the management of occupational health and safety.

40 The role of Human Resources



41 Employee satisfaction survey



Further details of our health and safety performance and approach are available in our 2007 Health and Safety Report which is available on request or via our website www.dwrcymru.com

Financial review

Glas Cymru's financial strategy is to offer a secure, low risk investment to long-term investors. By strengthening our financial position, we intend to keep our future borrowing costs low, enabling us to finance future investment in the business efficiently, whilst having the scope to return money to our customers through sustained 'customer dividends'

Financial results

The only trading activities of the Glas Cymru Group are carried out by its principal subsidiary, Welsh Water. The report and accounts of Welsh Water (Dŵr Cymru Cyfyngedig) for the year to 31 March 2007 are published separately.

Glas Cymru's turnover in the year to 31 March 2007 was £578 million (2006 £554 million) – an increase of 4%. The increase primarily reflects the price increase of 6.4% in the year offset by a loss of revenue due to customers switching to metered charging and a reduction in consumption from metered and trade effluent customers. The effect of 'customer dividends' in the year was that turnover was some £25 million (2006 £23 million) below the level that would have resulted from the full price control allowed by Ofwat. The rate of voluntary customer switching to metered charging in the year slowed somewhat to nearly 22,000 customers (2006 27,000 customers), whilst some 9,000 new customers (2006 10,000 customers) were added during the year, who are all metered.

Net interest charges for the year were £152 million (2006 £150 million). Despite interest rate increases, the average cost of net debt during the period was 6.2% (2006 6.4%), reflecting the benefit of refinancing undertaken during the year. In addition, a credit of £46 million is made to the income statement for the movement in the fair value of financial instruments (2006 £33 million charge), which is a non-cash item.

Profit after tax was £33 million (2006 £16 million). This profit was made after funding the 'customer dividend' of £19 for customers receiving both water and wastewater services. The Board of Glas Cymru has decided to increase the 'customer dividend' for 2007-08 to £20.

The tax charge for the period was £14 million (2006 £5 million credit), comprised entirely of a deferred tax charge.

Continued focus on cost control

Glas Cymru's operating costs (excluding infrastructure renewals expenditure and depreciation) were £229 million (2006 £213 million), which represents an increase in real terms of some £9 million. This increase largely reflects substantial increases in energy costs, which were some £8 million (or 29%) higher than in the previous year, which in turn were some £9 million higher than the year before.

Around 70% of operating costs were incurred under outsourced service contracts, including the contract with United Utilities Operating Services (UUOS) for the operation of the water network and the wastewater network in North Wales and with Kelda Water Services, for the operation of the wastewater network in South Wales and Herefordshire. These contracts operate on a target cost basis which are designed to incentivise further improvements in operating efficiency in the period up to March 2010.

Customer debt recovery remains subject to very close attention by Welsh Water and by Thames Water, the billing and income services contract partner. Despite a difficult environment – water companies are not allowed to disconnect supplies to domestic customers due to non-payment – cash collection performance was on target. The bad debt charge for the year of £11 million (2006 £8 million) represents around 2% of annual turnover.

Capital expenditure by Welsh Water during the year (before capital grants and developer contributions and including infrastructure renewals expenditure) was £269 million (2006 £238 million), bringing the total expenditure over the first two years of the five-year AMP4 period to £507 million or some 2/5ths of the total programme. Welsh Water works with an alliance of capital investment partners (Laing Utilities, Morrison,

42 Breakdown of operating costs

£229m



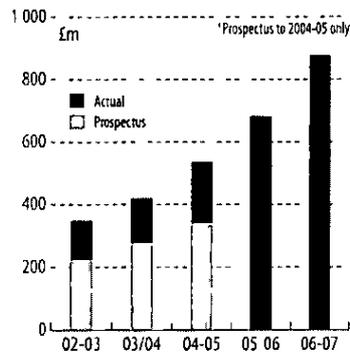
- Operations contracts
- Billing and Call Centre
- Other contracts
- Laboratories and sampling
- Welsh Water's own costs
- Other (bad debt charge rates licence fees, etc.)

AMEC, Costain, Imtech Process, MEICA, and Black and Veatch) with the aim of delivering the AMP4 investment programme at the best value for money for customers. A priority during the first two years of the programme has been to reappraise rigorously the design of certain key schemes with a view to achieving the reductions in unit costs assumed by Ofwat in the 2004 Price Review. Welsh Water is planning to invest some £600 million over the next two years, a challenging target compared to historical levels. At this stage, it is expected that investment expenditure over the AMP4 period as a whole of some £1.3 billion will be broadly in line with the allowance made by Ofwat in the Final Determination.

Financing strategy and credit rating

The Board considers that it is in the best long-term interests of Welsh Water's customers to continue to reduce the level of gearing, with a view to achieving further reductions in its cost of finance. The Board intends to reduce gearing to around 70% and to keep it at that level going forward. The Board believes this can be achieved whilst maintaining the current progressive 'customer dividend' policy.

43 Growth in financial reserve



Credit ratings are unchanged during the year. However, on 14 June 2007, Moody's assigned an A3 corporate rating to Welsh Water, reflecting the improved credit quality of the company.

To protect the Group's high credit quality, the Board has implemented prudent financial policies, covering the fixing of interest rates and the investment of cash balances. Glas Cymru has minimised its exposure to movements in market rates, with a minimum of 85% of its liabilities being fixed rate, index linked (to UK RPI) or matched by cash balances. The Board considers that liabilities index linked to UK RPI inflation are particularly appropriate for the business, as its revenues and RCV are also linked to RPI through the regulatory system operated by Ofwat. As at 31 March 2007, approximately 57% of the group's gross debt was index linked via bonds and derivatives.

Financing activities

A key measure of financial performance for Glas Cymru is the level of gearing – the ratio of net debt to Regulatory Capital Value (RCV). By reducing the level of gearing from around 93% on the acquisition of Welsh Water in May

44 Net debt and reserves

As at 31 March	2007 £m	2006 £m
Regulatory Capital Value	3,310	3,042
Net Debt	2,434	2,359
'Reserves' (RCV less net debt)	876	683
Gearing (net debt/RCV)		
Senior debt	69%	73%
Senior debt + class C bonds	73%	77%
Total debt	74%	78%

2001 to 74% as at 31 March 2007, the financial position of the Group has been significantly enhanced. 'Financial reserves' (RCV less net debt) now stand at £876 million (2006: £683 million).

Net debt (throughout as defined for covenant purposes in the Common Terms Agreement for the bond programme) increased during the year by £74 million to £2,434 million, including the indexation charge of £23 million (2005: £17 million). The additional finance raised was used to fund part of the capital investment programme.

During the year Welsh Water drew down a further £75 million under a term loan facility with the European Investment Bank bringing the total drawn borrowings from this source to £135 million. These loans are used to finance a range of infrastructure investment projects, the majority of which are in European Objective One funding areas and which will all have a significant positive impact on the environment in Wales.

The Group has taken advantage of favourable market conditions and, on 28 November 2006, Dŵr Cymru (Financing) Limited (DCFL) issued £50 million Class B5 bonds via

Lloyds TSB at an index linked interest rate of 1.375%. This was followed on the 7 December 2006, when £100 million Class A6 bonds were issued via Royal Bank of Scotland at an effective index linked rate of 1.35%

The expected maturity of the out-standing fixed rate and index-linked bonds now ranges from 2011 to 2056, with not more than 20% falling due in any two-year period, in accordance with our refinancing policy **A A A A A A**

The listed bonds issued by DCFL have continued to perform well during the year, regularly trading at margins below many other equivalent water sector bonds of similar maturity. Glas Cymru believes that this performance reflects continued investor confidence with its performance and its improving financial position.

Cash on deposit or invested as at 31 March 2007 amounted to some £158 million, which together with undrawn bank facilities of £345 million, gave the Group a high degree of liquidity.

Future prospects

The objective of the Board will be to continue to improve the financial performance of the company during the period to 31 March 2010. The Board considers that the prime measures of this financial performance are the Regulatory Asset Ratio (RAR - the ratio of net debt to RCV), the various Interest Cover Ratios (ICR - as defined in the Common Terms Agreement) and bond credit rating as independently measured by three rating agencies, Moody's, Standard & Poor's and Fitch Ratings.)

Glas Cymru has taken advantage of the favourable rates of interests available in the financial markets during 2006-07 substantially to pre-fund its capital requirements for the period to 31 March 2010, the end of the current five-year investment and price control period. The Board believes that its financial strategy will put the company in a strong position to raise the funding for the following five-year investment programme in the period to 2015 on efficient terms, which is an important part of the company's strategy to keep down customers' bills in the long-term.

The main risks to the achievement of this financial objective involve upward cost pressures. The unit costs of investment schemes are under upward pressure due to increasing materials costs and emerging resource shortages in the construction industry. Welsh Water continues to seek to mitigate these input cost increases by securing the resources for a long-term programme of work with its partners and by revisiting designs and working methods to secure offsetting efficiency improvements.

In addition, power costs have increased dramatically over the last two years and Welsh Water, like all water and sewerage companies, has a large energy requirement, notably for pumping and treatment processes. The increase in power prices can be only partially offset by improved working practices and investment in energy efficiency schemes. More recently, power prices have fallen back, which has enabled Welsh water to purchase a large proportion of its power needs for the year to 31 March 2008 at a reduced cost.

However, the risk of future volatility in power prices remains. Under the target cost arrangements, these upward cost pressures are shared only to an extent between Welsh Water and its relevant partners.

Welsh Water and its partner, Thames Water, also maintain a tight focus on customer cash collection in recognition of the continuing risk to cash collection posed by increasing water bills and the absence of a disconnection sanction.

The company does not expect to pay tax on its trading profits during the year to 31 March 2008, due to the availability of tax allowances on its investment programme. Future tax liabilities beyond that date will also be primarily influenced by this factor.

Disclaimer

This Report contains certain forward-looking statements with respect to the future business and taxation prospects and the strategies of the Glas Cymru Group. These statements and forecasts involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. There are a number of factors that could cause actual results or developments to differ materially from those expressed or implied by these forward-looking statements. Past performance is no guide to future performance and persons needing advice should consult an independent financial adviser.

45 Key characteristics of the Bonds currently in issue

Bond class	Nominal (on issue) £m	Interest rate (on issue)	Interest basis	Expected maturity	Legal maturity
A1	350	6.015%	Fixed rate	31 March 2028	31 March 2028
A4	265	3.514%	Index-linked	31 March 2030	31 March 2030
A5	85	3.512%	Index-linked	31 March 2031	31 March 2031
A6*	100	4.473%	Fixed rate	31 March 2057	31 March 2057
B1	325	6.907%	Fixed rate	31 March 2021	31 March 2021
B3	128	4.377%	Index-linked	31 March 2026	31 March 2026
B4	75	4.375%	Index-linked	31 March 2027	31 March 2027
B5	50	1.375%	Index-linked	31 March 2057	31 March 2057
C1	125	8.174%	Fixed rate	31 March 2011	31 March 2036

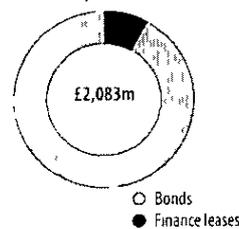
Bonds issued by Dŵr Cymru (Financing) Limited
 For full details of bonds refer to Prospectus dated 4 December 2006 available on our website www.dwrwymru.com
 *Swapped to an effective index-linked rate of 1.35%

46 Credit ratings of Glas Cymru bonds

	Standard & Poor's	Moody's	Fitch Ratings
Class A Bonds	AAA	Aaa	AAA
Class B Bonds	A-	A3	A
Class C Bonds	BBB	Baa2	BBB+

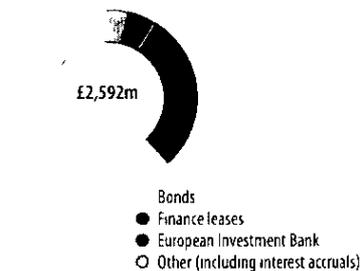
47 Source of gross debt 2001

As at 11 May 2001



48 Source of gross debt 2007

As at 31 March 2007



49 Credit rating of debt 2001

As at 11 May 2001



50 Credit rating of debt 2007

As at 31 March 2007



Risk

The assessment and mitigation of risk is a key priority for the business. The Board has overall responsibility for the system of risk management and internal control, as described in the Governance Statement on page 47 of this report.

Glas Cymru cannot diversify into activities unrelated to those of a regulated water and sewerage business. This means that the nature and balance of risk to be managed by the group is different, and in many respects lower, than that of other companies in the UK utility sector.

The Quality and Environment Committee of the Board (QEC) is an important part of our governance arrangements, providing critical focus on 'quality', 'service' and the management of risk in its monitoring of the performance of Welsh Water and its contract partners. The work of QEC is described in more detail in its annual report to the Board, which is available on our website or on request from the Company Secretary.

The principal risks faced by the group fall into the four broad categories of strategic risk: regulatory, operational, financial and procurement risks.

Regulatory risk

Regulatory risk can arise from Ofwat's price control determinations or from changes in the regulatory environment, such as proposals to increase competition in the water sector, which would affect all companies in the sector in the similar manner.

A price control determination generates risk in a number of ways, for example, if it were to provide an inadequate cost of capital allowance or be based on regulatory assumptions in respect of operating costs, required capital investment or revenue forecasts that prove unrealistic. Welsh Water's business plan seeks to meet and, where possible, exceed the assumptions made by Ofwat in its determination for the period 2005-10. However, at this stage in the five-year regulatory period, this objective is subject to considerable uncertainty. The outcome of the next periodic review process in 2009 will also directly impact on future cashflow and profitability.

Welsh Water has to provide extensive data to the regulators each year on all aspects of its business. This responsibility is taken very seriously and processes are reviewed annually to ensure that regulatory data are of appropriate accuracy and robustness.

Our Licence requires us to have strong governance arrangements, which ensure that the responsibility of Welsh Water for water quality, environmental quality and public health is not blurred. Further details of the group's governance arrangements can be found in the Governance Report on pages 43 to 49.

Operational risk

Operational risk is varied and may include:

The impact of major operational incidents on public health, environmental quality or customer

service, whether arising from equipment failure, from natural events (e.g. acts of God, or contamination from naturally occurring compounds) or from third party interference with Welsh Water assets or equipment. Changes in environmental, consumer protection and public health and safety law and regulation, which typically require ever-higher standards of water quality, environmental and safety performance.

The impact of more extreme weather conditions (i.e. climate change) on the availability of water resources during droughts and the ability of Welsh Water sewerage network to cope with severe rainfall events.

Health and safety incidents arising from the operation of a large and complicated network of assets. Our ability to retain and develop key people within Welsh Water thus ensuring that the business has the appropriate competencies and experience needed to meet its long term obligations.

The impact of operational change associated with our five year £75 million programme of IT enabled change (ITEC), which will include the replacement of ageing mainframe IT systems with new and more flexible systems. Accompanying the ITEC programme will be a phased review and simplification of business processes and the development of new tools to enable Welsh Water to become ever more efficient in its delivery of services to customers.

Policies and operational strategies exist to mitigate each of these risks that could create an adverse effect on the reputation, operating results and financial position of Welsh Water

In the long term, Welsh Water needs to maintain its £14 billion asset base to deliver the high standards of water and wastewater services that customers expect. The rate at which assets can be maintained, refurbished or replaced is determined by the funding allowed by Ofwat through its five yearly price determination. At the rate of investment provided in the price determination for 2005-10, the average age of Welsh Water's assets will be greater at the end of the period than at the start, which may increase risk of future asset failure and poor serviceability.

The availability and terms of insurance as a tool to mitigate business risk is also relevant. Insurance policies cover property, business interruption, public liability, environmental pollution and employer's liability. These are generally multi-tiered, with the first tier of self insurance in the form of a deductible and the second, and often further tiers, of cover provided by external insurers in the market.

Financial risk

Like any business, Welsh Water is exposed to many financial risks, in particular between regulatory price reviews. Examples include

Revenue risk, in particular, changes in metered demand, the loss of large water business customers, and the introduction of competition into water supply

The collection of customer charges and non-recovery of customer debt, which is a particular risk following the prohibition in 1997 of disconnection of domestic water supply for non-payment. Failure by Welsh Water to achieve the challenging price determination targets set by Ofwat for operating and capital efficiency or to deliver the capital investment programme. External cost pressures, such as the impact of recent increase in power prices, which could also prevent the business from achieving Ofwat's operating and capital cost targets set at the last price review.

The overall financial risk is that the group may not be able to finance the operating and capital investment obligations of Welsh Water, which continue to be financed from cash flow from operations (i.e. customer bills) and debt financing.

Group policy is to ensure that the business has sufficient committed facilities available to meet at least twelve months anticipated net cash requirement. However, recognising favourable market conditions, financing risk has been significantly reduced during the first two years of AMP4 as a result of treasury activity, which has substantially completed Welsh Water's financing requirements for the period until 2010. The group's financial position at 31 March 2007 shows a significant balance of cash and undrawn borrowing facilities available, which gives the business a high degree of liquidity.

Rising pension costs due to factors outside the Board's control, such as rising pensioner longevity, is also a risk, however, with only 160 members the closed Welsh Water defined benefit pension scheme is small relative to the size of the business.

Procurement risk

Procurement risk is a particular risk for Welsh Water, with 85% of its annual operating and capital expenditure being undertaken by outsourced service providers. Our framework for competitive outsourcing is described in a published Procurement Plan which is available on Welsh Water's website or on request from the Company Secretary.

Initial outsourced operating contracts were generally let for a period of four years, which ended on 31 March 2005. New outsourced contract arrangements for water and wastewater services were put in place following a successful competitive re-tendering, which provided for contract partners to work with Welsh Water for up to 15 years (subject to price and performance reviews every five years). This was designed to encourage contract partners to view their involvement with Welsh Water on a longer term basis than was previously possible, thereby reducing the risk of short term conflict of interest and encouraging longer term investment in the resources, people and systems needed to continue to deliver high levels of service to Welsh Water customers.

Definition, purpose and target for each KPI

Measure	Purpose	Source	Target	Progress to Target
Bond credit rating Strategy: Financing	A direct way of further reducing Welsh Water's financing cost is to improve the credit rating of the group's corporate bonds. Executive directors are incentivised to maintain bond ratings. Rating agencies apply their own definition and methodology in assessing bond credit rating.	Bond ratings as independently determined by three rating agencies: Standard & Poor's, Moody's and Fitch IVE	Corporate credit rating of A grade	✓
Gearing Strategy: Financing	The Glas Cymru business model aims to reduce Welsh Water's asset financing cost, the industry's single biggest cost. Improved credit quality is key to keeping Welsh Water cost of finance as low as possible. Gearing is the ratio of Net Debt to Regulatory Capital Value of Welsh Water.	Glas Cymru Investor Report	To reduce gearing to around 70%	✓
Interest cover Strategy: Financing	The Glas Cymru business model aims to reduce Welsh Water's asset financing cost, the industry's single biggest cost. Meeting interest cover covenants is key to maintaining investor confidence and to keeping Welsh Water cost of finance as low as possible. Interest cover is the ratio of operating cashflow (before maintenance) to net interest (excluding indexation).	Glas Cymru Investor Report	To maintain interest cover consistent with target credit rating	✓
Customer Dividend Strategy: Customer value	As well as improving credit quality, financing efficiency is used to build up reserves to insulate Welsh Water and its customers from unexpected costs and to have scope to return money to customers through sustained customer dividends. Through the customer dividend, therefore, the customers of Welsh Water share in the success of the business.	Glas Cymru Audited Accounts	Progressive customer dividend policy	✓
Overall Performance Assessment (OPA) Strategy: Customer service	OPA is the measure published by Ofwat of each company's overall delivery of service to customers. It reflects a broad range of services provided to customers across key areas of water supply, sewerage service, security of supply, customer service and environmental impact.	Ofwat	Upper quartile performance relative to the ten water and sewerage companies in England and Wales	✓*
Customer satisfaction Strategy: Customer service	Since 2001 the Board has monitored customer satisfaction with the services provided by Welsh Water via a six monthly customer opinion survey undertaken by Beaufort Research. Although customer opinion can be influenced (often adversely) by media coverage of events elsewhere in the UK water industry, this is an important indicator of the company's progress.	Beaufort Research	To maintain consistent high levels of customer satisfaction	✓
Overall bacteriological water quality Strategy: Customer service	An important measure of the quality of water supplied to customers is compliance with bacteriological standards. There is also a correlation between failures in bacteriological quality and unsatisfactory water supplied to customers. This measure is not a component of Ofwat's OPA index.	Drinking Water Inspectorate	100% of all assets compliant	✓
Health and safety (Accident Incident Rate – AIR) Strategy: Occupational health and safety	AIR is a statistical index used by the Health and Safety Executive (HSE) to benchmark company and sector relative performance. It is the number of reportable incidents occurring in a reported period per 100,000 employees.	June Return	To have one of the best AIR of the UK's water and sewerage companies and to compare favourably with appropriate HSE benchmark for AIR.	✓

* Latest published data for the year ended 31 March 2006

The service level indicators reported on page 3 derive from Welsh Water's annual regulatory report to Ofwat (the 'June Return') and are measures defined and monitored by Ofwat, the Drinking Water Inspectorate or the Environment Agency. An Overview of the latest June Return is available on request or from our website www.dwrcymru.com

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The Directors

The Board of Directors is responsible for the strategic direction of the Company and for reviewing operational and financial performance

LORD BURNS, Chairman ^(N)

Appointed Chairman in July 2000 Lord Burns (63) is Chairman of Abbey National plc and Marks and Spencer Group plc and a Non Executive Director of Banco Santander Central Hispano SA, and Pearson Group plc He was made a Life peer in 1998, and is a former Chief Economic Advisor and Permanent Secretary to HM Treasury He is also Chairman of the Governing Body of the Royal Academy of Music and former Chairman of the National Lottery Commission

NIGEL ANNETT, Managing Director

Appointed Managing Director in January 2005 Mr Annett (48) has been an Executive Director of Glas Cymru since April 2000, and of Dŵr Cymru (Welsh Water) since May 2001 He was previously a Director of Welsh Water between 1992 and 2000, prior to which he held various investment banking positions with Schroders, County Natwest and Wasserstein Perella

CHRIS JONES, Finance Director

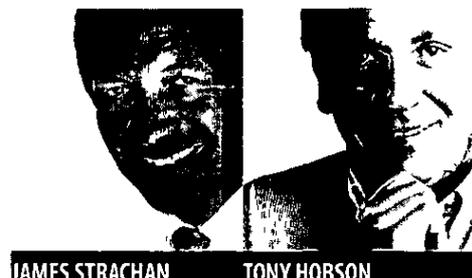
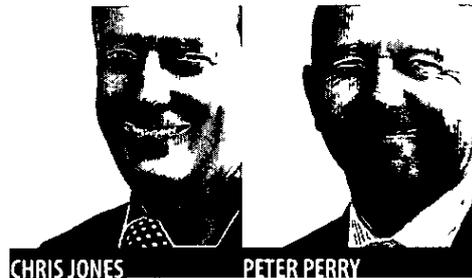
Appointed Finance Director of Glas Cymru in April 2000 and of Dŵr Cymru (Welsh Water) in May 2001 Mr Jones (43) was previously Director of Regulation of Welsh Water and South Wales Electricity PLC Before joining Welsh Water in 1995, he was a Director at National Economic Research Associates and, prior to that, worked for HM Treasury on nationalised industries and privatisation He is a Non Executive Director of the Principality Building Society and a Member of the Board of the Institute of Welsh Affairs

PETER PERRY, Operations Director ^(O)

Appointed Operations Director in August 2006 Mr Perry (45) has a civil engineering background and was formerly the Chief Operating Officer for United Utilities Operational Services (UUOS), having previously been the Operations Director for UUOS with responsibility for the operational contract with Welsh Water and UUOS's water interests in Scotland and Ireland Prior to joining UUOS he worked for Dŵr Cymru (Welsh Water) for over 17 years

JOHN BRYANT, Non Executive Director ^(O/NRM)

Appointed a Non Executive Director in March 2001 Mr Bryant (63) is a former Chief Executive of British Steel and, until December 2000, was Joint Chief Executive of Corus Plc He is a Non Executive Director of Costain Group Plc, and was a Non Executive Director of Bank of Wales Plc between 1996 and 2001



ALISON CARNWATH, Non Executive Director ^{(A)(R)(N)}

Appointed a Non Executive Director in July 2000 Mrs Carnwath (54) is a Non Executive Director of Friends Provident Group Plc, Land Securities Plc and Man Group Plc. After qualifying as a Chartered Accountant, Mrs Carnwath spent 20 years working in investment banking during which time she was a Director of J Henry Schroder Wagg and a Managing Director of Donaldson Lufkin Jenrette. She is also a former Director of Vitec Group plc, QA Group plc, Arcadia Group plc, Nationwide Building Society, Gallaher Group Plc, Manweb plc and National Power plc

GERAINT TALFAN DAVIES, Non Executive Director ^{(A)(R)(N)}

Appointed a Non Executive Director in July 2000 Mr Davies (63) is a former journalist whose career spanned both public and private sector broadcasting including Controller of BBC Wales throughout the 1990s and later as a member of the Radio Authority representing Wales. He is also Chairman of the Institute of Welsh Affairs and a member of the BT Wales Advisory Forum, and former Chairman of The Arts Council Wales (2003-2006)

DAME DEIDRE HINE, Non Executive Director ^{(Q)(R)(N)}

Appointed a Non Executive Director in March 2001 Dame Deidre (69) is Chairman of the BUPA Foundation and the Royal Society of Medicine Press Board, a member of the House of Lords Appointments Commission and President of the British Medical Association. She is a former Chairman of the Commission for Health Improvement, a former President of The Royal Society of Medicine and a former Chief Medical Officer for Wales. Dame Deidre was awarded the DBE in 1996 for services to medicine.

TONY HOBSON, Non Executive Director ^{(A)(R)(N)}

Appointed a Non Executive Director in February 2001 Mr Hobson (59) is the Chairman of Northern Foods Plc and Sage Group Plc and a Non Executive Director of HBOS Plc. He is a Chartered Accountant and was the Group Finance Director of Legal & General Group Plc between 1987 and 2001, and the Senior Independent Director of Thames Water Plc at the time of its acquisition by RWE in 2000.

JAMES STRACHAN, Non Executive Director

Appointed a Non Executive Director in June 2007 Mr Strachan (53) is a Non Executive Director of Legal & General Group plc and Care UK plc, and is a member of the Court of Directors of the Bank of England. He was previously Chairman of the Audit Commission (2002-06) and a Board member of Ofgem, the energy regulator. He is Chairman of RNID (the disability charity), where he was previously Chief Executive, a Trustee of Somerset House, and he is a former Disability Rights Commissioner and Trustee of the charity Save the Children. Earlier in his career Mr Strachan was an investment banker with Merrill Lynch for 13 years, latterly as a Board member of Merrill Lynch International.

Membership of Board Committees

(Q) Quality and Environment
(A) Audit
(R) Remuneration
(N) Nominations

The Members

There are presently 63 Members, including the Directors of Glas Cymru

A key role of the Members is to ensure that the business remains focused on its primary purpose of providing efficient high quality water and sewerage services to Welsh Water's customers. In so doing Members carry out an important corporate governance role.

Members are selected in accordance with a process overseen by an independent Membership Selection Panel, which is required to maintain a balanced and diverse membership, which as far as possible is broadly reflective of the range of customer and other stakeholder interests served by Welsh Water. Membership is personal, therefore Members do not represent any particular group or stakeholder interest. Members do not receive fees nor do they have any other financial interest in Glas Cymru.

A list of the Members of Glas Cymru, together with the Company's Membership Policy and Terms of Reference of the Membership Selection Panel, is published on our website www.dwrcymru.com or can be obtained by writing to the Company Secretary.

Directors' report

The Directors present their report and the audited financial statements of Glas Cymru Cyfyngedig for the year ended 31 March 2007.

Principal activities

A description of our principal activities and a review of the development and performance of the business, including financial and operational performance, key performance indicators and a description of the principal risks and uncertainties facing the business are described in the Operating and Financial Review on pages 4 to 30 ('OFR'). The OFR contains certain information of a forward-looking nature, which, by its nature, is uncertain since future events and circumstances can differ from those anticipated. Nothing in this annual report should be construed as a profit forecast.

Financial results and 'customer dividend'

Profit after tax for the financial year ended 31 March 2007 was £33m after funding the 'customer dividend' (2006: £16 million).

In 2006-07, customers received a 'customer dividend' of £25 million, or £19 per customer served by Welsh Water (£9.50 for water and £9.50 for wastewater services). For the financial year 2007-08, for which water bills have been issued, the 'customer dividend' was increased to £20 per household (£10 for water and £10 for wastewater services) at a cost of £27 million.

Directors

Details of the present Directors are given on page 32. With the exception of Jim O'Sullivan who resigned on 31 July 2006, Peter Perry who was appointed a Director on 1 August 2006, and James Strachan who was appointed a Director on 1 June 2007, all Directors served throughout the financial year. No Director has, or has had, a material interest, directly or indirectly, in any contract significant to the Company's business.

At the Annual General Meeting on 6 July 2007 ('2007 AGM') Peter Perry and James Strachan will seek election as Directors, and Nigel Annett, Chris Jones and Lord Burns will retire by rotation and seek re-election as Directors. Further details are set out in the governance report on page 44 and in the Notice of 2007 AGM.

Details of the remuneration of individual Directors and of the remuneration strategy approved by the Board are included in the Remuneration Report for the year ended 31 March 2007 on pages 37 to 42. A resolution will be proposed at the AGM to approve the 2007 Remuneration Report.

The Company has in place Directors' and officers' insurance giving cover against legal action brought against the Directors and an indemnity in circumstances where they are not considered to be culpable. Details are available from the Company Secretary on request.

Members

At the date of this report, Glas Cymru has 53 Members excluding the Directors of the Company but including 3 Members appointed during 2006-07 and 2 Members appointed subsequent to the financial year-end. Details of changes in the membership since the 2006 AGM, together with information about the role of Members and the process for their appointment under the direction of an independent membership selection panel, can be found in the Governance Report on page 48. Further information on this, and brief details of the current Members, is available on request or may be obtained from our website www.dwrcymru.com.

Responsible business

In addition to the information below, we describe our approach to meeting our corporate social responsibilities in the OFR on pages 16 to 23. Social, environmental and ethical risks are routinely taken into account in the internal control processes described in the Governance Statement on page 47.

Employees

At 31 March 2007 Welsh Water employed 165 people. Other than the Directors of the Company, Glas Cymru has no employees.

Health and safety

We are committed to achieving high standards of health and safety, as there is nothing more important to us than the health and safety of the people who work for us, and those we affect through our work.

The process of health and safety management we adopt across our outsourced business structure, the performance of Welsh Water and its contract partners in 2006-07 and our current challenges and goals are set out in detail in our 2007 Health and Safety Report. A copy of this document is available on request or may be obtained from our website www.dwrcymru.com.

Environment and community

Continuous improvement in environmental performance and in managing the direct and indirect environmental impacts of the business is key to our future success. Our performance is monitored by the Quality and Environment Committee of the Board ('QEC'), who also track development of key operational strategies as we aim to develop more sustainable water and wastewater businesses based on environmental best practice and knowledge. QEC also reviews the cause of and Welsh Water response to all major environmental incidents. As in previous years, a copy of the 2007 QEC Report is available on request or may be obtained from the Welsh Water website.

The business also encourages active participation by our staff in the community, through various forms of volunteering, charitable fund raising and community based projects, examples of which are included in the OFR.

Research and development

All expenditure on research and development is incurred by Welsh Water, which continues to monitor and selectively participate in water industry initiatives, most notably through membership of UK Water Industry Research Limited. Through this, and by continuing to benefit from a sharing of best practice from the R&D investment and initiatives by Welsh Water's outsourced contract partners, we aim to maintain our achievements in improving operational efficiency, and to ensure continued compliance with appropriate national and international standards for potable water, sewage effluent and sludge treatment.

Payment policy

Our policy is to agree payment terms at the start of a relationship with a supplier which will only be changed by agreement. Payment will be made in accordance with agreed terms, save where we advise suppliers when an invoice is contested, which we will do without unreasonable delay. We will seek to remedy disputes as promptly as possible. Standard payment terms to suppliers of goods and services will be 30 days from date of receipt of a correct invoice for satisfactory goods or services which have been ordered or received, unless other terms are agreed in a contract.

In 2006-07, the average payment period was 43 days (2006: 61 days). Regulations require that in calculating this we include within trade creditors monies retained under contract in respect of Welsh Water capital investment projects. This level of retentions varies from year to year and adversely affects the average payment period for the year.

Donations

During the year, charitable donations amounted to £32,874 (2006: £33,395). Individual donations of above £200 were made to WaterAid (£17,900), Keep Wales Tidy (£10,000), Mike Paines Bursary Memorial (£2,278), Ty Hafan (£1,500) and Business in the Community (£1,000).

No donations are made to political parties. Further, no payments or donations in kind have been made which are required to be disclosed under the Political Parties, Elections and Referendums Act 2000.

Directors' report

Welsh Language Scheme

We operate an approved Welsh Language Scheme under the provisions of the Wales Language Act 1993. We welcome dealing with customers and other stakeholders in Welsh or English and aim to provide an equally effective standard of service in both languages.

Regulatory accounts (Welsh Water)

Condition F of the Instrument of Appointment under which Welsh Water operates requires that Welsh Water publish additional financial information as an 'appointed business'. A copy of this information will be published on our website www.dwrcymru.com or will otherwise be available on request from the Company Secretary after 31 July 2007.

Going concern

The Directors are satisfied that the Group has adequate resources to continue in business for the foreseeable future. Accordingly, the financial statements for the year ended 31 March 2007 have been prepared on a going concern basis.

Auditors

PricewaterhouseCoopers LLP acted as auditors to Glas Cymru for the accounts for the year ended 31 March 2007. As part of the audit process, Directors have confirmed that as far as each Director is aware (a) there is no relevant audit information of which the Company's auditors are unaware, and (b) they have taken steps to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

PricewaterhouseCoopers LLP have expressed their willingness to continue as auditors and a resolution for their reappointment will be considered at the 2007 AGM.

Subsequent events

In April 2007, Dŵr Cymru (Financing) Limited took advantage of market conditions to terminate £433 million of surplus floating to fixed interest swaps at a cost of £32.5 million. Further information is provided in Note 27 to the Accounts.

HM Government have proposed to amend the rate of corporate tax from 30% to 28% with effect from 1 April 2008 in the Finance Bill 2007. It has also announced prospective changes to the capital allowances regime from 1 April 2008, to be included in next year's Finance Bill. The impact of these changes, and in particular the effect on the Group's deferred tax liability, will be reflected in the financial statements when these proposals become law.

Annual general meeting

The notice convening the 2007 AGM to be held on Friday 6 July 2007 is set out in a document sent to the Members of Glas Cymru with this report.

The business of the 2007 AGM includes the approval of the Directors' Report and Financial Statements and the Remuneration Report for the year ended 31 March 2007, the election or re-election of five Directors, a resolution to comply with the Political Parties, Elections and Referendums Act 2000 and a resolution to reappoint the auditors. These resolutions are matters of ordinary business for the 2007 AGM. There is no special business.

By order of the Board



Richard Curtis LLB, ACIS
Company Secretary
8 June 2007

Remuneration report 2006-07

Compliance

This report has been prepared in accordance with Schedule 7A of the Companies Act 1985 as introduced by the Directors' Remuneration Report Regulations 2002 (the 'Regulations'). The report has been approved by the Board and will be put to Members for approval at the 2007 Annual General Meeting (2007 AGM)

In accordance with the Regulations, the Directors' emoluments table, long-term performance related bonus table and pension table on pages 40 and 42 have been audited, the remainder of the report has been reviewed for consistency by PricewaterhouseCoopers LLP, but is not subject to audit under the Regulations

Remuneration Committee

The Remuneration Committee (the 'Committee') is chaired by Alison Carnwath and comprises all the Non Executive Directors. The Chairman of the Board, along with the Managing Director, attends meetings of the Committee by invitation, as appropriate. The Committee met on four occasions in 2006-07.

The role of the Committee is to approve, implement and keep under review the remuneration policy and practice and specifically

- to agree with the Board the policy and framework for the remuneration of the Chairman, Non Executive Directors and Executive Directors and senior managers
- to agree the terms of service contracts and remuneration for Executive Directors and senior managers
- to determine incentive arrangements that encourage enhanced performance and reward individuals in a fair and responsible manner for their contribution to the success of the Company

A copy of the full terms of reference of the Committee is available on the Company's website or on request from the Company Secretary

The Company Secretary and Head of Human Resources attend all meetings of the Committee and provide information and advice as necessary. In addition, the Committee has sought independent external advice on certain aspects of remuneration policy and best practice. In 2006-07, advisors to the Committee were

- New Bridge Street Consultants LLP ('New Bridge Street'), who advise on market best practice in the design of incentive performance arrangements, the benchmarking of Directors' remuneration and fees and senior management service contracts and remuneration and in relation to pension matters
- Linklaters & Alliance, who provide legal advice to the Committee on Directors' service contracts and pension matters

In the view of the Committee, there were no conflicts of interest in relation to these organisations advising both the Company and the Committee

Remuneration Policy

The aim of the remuneration policy is to ensure that, in a competitive market place, the business is well managed by high calibre executives who are incentivised to produce sector-leading performance for the benefit of Welsh Water's customers, investors and other key stakeholders. The policy is designed to align as closely as practicable the interests of the individual with the longer-term interests of the business, and, especially, the interests of the customers of Welsh Water. Accordingly, a high proportion of Directors' remuneration is dependent on performance.

The executive remuneration package comprises four elements: base salary and benefits, annual performance related bonus, a longer-term performance related incentive and pension.

The remuneration policy applies to the senior management team, as well as to Executive Directors, and has been founded on the following principles:

- overall, remuneration packages shall be broadly competitive when compared to the relevant market,
- the 'at-risk' performance related component of Directors' remuneration, which is non-pensionable, shall be above that typical in comparator companies for the achievement of stretching performance targets,
- customer service and financial performance are the key criteria by which the success of the business is judged and shall therefore be key determinants of performance related pay,

Remuneration report 2006-07

- only by an appropriate combination of annual and longer term incentivisation arrangements can the Committee ensure that individuals are motivated and that their interests are suitably aligned with the longer term objectives of Glas Cymru and the customers of Welsh Water, and
- the Remuneration Policy shall reflect the stated intention of the Board that Welsh Water should be one of the consistently best performing water companies in the sector, and that to earn bonuses Directors must outperform the level of customer service and financial performance expected by Welsh Water's regulators

For 2006-07 the comparator companies comprised the water companies (AWG, Kelda plc, Pennon plc, Severn Trent plc and United Utilities plc), together with National Grid plc and Scottish Power plc. The appropriateness of the comparator group is reviewed on an annual basis.

Bonus Policy Annual Performance Related Bonus

The maximum annual cash bonus payable is 80 percentage points of base salary ('PPBS'), with 50 PPBS (62.5% of the maximum) being payable for reaching 'target' level of performance. Maximum bonus is divided equally between customer service and financial performance components.

The customer service component is determined with reference to the 'Overall Performance Assessment' ('OPA') published by Ofwat, and can earn up to 40 PPBS for achieving 1st position in the OPA ranking of the ten water and sewerage companies of England and Wales ('OPA League Table'). 8 PPBS (20% of the maximum) will be payable for achieving median performance, being the average score of the 5th and 6th ranked companies, with ranking above this (but not below) rewarded on a linear scale.

The OPA includes non-financial performance measures for

- water supply e.g. interruptions to supply, restrictions on supply and drinking water compliance,
- sewerage measures e.g. sewage flooding incidents and quality of effluent discharges to the environment, and
- customer service performance e.g. speed of response to telephone and written billing enquiries and handling of written complaints

At the discretion of the Committee, this bonus entitlement may be adjusted upward or downward by up to 10 PPBS to reflect identifiable and significant aspects of customer service performance not captured by OPA.

The financial component is based on net cash flow (before capital expenditure but after net interest payable) and can earn up to 40 PPBS. Performance will be rewarded on a linear scale from zero for meeting the annual cash flows in the regulatory settlement for 2005-10 announced by Ofwat in December 2004 (the 'Final Determination'), 25 PPBS (62.5% of maximum) and 40 PPBS for reaching the respective target and maximum levels approved by the Committee. To achieve target level bonus accordingly requires that Welsh Water outperform the Final Determination, which is a key requirement if the business is to achieve the challenging objectives set by the Board.

The 2006-07 Accounts include a charge of £301,298 (equivalent to 43.5 basis points) reflecting the Committee's current estimate of Welsh Water's relative performance for the year ended 31 March 2007. The Committee will make its final assessment of bonus payable for 2006-07 in the Autumn 2007, following publication by Ofwat of its Levels of Service Report.

Bonus Policy Rolling Long Term Incentive Scheme ('RLTIS')

The RLTIS is a longer-term incentive scheme introduced on 1 April 2005 on the basis of a rolling three-year period (except during the first two years). The maximum bonus payable under RLTIS will be 60 PPBS, with 30 PPBS (50% of the maximum) being payable for reaching 'target' performance. Maximum bonus is divided equally between customer service and financial performance components.

Payments under RLTIS will normally be made within six months of the end of the final year to which they relate, but payment may be deferred at the discretion of the Committee in the event that there is a significant deterioration in performance. Deferral may be for up to two years, or until the shortfall has been remedied, whichever is the earlier.

In addition, payment of up to 20 PPBS will be deferred in the event that any of the Company's bonds have been put on credit watch by any of the Rating Agencies, either until taken off credit watch or until they have been downgraded, in which case the 20 PPBS shall be forfeited

The customer service component will be determined with reference to Welsh Water's position in an adjusted OPA League Table, compiled by aggregating OPA scores for each of the last three years up to and including the relevant year of assessment. Bonus will be payable on a sliding scale of 100% (30 PPBS) for achieving 1st position, 75% for 2nd, 50% for 3rd, 25% for 4th and zero for being ranked 5th or below of the ten comparator companies

The financial performance component will be based on 'Financial Reserves' (Regulatory Capital Value less net debt) at the end of the relevant year, as defined for the purposes of the quarterly Investor Report routinely published by the Company. Growth in Financial Reserves is considered the best financial measure of customers' interest in the business, as it is from Financial Reserves that the 'customer dividend' and additional investment to deliver service improvements will be funded. Growth in Financial Reserves therefore captures the dynamics on which the objectives of Glas Cymru were founded and aligns the financial interests of Executive Directors in a direct and simple way with those of customers

The Committee will normally confirm target ranges three years in advance. However, these ranges will be subject to revision by the Committee each year in certain circumstances. These include (a) where there are differences between actual inflation and the assumptions originally made, (b) where the Board changes the 'customer dividend' after the original forecast was made, and (c) where there is any other material influence on Financial Reserves not originally foreseen and which the Committee determines to be outside the control of Executive Directors. Payment of bonus will be measured by reference to a lower limit, the Final Determination, at which no bonus will be earned, a target level at which 50% of maximum will be earned and an upper limit, set by the Committee, at which maximum bonus will be earned. Again, to achieve target level bonus accordingly requires that Welsh Water outperform the Final Determination

The Committee may at its discretion adjust any bonus calculation, up or down, to reflect events or factors that are not captured by the bonus formulae described above, providing that justification for any such adjustment will be disclosed in the next annual report

The 2006-07 Accounts include an accrual of £206,644 (equivalent to 39.1 basis points) reflecting the Committee's current estimate of Welsh Water's relative performance for the three year period ended 31 March 2007. The Committee will make its final assessment of bonus payable under the RLTIS for 2006-07 in the Autumn 2007 following publication by Ofwat of its Levels of Service Report

Remuneration Chairman and Non Executive Directors

Responsibility for determining the fees of the Chairman of the Board and of the Non Executive Directors sits with the Committee and with the Board respectively. These fees are reviewed annually and were last revised with effect 1 April 2007, when they were increased to

Chairman	£180,000 (2006 £172,000)
Non Executive Directors	£50,000 (2006 £48,000)

No additional amount is payable to the Chairman or any Non Executive Director for the chairmanship of, or membership of, Board Committees or for the undertaking of any special responsibilities on behalf of the Board (further details of which can be found in the Corporate Governance Statement on page 44). Fees are reviewed annually

The Chairman and the Non Executive Directors are appointed under letters of appointment, terminable by either party on three months written notice

Remuneration report 2006-07

Remuneration Executive Directors

Salary

At 1 April 2007 the base salaries of the Executive Directors were as below

Nigel Annett (Managing Director)	£240,000 (2006 £231,000)
Chris Jones (Finance Director)	£185,400 (2006 £178,500)
Peter Perry (Operations Director)	£185,400 (2006 £178,500) <i>Appointed 1 August 2006</i>

The Committee reviews base salary on an annual basis using competitive market data provided by New Bridge Street

Bonus

Annual performance related bonus

In Autumn 2006 Executive Directors received an annual incentive bonus for the year ended 31 March 2006 equivalent to 68.9% of salary, of which 28.9% related to performance against customer service targets and 40% to meeting financial targets. This compared to an accrual in the 2005-06 Accounts of 49.9%.

Rolling Long Term Incentive Scheme

In Autumn 2006 Executive Directors received a first payment under the RLTI in respect of the period ended 31 March 2006 equivalent to 59.1% of salary, of which 30% related to performance against customer service targets and 29.1% to meeting financial targets. This compared to an accrual in the 2005-06 Accounts of 44.1%.

Pensions

It is Company policy to make provision for pensions for Executive Directors. Welsh Water has a Defined Benefit pension scheme and a Defined Contribution pension scheme. All Executive Directors are members of the Defined Benefit Scheme.

	Accrued Pensions (per annum) at 31 March 2007	Increase in accrued pension in the year	Transfer value at 31 March 06	Transfer value equivalent of increase in accrued pension	Transfer value at 31 March 07	Contributions paid by Director	Contributions paid by company
NC Annett*	£72,785	£21,463	£421,890	£210,332	£747,623	£13,860	£50,127
CA Jones*	£47,870	£9,150	£243,621	£73,250	£319,355	£10,710	£38,735
PD Perry**	£6,640	£6,640	-	£58,519	£58,519	£7,140	£25,823

* Accrued pension includes previous service in Hyder Water Pension Scheme

** Peter Perry joined the Company on 1 August 2006

Jim O'Sullivan was a member of the defined contributions scheme for which there are no accrued liabilities. Company contributions to the scheme until the date of his resignation totalled £8,594 (2006 £23,702)

Prior to the introduction of the new pension tax regime on 6 April 2006, executive pension entitlement in the Scheme were restricted by the Inland Revenue Earnings Cap with the balance of their entitlement being provided by the Company through an un-funded arrangement. The Company has chosen to remove the application of the Earnings Cap meaning that all executive benefits can now be provided through the Scheme. In the case of NC Annett, this is being phased in on an annual basis until such time that the whole of his target pension can be provided through the Scheme.

The Company has made a provision for liabilities arising from contractual commitments to Executive Directors over the previous Inland Revenue 'earnings cap'. As at 31 March 2007 this liability totalled £105,000 (2006 £220,000).

The normal retirement age for Directors under the Welsh Water Pension Scheme is 60 and, for the Defined Benefit scheme, benefits accrue at 1/45th of salary per year of pensionable service, subject to a maximum overall pension at normal retirement age of two-thirds of final pensionable salary. Both the Defined Benefit and the Defined Contribution schemes also provide life cover of four times pensionable pay for death in service, a pension payable in the event of ill health and a spouse's pension payable on death. Executive Directors also participate in a private health and medical insurance scheme.

Directors' emoluments (Excluding pension benefits and long term performance related bonus)

The table below reports emoluments receivable in respect of the year ended 31 March 2007, and includes a best estimate of the performance related annual bonus relating to customer service performance for 2006-07. The annual performance related bonus is ordinarily paid in October, following publication by Ofwat of its Levels of Service Report, which sets out the comparative performance of the ten water and sewerage companies of England and Wales and the OPA data for the financial year in question. The extent to which this element of the bonus has been over or under estimated will be disclosed in the Remuneration Report for next year.

The Committee believes the presentation adopted below to be the most meaningful, as it allows a direct comparison of Directors' remuneration year on year. The information required to comply with the Companies Act is provided in full and is disclosed in the table and in the supplementary notes.

The following emoluments were earned by the Directors in respect of the financial year ended 31 March 2007

2006-07	Lord Burns	NC Annett	CA Jones	J O'Sullivan	P Perry	JM Bryant	A Carnwath	GT Davies	DJ Hine	AJ Hobson	Total
Salary	-	£231,000	£178,000	£89,250	£119,000						£617,750
Bonus 2006-07 Provision											
Annual bonus ³	-	£100,485	£77,648	£71,400	£51,765						£301,298
Benefits in kind ⁴	-	£878	£669	£323							£1,870
Compensation for loss of office ⁴				£178,500							£178,500
Fees	£172,000					£48,000	£48,000	£48,000	£48,000	£48,000	£412,000
Total emoluments relating to 2006-07	£172,000	£332,363	£256,817	£339,473	£170,765	£48,000	£48,000	£48,000	£48,000	£48,000	£1,511,418

The following emoluments were earned by the Directors in respect of the financial year ended 31 March 2006

2005-06	Lord Burns	NC Annett	CA Jones	J O'Sullivan	P Perry	JM Bryant	A Carnwath	GT Davies	DJ Hine	AJ Hobson	Total
Salary		£220,000	£170,000	£94,808	-	-	-	-	-	-	£484,808
Bonus 2005-06 Provision											
Annual bonus provided in the accounts ⁵	-	£109,741	£84,800	£47,292	-	-	-	-	-	-	£241,833
2005-06 bonus adjustment	-	£41,839	£32,330	-							£74,169
Total bonus ⁶	-	£151,580	£117,130	£47,292							£316,002
Benefits in kind ⁴	-	£1,931	£1,451	£708							£4,090
Fees	£164,000	-				£45,000	£45,000	£45,000	£45,000	£45,000	£389,000
Total emoluments relating to 2005-06	£164,000	£373,511	£288,581	£142,808		£45,000	£45,000	£45,000	£45,000	£45,000	£1,193,900

Notes

- 1 J O'Sullivan resigned as a Director on 31 July 2006
- 2 P Perry was appointed a Director on 1 August 2006
- 3 The financial statements for the year ended 31 March 2007 include a provision of £301,298 (43.5% of base salary) for annual cash bonus potentially payable to Executive Directors for performance in the financial year 2006-07. This provision has been estimated on the basis that performance in Ofwat's Overall Performance Assessment for 2006-07 will be 5th. The final amount to be paid to each Director will be determined when Ofwat publishes OPA results for 2006-07 in the Autumn of 2007, and could be higher or lower.
- 4 Benefits in kind relate to receipt of private medical insurance, all health cover and life insurance.
- 5 A performance bonus of £241,833 was provided for in the Report and Accounts for 2005-06 and was estimated on the basis that OPA performance on 2005-06 would be 5th.
- 6 The actual performance bonus in respect of 2005-06 totalled £316,002 (68.9% of salary) and was paid in October 2006, following publication of Ofwat's OPA report for 2005-06 which confirmed Welsh Water's position as 3rd.
- 7 The highest paid Director in 2006-07 was NC Annett who received emoluments of £332,363 (2006: NC Annett £373,511).
- 8 The compensation for loss of office equates to one year's salary and, in accordance with the Companies Act 1985, is not included in the calculation of emoluments for the highest paid Director.
- 9 Details of payments under the Rolling Long Term Incentive Scheme are disclosed on page 42 of the 2007 Remuneration Report.

Remuneration report 2006-07

Directors' Earnings Rolling Long Term Incentive Scheme

In addition to the emoluments disclosed in the table on page 41, provision is made in the 2006-07 Accounts for the second payment under the three year rolling long term incentive scheme (RLTIS) which is payable in October 2007

The provision of £206,644 equates to 39.1% of salary, and has been estimated on the basis that the performance in Ofwat's Overall Performance Assessment for the three year period 2004-05 to 2006-07 will be 3rd, as follows

NC Annett	£90,321
CA Jones	£69,794
PD Perry	£46,529

The final amount to be paid to each Director will be determined when Ofwat publishes its OPA results for 2006-07 in Autumn 2007, and could be higher or lower than the provision made

The 'Levels of Service Report' published by Ofwat for the year ended 31 March 2006 ranked Welsh Water third in OPA performance of the ten water and sewerage companies. Following publication of this report, in November 2006 payments were made to executive Directors totalling £272,309 (equivalent to 59.1 basis points) NC Annett £130,020, CA Jones, £100,470 and J O'Sullivan £41,819. Welsh Water's relative performance in 2005-06 exceeded the assumptions made in the 2005-06 Accounts, which provided an accrual for bonus of £213,844 (equivalent to 44.1 basis points)

Directors' Earnings: Long Term Bonus Entitlement (2001-2005)

In Autumn 2005, Executive Directors in post at 31 March 2005 received a payment under the long-term bonus scheme that applied for the period 2001 to 2005. Under this scheme half of award earned at the end of the four-year period was paid in Autumn 2005, with the remaining half deferred for two years, with no further performance conditions. Payment of the deferred award of £111,405 is payable to each of NC Annett and CA Jones in Autumn 2007.

Service contracts

The Executive Directors have service contracts that are subject to one year's notice. Directors' service contracts do not provide for compensation to be payable in the event of early termination by the Company. At the Company's discretion, an Executive Director may be paid base salary alone in lieu of notice. As such, a significant element of mitigation is built into the Executive Directors contracts should the Company choose to exercise its option to make a payment in lieu of notice.

External appointments

The Board recognises the benefit of broadened experience that might be achieved through the involvement of Executive Directors in external activities. Any appointment is subject to annual approval by the Committee and, subject to the Committee's agreement, a Director may retain any fees. CA Jones is a Non Executive Director of the Principality Building Society, in respect of which he retains a fee of £26,000 per annum.

Recommendation

The Committee believes that the Remuneration Policy continues to provide the right balance of salary and incentives to reward and motivate Executive Directors to the attainment of the challenging goals the Board has set for the Company. Accordingly, the Committee encourages the Members of Glas Cymru to approve this 2007 Remuneration Report.



Alison Carnwath

Chairman Remuneration Committee

8 June 2007

Corporate governance

Glas Cymru is committed to high standards of corporate governance and this is critical to maintaining our credentials as a well-managed provider of an essential public service in the eyes of Welsh Water's customers and regulators, and Glas Cymru's bondholders and other stakeholders

This report explains the key features of the Company's governance structure and how it complies with the applicable Principles of Good Governance and Best Practice as annexed to the Listing Rules of the United Kingdom Listing Authority (the 'Combined Code adopted in 2003'), although not all of the provisions of the Combined Code apply to Glas Cymru as a Company limited by guarantee. The Company complies with all applicable provisions of the Combined Code, save in respect of the appointment of a Senior Independent Director which is referred to on page 49.

The Board

The Board comprises ten Directors: a Chairman, three executive Directors and six independent Non Executive Directors. The Company believes the Board has an appropriate mix of experience and expertise to oversee the Group's business and to maximise the effectiveness of the Board ensuring that matters are fully debated and that no individual or group dominates the Board's decision making process. The Company considers each of the Non Executive Directors to be independent.

The roles of the Chairman and Managing Director are separate and clearly defined. The Chairman is principally responsible for ensuring the effective operation of the Board and that the information it receives is sufficient to make informed judgements. The Managing Director is responsible for leading executive management in the day-to-day management of the business and for the implementation of the business plan, policies and procedures adopted by the Board.

The Non Executive Directors have access to all information relating to the Group, the advice and services of the Company Secretary, and, as required, independent external advice at the expense of the company. The Company Secretary is an employee, but not a Director, of the Company.

Biographical details of the current Directors can be found on page 32 to 33. With the exception of Jim O'Sullivan who resigned on 31 July 2006, Peter Perry who was appointed a Director on 1 August 2006 and James Strachan who was appointed a Director on 1 June 2007, all Directors held office throughout the financial year. Each of the Executive Directors has a written service contract subject to termination by the Company on twelve months notice. Each of the Non Executive Directors has a written letter of appointment subject to termination by the Board on three months notice. Details of Directors' remuneration and fees are provided in the 2007 Remuneration Report on pages 37 to 42.

Board proceedings

The Board meets regularly to set the strategic direction of the business and to review the operating, financial and risk performance of the business. There is a formal schedule of matters reserved to the Board, which is reviewed annually and which can only be amended by the Board. This includes approval of the annual business plan (which sets the operating and strategic objectives for the business, and the risk framework within which the business will operate), corporate policies, significant transactions above specified thresholds or outside the ordinary course of business and the delegation of Board authority to committees and Executive Directors.

Corporate governance

The Board and its committees meet on a regular basis. The table below summarises the number of meetings held in 2006-07 and the level of attendance at each.

	Board	Audit ^A	Remuneration ^B	QEC ^C	Nominations ^D
Number of meetings held in year	9	4	4	12	4
Number of meetings attended by					
Lord Burns ^(N)	9	-	-	-	4*
Nigel Annett	9	-	-	-	4
Chris Jones	9	-	-	-	-
Peter Perry ^(O)	6	-	-	8	-
John Bryant ^(R, Q, N)	9	-	4	12	4
Alison Carnwath ^(A, R, N)	9	4	4*	-	4
Geraint Talfan Davies ^(A, R, N)	9	4	4	-	4
Dame Deidre Hine ^(R, Q, N)	9	-	4	12*	4
Tony Hobson ^(A, R, N)	8	4*	3	-	4

Peter Perry was appointed a Director on 1 August 2006

James Strachan was appointed a Director on 1 June 2007

** Denotes committee Chairman*

Election and re-election of Directors

In accordance with the Company's articles of association, all Directors must stand for re-election at intervals of no more than three years, and any new Director must stand for election at the first annual general meeting following his or her appointment.

At the Annual General Meeting on 6 July 2007 ('2007 AGM') two Directors, Peter Perry and James Strachan will stand for election as a Director, this being the first AGM since their appointment. In addition, three Directors, Lord Burns, Nigel Annett and Chris Jones will retire by rotation and seek re-election at the 2007 AGM. The Board recommends the appointment of each of the five Directors seeking re-election.

Information, induction and development of Directors

It is the role of the Chairman, aided by the Company Secretary, to ensure that the Board, its committees and individual Directors receive timely and clear information in respect of the Company's strategy and performance to ensure meaningful debate and effective decision making. The Company Secretary also advises the Board on corporate governance.

The appointment of a new Director is the responsibility of the Board, having received advice and recommendation from the Nominations Committee. In line with Principle A5 of the Combined Code, new Directors receive an induction programme to familiarise them with the business, the risks and strategic challenges, and the economic, competitive, legal and regulatory environment in which it operates.

A programme also exists to ensure that all Directors have the opportunity to continually update their skills and business knowledge. This takes the form of occasional attendance on external courses, by the provision of information and presentations to the Board on key strategic issues and through visits to strategic operational assets.

Evaluation of the Board

There is an established process to evaluate the performance of the Board, the Chairman and the principal committees of the Board. This comprises questionnaires completed by all Directors, the conclusions of which are collated and analysed by the Company Secretary and collectively discussed at the Board. This is supplemented, as appropriate, by one to one discussions with each Director by the Chairman, following which actions are agreed to address issues raised. The most recent evaluation in March 2007 raised no material weaknesses or failings, but highlighted a number of minor aspects for consideration to further improve the effectiveness of the Board.

The Board also met, without the Chairman, specifically to review and evaluate the performance of the Chairman.

The Chairman assesses the performance of the Managing Director after taking into account the views of other Directors. The performance of Executive Directors and Company Secretary is assessed by the Managing Director, under a process of annual appraisal that applies to all employees.

Committees of the Board

There are four principal committees of the Board each of which has written terms of reference, which define the role and responsibilities of the committee and which are reviewed annually: the Nominations Committee, the Audit Committee, the Remuneration Committee, and the Quality and Environment Committee.

Membership of the various committees, which is intended to make best use of the skills and experience of Non Executive Directors in particular, is set out on page 44. Following each committee meeting a summary of matters discussed is reported to the Board, and the Board subsequently receives the minutes of all committee meetings. Each committee of the Board has authority to employ the services of such advisors, within and outside the Company, as it deems necessary to fulfil its responsibilities.

Details of the work of the Audit Committee, Quality and Environment Committee and Nominations Committee are set out below. Details of the work of the Remuneration Committee can be found in the 2007 Remuneration Report on page 37. In addition to contributing to the formal committees of the Board, certain Directors have been allocated 'special responsibilities' covering important areas such as procurement (John Bryant), communications (Geraint Talfan Davies) and government and regulation (Lord Burns). In April 2006, the Board also established a Finance Committee to approve finance transactions where a decision is required between formal meetings of the Board.

Nominations Committee

The Nominations Committee meets on an ad hoc basis. It is chaired by the Chairman of the Board and comprises the five Non Executive Directors and the Managing Director. Other Executive Directors attend meetings at the invitation of the Chairman.

The role of the Nominations Committee is to review the size, structure and composition of the Board and, in particular, to

- lead the process and, with the aid of external search and recruitment consultants, make recommendations to the Board on Executive or Non Executive Director appointments
- ensure that there is a rigorous and transparent process for the appointment of new Directors
- keep under review the composition of the Board through routine evaluation of the skills, knowledge and experience around the board table
- ensure that plans are in place for orderly succession for appointment to the Board and to other senior executive management positions

The Committee met on four occasions in 2006-07 with all members at the time present.

The Board has commenced a process of planning Board succession and Russell Reynolds & Associates has been engaged to advise the Committee and the Board on the recruitment of new Non Executive Directors. The Board faces an unusual challenge in that five of the current Non Executive Directors, who were appointed within a short time of each other in 2000-01, will have served as Directors for nine years by May 2010.

The Committee and the Board have agreed in principle that it would be in the best interests of the company (and of the customers of Welsh Water) to, in due course, consider extending the term of office of some of the Non Executive Directors beyond nine years. This would facilitate some continuity on the Board between the AMP4 (2005-10) and AMP5 (2010-15) regulatory investment periods, and around the first review in 2010 of contract pricing under Welsh Water's outsourced procurement arrangements. This would also significantly reduce the risk otherwise associated with completing a Board refresh over a relatively short three-year period.

Corporate governance

Audit Committee

The members of the Audit Committee are independent Non Executive Directors Tony Hobson (Chairman), Alison Carnwath, Geraint Talfan Davies and James Strachan. By invitation of the Chairman, meetings of the committee are attended by the Finance Director, Head of Business Assurance and Internal Audit and selected other senior managers. The Company Secretary acts as secretary to the Committee.

The Board considers that Tony Hobson, a chartered accountant and until 2001 Group Finance Director of Legal & General Group plc, has the significant, recent and relevant financial experience required to chair the Audit Committee.

The role of the Committee is to receive and challenge reports from executive management and, as appropriate, from the Group's internal and external auditors, and in particular to

- review and advise the Board on the Group's interim and annual financial statements, its accounting policies and on the control of its financial and business risks
- review the nature and scope of the work to be performed by the external auditors and outsourced internal audit function, the results of their audit work and of the response of management
- review and advise the Board on the effectiveness of the Group's internal control environment, including the 'Whistleblowing' procedures
- make recommendations on the appointment and remuneration of external auditors and to monitor their performance
- approve and monitor the policy for non-audit services provided to the Group by the external auditors to ensure that the independence of the auditors is not compromised

During 2006-07, the Audit Committee met on four occasions, with all members present. The Committee reviewed the draft annual and interim reports and associated preliminary and interim results announcements, focusing on key areas of judgement and significant accounting policies. Time is allocated at two meetings a year to review the findings of the risk management process, including a review of mitigation plans for significant business risks. Significant reports and issues arising from the risk based audit programme are discussed at every meeting.

Relationships with the external auditor and outsourced internal audit service provider are managed through the Managing Director and Finance Director. During the year, the Audit Committee approved external and internal audit plans, and met privately with the internal and external auditors without executives present as part of its annual review of audit independence. The Audit Committee also met with Executive Directors and management. On the basis of this work, the Audit Committee is able to assess the ongoing effectiveness of internal and external audit.

The role of internal audit is to advise management and the Board on the extent to which systems of internal control are effective and to provide independent and objective assurance that the processes by which significant risks are identified, assessed and managed are appropriate and effectively applied. The internal audit work-plan (which covers the scope, authority and resources of such activity) is determined through a structured process of risk assessment and is approved by the Audit Committee.

In 2006-07 PricewaterhouseCoopers LLP was re-appointed as external auditor following a process of competitive tendering of external audit services. During the year, the conduct, but not the management, of internal audit activity was outsourced to Grant Thornton, which gives access to a wider range of experienced auditors. The Audit Committee has reviewed the policies of the external auditors to ensure their independence and that of their engagement partner and that stated policy on non-audit fees has been met. This provides that the external auditor will not be used for internal audit services, and all non-audit work above a threshold of £25,000 will be subject to prior competitive tendering and approval by the Audit Committee. Total auditor remuneration is analysed between audit and non-audit work in Note 4 to the Accounts on page 63.

The terms of reference of the Audit Committee include all matters required by the Combined Code and the Committee reviews its own effectiveness through a process of annual self-assessment. The Committee has unrestricted access to Company documents and staff and to external auditors and the Finance Director and Head of Business Assurance and external auditors each have a right of direct access to the Chairman of the Audit Committee in respect of matters they wish to bring to his attention.

Quality and Environment Committee (QEC)

QEC meets each month and comprises two Non Executive Director members (Dame Deidre Hine, Chair, and John Bryant) and two Executive members (Peter Perry and Tim Masters, Head of Operational Performance), advised by two independent experts on the public health and operational aspects of water supply and environmental management. By invitation of the Chair, meetings of the Committee are attended by Director level representation from Welsh Water's principal operating partners, United Utilities Operating Services and Kelda Water Services Wales. The Company Secretary acts as secretary to the Committee.

The role of QEC is to

- Advise the Board on matters of operational policy and practice, and to routinely review the performance of Welsh Water and its contract partners against key performance indicators, in relation to matters of public health, compliance with drinking water regulations and environmental laws and regulations and occupational health and safety
- Review the development of key operational strategies, as Welsh Water aims to develop more sustainable water and wastewater businesses based on industry best practice and knowledge
- Assess Welsh Water's management of and response to significant water quality or environmental incidents, or any weakness identified under the internal audit quality programme of work

QEC produces an annual report to the Board, which is a published document. This report is issued to the Drinking Water Inspectorate and Environment Agency (the 'Quality Regulators'), and the Board is required to notify the Quality Regulators at once if it does not implement any recommendation made by QEC. The activities of QEC are also subject to review by Welsh Water's Reporter (the independent consultant appointed by Welsh Water with the approval of Ofwat) who will report to Ofwat and the Quality Regulators on the effectiveness of Welsh Water's system of planning and internal control. Copies of the 2007 QEC Report may be obtained on request from the Company Secretary or from our website www.dwrcymru.com

Internal control and risk management

The Board is responsible for the Group's system of internal control and for monitoring its effectiveness. An essential part of internal control is the establishment of processes designed to identify, evaluate and manage the significant risks faced by the Group (for further information see page 28, Principal Risks). However, there are limitations in any control process and even the most effective system can only provide reasonable, and not absolute, assurance against material misstatement or loss. In assessing what constitutes reasonable assurance, the Board has regard to materiality and to the relationship between the cost of, and the benefit from, internal control systems.

Key features of the system of internal control and risk management are

- systems that provide clear accountability for risk management and provide assurance to successive levels of management and to the Board, including regular reporting of performance for all significant aspects of the Group's business
- controls that recognise that the nature and balance of risk changes and evolves continuously and provide a framework within which controls, standards and policies are progressively developed
- key risks and hazards are identified, measured and managed to achieve an acceptable balance between risk and reward in delivery of the annual business plan, through which the Board approves the parameters of acceptable risk for the business
- assurance is provided by external independent audit and assessment of internal quality management systems. All audit activity is conducted under broad risk based programme approved by the Audit Committee, which is designed to ensure that management information is accurate, timely and relevant and reflects the true position of the business.

Corporate governance

- procedures exist to monitor policies for the approval and control of major items of capital expenditure, the acquisition and disposal of material assets, or the entering into of any arrangement that gives rise to, or could give rise to, a material liability
- managing risk is a responsibility for all managers in the business. For each major type of risk, there is a designated individual or team to ensure that appropriate guidance is available for managers across the business

Executive management review the effectiveness of risk management controls on a continuing basis through a Risk Management Group, chaired by the Managing Director. This group reviews and challenges the robustness of risk management procedures, including that of Welsh Water's contracting partners, and includes areas such as public health, environment, business ethics, employment, occupational health and safety and business continuity. The Risk Management Group also monitors procedures that encourage all staff to participate in open two-way dialogue to ensure that risk is understood and managed early and effectively, and to learn from our own experience and the experience of others to promote best practice. The Audit and Quality and Environment Committees of the Board receive an update on the Group's Risk Register and process of risk management at least every six months.

In judging the effectiveness of the Group's systems of internal controls, the Board considers periodic reporting from the Risk Management Group, the Audit Committee and the Quality and Environment Committee, in addition to its routine monitoring of key performance indicators and monthly reports of financial and operational performance, which flag variances against business plan and budget. By so doing, the Board reviews the effectiveness of the internal control system over the course of the year.

Members

A key role of the Members of Glas Cymru is to ensure that the business remains focused on its primary purpose of providing efficient high quality water and sewerage services to the communities served by Welsh Water. In doing this, Members carry out an important corporate governance role - and for this reason membership is personal. Members are not appointed to represent any particular group or stakeholder interest.

Members are appointed by the Board, but only individuals recommended by an independent membership selection panel (the 'panel') can be considered for appointment. The role of the panel is to recommend individuals who in a written application have shown they have the skills, experience and interests to be an effective Member. In addition the panel is required to ensure that overall a balanced and diverse membership is maintained, which is as far as possible broadly reflective of the range of customer and other stakeholder interests served by Welsh Water. The Chairman of the panel has confirmed to the Board compliance by Glas Cymru with the terms of its published Membership Policy.

At the date of this report, Glas Cymru has 53 Members, excluding the Directors of the Company but including 3 Members appointed during 2006-07 and 2 Members appointed subsequent to the financial year-end. Also subsequent to the financial year-end, and following evaluation and recommendation by the panel, 13 of the 14 Members whose term of office will expire at the end of the 2007 AGM, have applied for and have been reappointed for a further three-year term ending at the end of the AGM in 2010. As a result on 6 July 2007 the number of Members (excluding the Directors) will reduce to 52. Further details of the Membership Policy and the Members of Glas Cymru can be obtained from the Company Secretary or from our website www.dwrcymru.com

Communication with Members and key stakeholders

The Board attaches high importance to maintaining good relationships with Members and all key stakeholders. Members of Glas Cymru have regular opportunity to meet with Directors and all Members attended at least one of the two Members' Meetings in the year at which all Directors, including the chairmen of the key Board committees, were available to answer questions. All Members, including those unable to attend any meeting, receive a written brief of issues discussed.

In addition to an annual bondholder/investor meeting, there are informal meetings with bondholders and other investors, who may request a meeting with an independent Non Executive Director at any time. The Board receives a report following meetings with investors following the announcement of interim and preliminary results for any period. Regular communication is also maintained with each of the economic, quality and customer service regulators of Welsh Water. As a result of the above, the Board has concluded that the nomination of a Senior Independent Director would not improve governance and has not appointed one.

By order of the Board



Richard Curtis LLB, ACIS
Company Secretary
8 June 2007

Directors' responsibility

The Directors are responsible for preparing the Annual Report and the Group and parent Company financial statements in accordance with applicable law and regulations

Company law requires the Directors to prepare Group and parent Company financial statements for each financial year. They are required to prepare the Group financial statements in accordance with International Financial Reporting Standards ('IFRS') as adopted by the EU and have elected to prepare the parent Company financial statements on the same basis.

The Group and parent Company financial statements are required by law and IFRS as adopted by the EU to present fairly the financial position of the Group and the parent Company and of the performance for that period, the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

In preparing each of the Group and parent Company financial statements, the Directors are required to

- select suitable accounting policies and then apply them consistently
- make judgments and estimates that are reasonable and prudent
- state whether they have been prepared in accordance with IFRS as adopted by the EU
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the parent Company will continue in business

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the parent Company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Directors' Report, a Directors' Remuneration Report and the Corporate Governance Statement that comply with that law and those regulations.

The Company is responsible for the maintenance and integrity of the corporate and financial information included on our Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By order of the Board



Richard Curtis LLB, ACIS
Company Secretary
8 June 2007

Independent auditors' report to the members of Glas Cymru Cyfyngedig

We have audited the Group and parent company financial statements (the 'financial statements') of Glas Cymru Cyfyngedig for the year ended 31 March 2007 which comprise the Consolidated Income Statement, the Statement of Changes in Reserves, the Consolidated and parent company Balance Sheets, the Consolidated Cash Flow Statement and the related notes

These financial statements have been prepared under the accounting policies set out therein. We have also audited, at the request of the Directors, the information in the Directors' Remuneration Report that is described as having been audited.

Respective responsibilities of Directors and auditors

The Directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities. The Directors are also responsible for preparing the Directors' Remuneration Report (because the Company applies the requirements of Schedule 7A to the Companies Act 1985 as if it were a listed company).

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). We also, at the request of the Directors, audit the part of the Directors' Remuneration Report to be audited (because the Company applies the requirements of Schedule 7A to the Companies Act 1985 as if it were a listed company). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements. The information given in the Directors' Report includes that specific information presented in the Operating and Financial Review that is cross referred from the Business Review section of the Directors' Report. We also report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises only the Directors' Report, the unaudited part of the Directors' Remuneration Report, the Chairman's Statement, the Operating and Financial Review and the Corporate Governance Statement. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

We also, at the request of the Directors (because the company applies the Financial Services Authority listing rules as if it were a listed company), review whether the corporate governance statement reflects the company's compliance with the nine provisions of the 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the company's corporate governance procedures or its risk and control procedures.

Independent auditors' report to the members of Glas Cymru Cyfyngedig

Basis of audit opinion

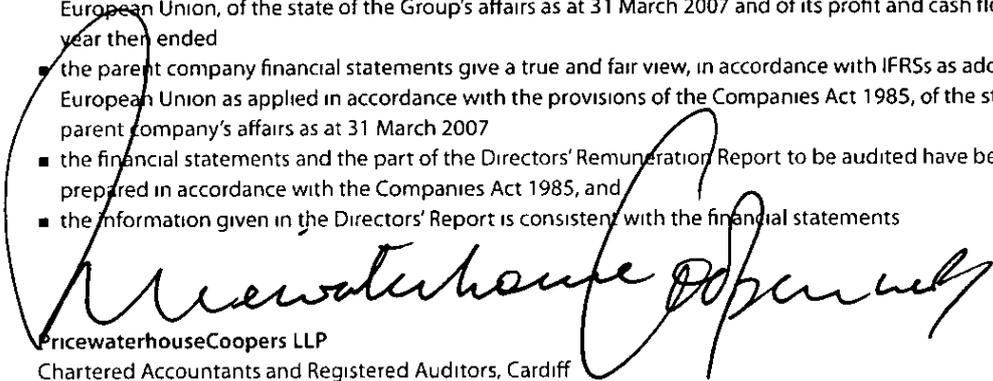
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Directors' Remuneration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

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

Opinion

In our opinion

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 31 March 2007 and of its profit and cash flows for the year then ended
- the parent company financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union as applied in accordance with the provisions of the Companies Act 1985, of the state of the parent company's affairs as at 31 March 2007
- the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985, and
- the information given in the Directors' Report is consistent with the financial statements



PricewaterhouseCoopers LLP

Chartered Accountants and Registered Auditors, Cardiff
13 June 2007

Primary statements

Consolidated income statement for the year ended 31 March 2007

	Note	2007 £m	2006 £m
Revenue		578 0	553 5
Operating costs			
- Operational expenditure	4	(228 6)	(213 2)
- Infrastructure renewals expenditure	4	(84 1)	(48 8)
- Depreciation and amortisation	4	(111 8)	(97 5)
- Profit on disposal of fixed assets	4	-	0 8
Operating profit		153 5	194 8
Financing costs			
- Interest payable and similar charges	3a	(159 1)	(156 9)
- Interest receivable	3a	7 4	6 7
- Fair value gains/(losses) on financial instruments	3b	45 7	(33 3)
		(106 0)	(183 5)
Profit before taxation	4	47 5	11 3
Taxation (charge)/credit	5	(14 2)	4 8
Profit for the year		33 3	16 1

Statement of changes in reserves for the year ended 31 March 2007

	2007 £m	2006 £m
Reserves at 1 April	(79 2)	(95 3)
Profit for the year	33 3	16 1
Reserves at 31 March	(45 9)	(79 2)

The Group has no other recognised gains or losses in the year (2006 nil) and accordingly a statement of recognised income and expense has not been presented. There are no changes in reserves of the parent company during the year.

Primary statements

Consolidated balance sheet as at 31 March 2007

	Note	2007 £m	2006 £m
Assets			
Non-current assets			
Intangible assets	6	7 0	4 4
Property, plant & equipment	7	2,846 9	2,795 6
Investments	8a	-	-
Financial assets			
- derivative financial instruments	14	14 7	6 3
		2,868 6	2,806 3
Current assets			
Trade and other receivables	9	90 4	86 7
Financial assets			
- held to maturity investments	10	-	0 3
- derivative financial instruments	14	4 2	4 2
Cash and cash equivalents	11	158 0	14 0
		252 6	105 2
Liabilities			
Current liabilities			
Financial liabilities			
- borrowings	13	(65 8)	(124 6)
- derivative financial instruments	14	(38 8)	(6 2)
Trade and other payables	12	(101 5)	(118 5)
		(206 1)	(249 3)
Net current assets/(liabilities)		46 5	(144 1)
Non-current liabilities			
Financial liabilities			
- borrowings	13	(2,520 0)	(2,244 9)
- derivative financial instruments	14	(36 0)	(105 9)
Trade and other payables	12	(2 5)	-
Retirement benefit obligations	21	(5 5)	(6 6)
Provisions	16	(8 6)	(9 8)
		(2,572 6)	(2,367 2)
Net assets before deferred tax		342 5	295 0
Deferred tax	17	(388 4)	(374 2)
Net liabilities		(45 9)	(79 2)
Reserves			
Retained earnings		(45 9)	(79 2)
Total reserves		(45 9)	(79 2)

These financial statements were approved by the Board of Directors on 8 June 2007 and were signed on its behalf by



N C Annett
Managing Director

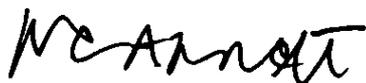


C A Jones
Finance Director

Parent company balance sheet as at 31 March 2007

	Note	2007 £m	2006 £m
Assets			
Non-current assets			
Investment in subsidiaries	8b	-	-
Current assets			
Trade and other receivables	9b	3.4	3.4
Cash and cash equivalents	11	0.1	0.1
		3.5	3.5
Liabilities			
Current liabilities			
Trade and other payables	12	(3.5)	(3.5)
Net assets			
		-	-
Reserves			
Retained earnings		-	-
Total reserves		-	-

These financial statements were approved by the Board of Directors on 8 June 2007 and were signed on its behalf by



N C Annett
Managing Director



C A Jones
Finance Director

Primary statements

Consolidated cashflow statement for the year ended 31 March 2007

	Note	2007 £m	2006 £m
Cash generated from operations	18	245.6	259.3
Interest received		7.1	7.2
Interest paid		(73.7)	(139.8)
Tax paid		-	(1.1)
Net cash inflow from operating activities		179.0	125.6
Cash flows from investing activities			
Purchase of property, plant and equipment		(188.7)	(182.5)
Grants and contributions received		22.5	16.8
Proceeds from sale of property, plant and equipment		-	0.8
Net cash used in investing activities		(166.2)	(164.9)
Net cash inflow/(outflow) before financing activities		12.8	(39.3)
Cash flows from financing activities			
Long term loans and finance leases received		32.2	113.8
Revolving credit facility (repayments)/drawdowns		(45.3)	145.3
Purchase of own bonds		-	(3.3)
Bond redemption		-	(465.5)
Bonds issued		150.0	-
Capital element of finance lease payments		(5.5)	(5.2)
Reduction in financial assets		0.3	33.6
Other loan repayments		(0.5)	(0.4)
Net cash used in financing activities		131.2	(181.7)
Increase/(decrease) in net cash	19	144.0	(221.0)
Net cash at 1 April		14.0	235.0
Net cash at 31 March	11	158.0	14.0

The parent company had no cashflows during the year

Notes to the financial statements

1 Accounting policies, financing risk management and accounting estimates

Basis of preparation

The financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and those parts of the Companies Act 1985 applicable to reporting under IFRS. The financial statements have been prepared under the historical cost convention as modified by the revaluation of certain financial instruments to fair value in accordance with IFRS and as permitted by the Fair Value Directive as implemented in the amended Companies Act 1985.

At the date of approval of these financial statements, the following Standards and Interpretations which have not been applied in these financial statements were in issue but not yet effective:

IFRS 7	Financial Instruments: Disclosures, and the related amendment to IAS 1 on capital disclosures
IFRS 8	Operating Segments
IFRIC 8	Scope of IFRS 2 – Share Based Payment
IFRIC 9	Reassessment of Embedded Derivatives
IFRIC 10	Interim Financial Reporting and Impairment
IFRIC 11	Group and Treasury Share Transactions
IFRIC 12	Service Concession Arrangements

The Directors anticipate that the adoption of these Standards and Interpretations in future periods will have no material impact on the financial statements of the Group except for additional disclosures that may be required on financial instruments when the relevant standards come into effect for periods commencing on or after 1 January 2007.

Basis of consolidation

The consolidated financial statements include the financial statements of the company and all of its subsidiaries. The results of companies and businesses acquired during the year are dealt with in the consolidated financial statements from the date of acquisition. Intra-group transactions and profits are eliminated on consolidation.

Accounting policies for the year ended 31 March 2007

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented.

Revenue recognition

Revenue represents the income receivable in the ordinary course of business for services provided, excluding value added tax. Where services have been provided, but for which no invoice has been raised at the year-end, an estimate of the amounts are included in revenue. See further details in the critical accounting estimates section.

Revenue recognised reflects the actual charges levied on customers in the year. The difference between the actual revenue and the level of revenue that could have resulted had the full Ofwat allowed level of charges been levied is referred to as a 'customer dividend'.

Property, plant & equipment

Property, plant and equipment are included at cost less accumulated depreciation. Cost reflects purchase price together with any expenditure directly attributable to bringing the asset into use, including directly attributable internal costs but excluding interest.

Property, plant and equipment comprise:

- (i) infrastructure assets (being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls), and
- (ii) other assets (including properties, overground operational structures and equipment, and fixtures and fittings)

Notes to the financial statements

The carrying value of assets is reviewed for impairment if circumstances dictate that the carrying value may not be recoverable. Asset lives and residual values are reviewed annually, which has this year resulted in a change to the useful economic life of water distribution network assets.

Infrastructure assets

Infrastructure assets, which comprise principally of impounding reservoirs and a network of underground water and wastewater systems, are stated at fair value on the date of transition to IFRS as a deemed cost under the exemption available under IFRS1. For accounting purposes, the water system is segmented into components representing categories of asset classes with similar characteristics and asset lives. The wastewater system is segmented into components representing geographical operating areas reflecting the way the Group operates its wastewater activities.

Expenditure on infrastructure assets relating to increases in capacity, enhancements or material replacements of network components, is treated as additions, which are included at cost. Expenditure incurred in repairing and maintaining the operating capability of individual infrastructure components, 'infrastructure renewals expenditure', is expensed in the year in which the expenditure is incurred.

The depreciation charge for infrastructure assets is determined for each component of the network and is based on each component's cost, estimated residual value and the expected remaining average useful life. The useful average economic lives of the infrastructure components range from 80 to 150 years (2006: 60 to 150 years).

Other assets

Other assets are depreciated on a straight line basis over their estimated useful economic lives, which are as follows:

Freehold buildings	60 years
Leasehold properties	over the lease period
Operational structures	40 - 80 years
Fixed plant	8 - 40 years
Vehicles, mobile plant, equipment and computer hardware & software	3 - 16 years

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

Intangible assets

Intangible assets, which comprise principally computer software and system developments, are included at cost less accumulated depreciation. Cost reflects purchase price together with any expenditure directly attributable to bringing the asset into use, including directly attributable internal costs but excluding interest.

The carrying values of intangible assets are reviewed for impairment if circumstances dictate the carrying value may not be recovered.

Intangible assets are depreciated on a straight line basis over their estimated useful economic lives, which range between 3 and 15 years. These asset lives are reviewed annually.

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 capitalised and included in 'property, plant & equipment' with the corresponding liability to the lessor included within 'finance liabilities – borrowings'. Leasing payments are treated as consisting of a capital element and a finance charge, the capital element reducing the obligation to the lessor with the finance charge being recognised over the period of the lease based on its implicit rate so as to give a constant rate of interest on the remaining balance of the liability.

All other leases are regarded as operating leases. Rental costs arising under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

Asset revaluations

The economic value of the Group's water and sewerage business is derived from the regulatory capital value (RCV) set by Ofwat during its five yearly price reviews. Accordingly, the carrying values of the regulatory assets will be periodically revalued to their economic values at five-yearly intervals, starting on 31 March 2010. The previous revaluation of regulatory assets was undertaken at 31 March 2004, as part of the transition to IFRS.

Grants and customer contributions

Grants and customer contributions in respect of expenditure on property, plant and equipment have been offset against fixed assets

Grants in respect of revenue expenditure are credited to the Income Statement over the same period as the related expenditure is incurred

Capital expenditure programme incentive payments

The Group's agreements with its construction partners involved in delivering capital expenditure programmes incorporate incentive bonuses payable after completion of the programmes. The cost of fixed asset additions includes an accrual for incentive bonuses earned to date, relating to projects substantially completed at the year-end, where the likelihood of making the incentive payment is considered probable. Amounts recoverable from contract partners, relating to targets not being achieved are only recognised on completed projects

Target cost contracts

The Group maintains target cost contracts with its main operating partners. The Group's policy in respect of pain/gain share payments/receivables arising from these contracts is to recognise when final agreement with the relevant service partner has been achieved

Allowance for doubtful debts

Trade receivables are first assessed individually for impairment, or collectively where the receivables are not individually significant. Where there is no objective evidence of impairment for an individual receivable, it is included in a group of receivables with similar credit risk characteristics and these are collectively assessed for impairment. Movements in the provision for doubtful debts are recorded in the income statement

Cash and cash equivalents

Cash and cash equivalents include highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of change in value. Such investments are normally those with less than three months maturity from the date of acquisition and typically include cash in hand and deposits with banks or other financial institutions, less any overdrafts

Pension costs

The majority of the Group's employees belong to the Group pension scheme, which is funded by both employers' and employees' contributions and which is of the defined benefit type. Actuarial valuations of the scheme are carried out at intervals of not more than three years. Contribution rates are based on the advice of a professionally qualified actuary

For the Group's defined benefit scheme, the net asset or liability recognised in the balance sheet represents the present value of the defined benefit obligations less the fair value of the plan's assets. In accordance with the amendment to IAS19, all cumulative actuarial gains and losses have been recognised in reserves at the date of transition to IFRS

The full cost of providing pension benefits to employees (including the expected return on scheme assets and interest on scheme liabilities) is reported in the income statement within operating costs. All actuarial gains and losses are also recognised in the year in which they arise in determining the profit or loss for the year

Financial liabilities – borrowings

Debt is initially measured at fair value, which is the amount of the net proceeds after deduction of directly attributable issue costs, with subsequent measurement at amortised cost. Debt issue costs are recognised in the income statement over the expected term of such instruments at a constant rate on the carrying amount

Foreign currency borrowings are translated into sterling at the rates ruling at the balance sheet date

Financial assets

Financial assets represent held to maturity investments that are non-derivative, with fixed or determinable payments and fixed maturities of over three months at the date of acquisition, which the Group intends to hold until maturity

Notes to the financial statements

Derivative financial instruments

Derivative instruments utilised by the Group are currency swaps, currency forward exchange contracts and interest rate swaps. Derivative instruments are used for hedging purposes to alter the risk profile of existing underlying exposures within the Group.

Derivatives are recognised initially, and are subsequently remeasured at fair value.

The movement in the fair value between balance sheet dates is recognised in the income statement to the extent that such instruments do not qualify for hedge accounting under IAS 39. At present, no such derivatives qualify for hedge accounting.

Deferred taxation

Deferred corporation tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised in respect of all temporary differences. Deferred tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and tax losses, to the extent that they are regarded as recoverable. They are regarded as recoverable where, on the basis of available evidence, there will be suitable taxable profits against which the future reversal of the underlying temporary differences can be deducted. The carrying value of the amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all, or part, of the asset to be utilised.

Deferred corporation tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on the tax rates that have been substantially enacted at the balance sheet date.

Provisions

Provision is made for all known and estimated liabilities of the Group where there is a present obligation and it is probable that a transfer of economic benefits will be required to settle the obligation.

In the case of leases, where properties are no longer occupied by the Group, provision is made for the liabilities that are expected to arise in respect of rental payments and dilapidations, prior to disposal or termination of the lease.

Where the Group receives claims that are either not covered by insurance or where there is an element of the claim for which insurance cover is not available, a provision is made for the expected future liabilities.

Financing risk management objectives and policies

Treasury activities are managed within a formal set of treasury policies and objectives, which are reviewed regularly and approved by the Board. The policy specifically prohibits any transactions of a speculative nature and the use of complex financial instruments. Certain detailed policies for managing interest rate, currency and inflation risk and that for managing liquidity risk are approved by the Board and may only be changed with the consent of Dwr Cymru Cyfyngedig's security trustee (the 'Security Trustee'). The risk is further mitigated by limiting exposure to any one counterparty. We use financial instruments, which principally include listed bonds, finance leases, bank loan facilities and derivatives, to raise finance and manage risk from our operations.

Credit risk

Surplus cash is invested in short and medium term sterling financial investments. The Board annually establishes the investment criteria, which is restricted to banks and other financial institutions meeting required standards assessed by the major credit rating agencies.

Interest rate/Currency risk

The Group minimises exposure to currency risk in respect of any foreign currency denominated borrowings by using appropriate derivative instruments to hedge these liabilities into sterling obligations.

The Group hedges at least 85% of its total outstanding financial liabilities, including finance leases, into either index-linked or fixed rate obligations. For this purpose interest rate liabilities on floating rate liabilities are hedged through a combination of derivative instruments and cash balances. The regulatory framework, under which revenues and the regulatory asset value are indexed also expose the Group to inflation risk. Subject to market constraints and Board approval the Group therefore may seek to raise new debt through index-linked instruments or to enter into appropriate hedging transactions.

The 'hedged' established to manage interest rate risks are economic in nature, but do not satisfy the specific requirements of IAS 39 in order to be treated as hedges for accounting purposes

Liquidity risk

Liquidity risk is managed by maintaining a balance between the continuity of funding and flexibility through the use of borrowings across a range of currencies, instruments, type and maturities. Our policy is to ensure that the maturity profile does not impose an excessive strain on our ability to repay loans. Under this policy, no more than 20% of the principal of group borrowings can fall due in any twenty-four month period.

Banking facilities

We maintain committed banking facilities in order to provide flexibility in the management of the Group's liquidity.

There is also a special liquidity facility, which we are required to maintain in order to meet certain interest and other obligations that cannot be funded through operating cashflow in the event of a standstill being declared by the Security Trustee, following an event of default under the Group's debt financing covenants.

Critical accounting estimates

The preparation of financial statements to conform with generally accepted accounting principles requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates.

Allowance for doubtful debts

Individual impairment losses on customer debts are calculated based on an individual assessment of the cash flows that are expected. Collective impairment losses on receivables with similar credit risk are calculated using a statistical model. The key assumption in the model is the probability of a failure to recover amounts when they fall into arrears. The probability of failing to recover is determined by past experience, adjusted for changes in external factors. The accuracy of the impairment calculation would therefore be affected by unexpected changes to the economic situation, and to changes in customer behaviour. To the extent that the failure to recover debts in arrears alters by +/-5%, the bad debt allowance would increase or decrease by £4.2 million (2006: £3.6 million).

Pension benefits

The present value of the pension obligations is dependent on the actuarial calculation, which includes a number of assumptions. These assumptions include the discount rate, which is used to calculate the present value of the estimated future cash outflows that will be required to meet the pension obligations. In determining the discount rate to use, the Group considers market yields of high quality corporate bonds, denominated in sterling, that have times to maturity approximating the terms of the pension liability. Were this discount rate to reduce or increase by 0.1%, the carrying value of the pension obligations would increase or reduce by £0.8 million (2006: £0.9 million).

Measured income accrual

Revenue includes an estimation of charges unbilled at the period end. The accrual is estimated using a defined methodology based upon the weighted average water consumption by tariff, which is calculated based upon historical billing information, adjusted for changes in external factors, such as weather. A 5% change in actual consumption from that estimated would have the effect of increasing/decreasing the accrual by £2.3 million (2006: £2.2 million).

2 Segmental information

The Directors consider that there is only one reporting segment being the operation of the water and sewerage business in the UK. Therefore the disclosures for the primary segment have already been given in these financial statements.

The secondary reporting format is by geographical analysis by origin and destination. As the Group virtually only has domestic activities there is only one geographical segment. Therefore the disclosures for the secondary segment have also already been given in these financial statements.

Parent Company

The parent company's business is solely to act as a holding company and therefore it operates in a single segment.

Notes to the financial statements

3 Financing costs

3a) Net interest before fair value losses on financial instruments

	GROUP	
	2007 £m	2006 £m
Interest payable on bonds	(84.5)	(91.9)
Indexation on index-linked bonds	(23.0)	(17.4)
Interest payable on finance leases	(33.8)	(31.9)
Interest payable on other loans	(16.9)	(12.8)
Amortisation of bond issue costs	(0.9)	(2.9)
Interest payable	(159.1)	(156.9)
Interest receivable	7.4	6.7
Net interest payable before fair value adjustments	(151.7)	(150.2)

3b) Fair value gains/(losses) on financial instruments

Whilst the Group employs an economically effective policy using interest rate and currency swaps, this policy does not satisfy the stringent hedge accounting criteria of IAS39. Consequently, the Group's interest rate and currency swaps are fair valued at each balance sheet date with the movement (gains or losses) disclosed in the income statement. Over the life of these swaps, providing that there is an effective match, these fair value adjustments will reverse and reduce to zero. (See note 14 for the balance sheet note in respect of derivative financial instruments)

	GROUP	
	2007 £m	2006 £m
Fair value gains/(losses) on interest rate swaps	34.9	(29.8)
Fair value gains/(losses) on index linked swaps	10.8	(3.5)
Fair value gains/(losses) on foreign exchange		
- Cross-currency swaps	-	48.5
- Foreign denominated bonds	-	(48.5)
Fair value gains/(losses) on financial instruments	45.7	(33.3)
Tax effect of fair value (gains)/losses on financial instruments	(13.7)	10.0
Net of tax impact of fair value gains/(losses) on financial instruments	32.0	(23.3)

4 Profit before taxation

The following items have been included in arriving at profit before taxation

	GROUP	
	2007	2006
	£m	£m
Operating charges from outsourced activities		
- Operating services agreements	115.9	107.7
- Customer services agreement	18.6	19.4
- Laboratories and analytical services	7.6	7.3
- Other contracts	14.2	11.7
	156.3	146.1
Employee costs (note 20)		
- Wages and salaries	8.0	7.7
- Social security	0.9	0.7
- Severance programme and other termination costs	0.2	-
- Net actuarial loss/(gain) (note 21)	0.9	(1.5)
- Pension costs (excluding actuarial loss/gain) (note 21)	1.7	2.5
Research and development expenditure	0.4	0.4
Trade receivables impairment	11.0	7.6
Rates	21.0	18.8
Environment agency charges	13.5	13.0
Fees paid to auditors (see below)	0.2	0.2
Own work capitalised	(8.5)	(7.3)
Net rents payable	-	0.5
Other operating charges	23.0	24.5
	228.6	213.2
Depreciation of property, plant and equipment		
- Owned assets	75.1	60.1
- Under finance leases	35.0	33.6
Amortisation of intangible assets	1.7	3.8
Infrastructure renewals expenditure	84.1	48.8
Profit on disposal of fixed assets	-	(0.8)
	424.5	358.7

Services provided by the Group's auditor

During the year the Group obtained the following services from the Group's auditor as detailed below

	GROUP	
	2007	2006
	£'000	£'000
Audit of parent company and consolidated financial statements	11	13
Other services		
- Subsidiary company audit services	69	86
- Regulatory audit services pursuant to legislation	49	32
- Tax advisory services	1	10
- Interim review	20	25
- Bond issue	24	-
- Grant applications	2	6
- Financial modelling	1	12
- IFRS transition	-	48
	177	232

Regulatory audit services includes work on the Regulatory Accounts, June Return and Principal Statement

Notes to the financial statements

In addition to the above services, PricewaterhouseCoopers LLP acted as auditor to the Welsh Water Pension Scheme. The appointment of auditors to the pension scheme and the fees paid in respect of the audit are agreed by the trustees of the scheme, who act independently from the management of the Group. The fees paid in respect of audit services to the pension scheme during the year were £7,000 (2006: £7,000).

The Board has adopted a formal policy with respect to services received from external auditors. The external auditor will not be used for internal audit services and all non-audit work above a threshold of £25,000 will be subject to prior competitive tendering and approval by the Audit Committee.

5 Taxation

Analysis of (charge)/credit in the year

	GROUP	
	2007 £m	2006 £m
Current tax		
- Adjustment in respect of prior years	-	(1.4)
Deferred tax		
- Current year movements	(15.9)	0.9
- Adjustment in respect of prior years	1.7	5.3
Taxation (charge)/credit	(14.2)	4.8

The tax for the year is lower (2006: lower) than the standard rate of corporation tax in the UK (30%). The differences are explained below.

	GROUP	
	2007 £m	2006 £m
Profit before tax	47.5	11.3
Profit before tax multiplied by the corporation tax rate in the UK of 30% (2006: 30%)	14.3	3.4
Effects of		
Expenses not deductible for tax purposes	0.1	0.2
Adjustments in respect of prior years	(1.7)	(3.9)
Other permanent differences	1.5	(4.5)
Total taxation charge/(credit)	14.2	(4.8)

6 Intangible assets

Intangible assets comprise computer software and related system developments

GROUP	Cost £m	Depreciation £m	Net book value £m
Current year			
At 1 April 2006	53.4	(49.0)	4.4
Additions	4.3	-	4.3
Charge for the year	-	(1.7)	(1.7)
At 31 March 2007	57.7	(50.7)	7.0
Prior year			
At 1 April 2005	49.6	(45.2)	4.4
Additions	3.8	-	3.8
Charge for the year	-	(3.8)	(3.8)
At 31 March 2006	53.4	(49.0)	4.4

The parent company owns no intangible fixed assets

7 Property, plant and equipment

GROUP	Freehold land and buildings £m	Infrastructure assets £m	Operational structures £m	Plant equipment, computer hardware £m	Total £m
Current year					
Cost					
At 1 April 2006	32.7	1,375.2	2,055.0	193.2	3,656.1
Additions net of grants and contributions	0.2	37.5	128.0	25.0	190.7
Disposals	-	-	(64.9)	-	(64.9)
At 31 March 2007	32.9	1,412.7	2,118.1	218.2	3,781.9
Accumulated depreciation					
At 1 April 2006	15.5	39.8	654.6	150.6	860.5
Charge for the year	0.4	31.4	72.1	6.2	110.1
Disposals	-	-	(35.6)	-	(35.6)
At 31 March 2007	15.9	71.2	691.1	156.8	935.0
Net book value					
At 31 March 2007	17.0	1,341.5	1,427.0	61.4	2,846.9

Notes to the financial statements

GROUP	Freehold land and buildings £m	Infrastructure assets £m	Operational structures £m	Plant equipment, computer hardware £m	Total £m
Prior year					
Cost					
At 1 April 2005	32.8	1,310.6	1,959.6	184.8	3,487.8
Additions net of grants and contributions	-	64.6	95.4	8.4	168.4
Disposals	(0.1)	-	-	-	(0.1)
At 31 March 2006	32.7	1,375.2	2,055.0	193.2	3,656.1
Accumulated depreciation					
At 1 April 2005	14.8	18.8	589.1	144.2	766.9
Charge for the year	0.8	21.0	65.5	6.4	93.7
Disposals	(0.1)	-	-	-	(0.1)
At 31 March 2006	15.5	39.8	654.6	150.6	860.5
Net book value					
At 31 March 2006	17.2	1,335.4	1,400.4	42.6	2,795.6

Included within fixed assets is an amount £157.6m in respect of assets in the course of construction (2006: £99.9m)

Assets held under finance leases

Included within the above are assets held under finance leases, analysed as below

GROUP	Infrastructure assets £m	Operational structures £m	Total £m
Current year			
Cost			
At 1 April 2006	526.8	565.9	1,092.7
Additions	-	32.2	32.2
At 31 March 2007	526.8	598.1	1,124.9
Accumulated depreciation			
At 1 April 2006	30.1	126.1	156.2
Charge for the year	6.6	28.4	35.0
At 31 March 2007	36.7	154.5	191.2
Net book value			
At 31 March 2007	490.1	443.6	933.7

GROUP	Infrastructure assets £m	Operational structures £m	Total £m
Prior year			
Cost			
At 1 April 2005	424.7	535.5	960.2
Additions	102.1	30.4	132.5
At 31 March 2006	526.8	565.9	1,092.7
Accumulated depreciation			
At 1 April 2005	22.5	100.1	122.6
Charge for the year	7.6	26.0	33.6
At 31 March 2006	30.1	126.1	156.2
Net book value			
At 31 March 2006	496.7	439.8	936.5

The parent company owns no property plant or equipment

8 Fixed asset investments

a) Group

Cost and net book value	2007 £m	2006 £m
At 1 April and 31 March	-	-

Equity of less than 10% is held in the following unlisted company

	Nature of business	Country of incorporation	Description of holding
Water Research Centre (1989) plc	Water Research	Great Britain	'B' Ordinary Shares of £1

In addition, the Group holds 5% Convertible Unsecured Loan Stock 2014 at a cost of £23,326 in Water Research Centre (1989) plc

b) Parent Company

The Company has a £1 investment in Glas Cymru (Securities) Cyfyngedig and has indirect investments in the following subsidiary undertakings

	Principal activity	Country of incorporation	Holding
Dŵr Cymru (Holdings) Limited	Holding company	England and Wales	100%
Dŵr Cymru Cyfyngedig	Water and sewerage	England and Wales	100%
Dŵr Cymru (Financing) Limited	Raising finance	Cayman Islands	100%
Welsh Water Utilities Finance Plc	Raising finance	England and Wales	100%

Notes to the financial statements

9 Trade and other receivables

	GROUP		COMPANY	
	2007 £m	2006 £m	2007 £m	2006 £m
a) Amounts falling due within one year				
Trade receivables	84.7	77.0	-	-
Less provision for impairment of receivables	(53.0)	(49.6)	-	-
Trade receivables - net	31.7	27.4	-	-
Other receivables	5.2	9.8	-	-
Prepayments and accrued income	53.5	49.5	-	-
	90.4	86.7	-	-
b) Amounts falling due after more than one year				
Amounts owed by group undertakings	-	-	3.4	3.4
	90.4	86.7	3.4	3.4

10 Held to maturity investments

	GROUP		COMPANY	
	2007 £m	2006 £m	2007 £m	2006 £m
Investments in				
Fixed term deposits - due within one year	-	0.3	-	-

The effective interest rate on held to maturity investments as at 31 March 2006 was 4.7% and these investments had an average maturity of 364 days

11 Cash and cash equivalents

	GROUP		COMPANY	
	2007 £m	2006 £m	2007 £m	2006 £m
Cash at bank and in hand	3.8	3.8	0.1	0.1
Short-term bank deposits	154.2	10.2	-	-
	158.0	14.0	0.1	0.1

The effective interest rate on short-term deposits as at 31 March 2007 was 5.4% (2006 4.7%) and these deposits have an average maturity of 30 days (2006 82 days)

12 Trade and other payables

	GROUP		COMPANY	
	2007 £m	2006 £m	2007 £m	2006 £m
Current				
Trade payables	12.3	26.8	-	-
Capital creditors	41.9	45.3	-	-
Deferred income	0.4	-	-	-
Other taxation and social security	0.3	0.3	-	-
Amounts owed by group undertakings	-	-	3.5	3.5
Other payables	46.6	46.1	-	-
	101.5	118.5	3.5	3.5
Non-current				
Deferred income	2.5	-	-	-

13 Financial liabilities – borrowings

	GROUP		COMPANY	
	2007 £m	2006 £m	2007 £m	2006 £m
Current				
Revolving credit facilities	-	120.3	-	-
Local Authority loans	0.3	0.3	-	-
European Investment Bank loans	4.4	-	-	-
Finance lease obligations	4.7	3.7	-	-
Interest accruals	56.4	0.3	-	-
	65.8	124.6	-	-
Non-current				
Bonds	1,592.7	1,419.7	-	-
Unamortised bond premium	13.4	13.9	-	-
Unamortised loan issue costs	(6.3)	(7.2)	-	-
Finance lease obligations	762.1	736.4	-	-
European Investment Bank loans	130.6	60.0	-	-
Local Authority loans	2.9	3.4	-	-
Interest accruals	24.6	18.7	-	-
	2,520.0	2,244.9	-	-

A security package was granted by Dŵr Cymru Cyfyngedig (DCC), as part of the Group's bond programme for the benefit of holders of senior bonds, finance lessors and other senior financial creditors

The obligations of DCC are guaranteed by the Company, Glas Cymru (Securities) Cyfyngedig and Dŵr Cymru (Holdings) Limited. The main elements of the security package are

- i) a first fixed and floating security over all of DCC's assets and undertaking, to the extent permitted by the Water Industry Act, other applicable law and its licence, and
- ii) a fixed and floating security given by the guarantors referred to above which are accrued on each of these companies' assets including, in the case of Dŵr Cymru (Holdings) Limited, a first fixed charge over its shares in DCC

Notes to the financial statements

14 Derivative financial instruments

Derivative financial instruments are held for economic hedging purposes although they do not qualify as accounting hedges under IAS 39. As such, movements in their fair value are taken to the Income Statement (note 3b). Fair values are obtained by reference to actual market transactions.

	FAIR VALUES	
	Assets £m	Liabilities £m
GROUP - 2007		
Current		
Interest rate swaps	-	(34.2)
Index linked swaps	4.2	(4.6)
	4.2	(38.8)
Non-current		
Interest rate swaps	-	(21.3)
Index linked swaps	14.7	(14.7)
	14.7	(36.0)
Total	18.9	(74.8)

The notional value of the interest rate swaps are £625m (2006: £625m) and the indexed linked swaps £679m (2006: £587m).

	FAIR VALUES	
	Assets £m	Liabilities £m
GROUP - 2006		
Current		
Interest rate swaps	-	(6.2)
Index linked swaps	4.2	-
	4.2	(6.2)
Non-current		
Interest rate swaps	-	(91.9)
Index linked swaps	6.3	(14.0)
	6.3	(105.9)
Total	10.5	(112.1)

In accordance with IAS 39, 'Financial Instruments: Recognition and Measurement', the Group has reviewed all contracts for embedded derivatives that are required to be separately accounted for if they do not meet certain requirements set out in the standard. Glas Cymru Cyfyngedig has no embedded derivatives as per IAS 39.

Parent Company

The parent company has no derivative financial instruments or embedded derivatives.

Interest rate swaps

At 31 March 2007 the interest rate swaps fix the interest rate on the £279 million (2006: £295 million) of floating rate liabilities held by the Group.

The principal terms of the interest rate swaps are as follows:

Notional Amount (£m)	Swap Maturity	Quarterly interest rate
478	31 March 2031	5.67%
32	31 March 2021	5.82%
115	31 March 2008	5.95%
625		

In April 2007 Dwr Cymru (Financing) Limited took advantage of market conditions to terminate £433 million of surplus floating to fixed interest swaps at a cost of £32.5 million. This cost is reflected within the fair value of the derivative financial instruments at 31 March 2007.

Indexed-linked swaps

Finance lease swaps

The indexed-linked swaps have the effect of index linking the interest rate on £626 million (2006 £630 million) of finance lease liabilities by reference to the retail price index ('RPI')

The notional amount of the swaps as at 31 March 2007 is £579 million (2006 £587 million), representing the average balance on the finance leases subject to floating interest rates for the year to 31 March 2008. The notional amount amortises over the life of the swaps to match the average floating rate balances of the leases.

The principal terms are as follows

Notional Amount	£579 million (amortising)
Average swap maturity	25 years
Average interest rate	1.60% (fixed) plus RPI

Bond swap

The index-linked swaps have the effect of index linking the interest rate on £102 million of fixed rate bonds by reference to the retail price index ('RPI')

The principal terms are as follows

Notional Amount	£100 million
Swap maturity	50 years
Interest rate	1.35% (fixed) plus RPI

15 Financial risk management

The policies of the Group in respect of financial risk management are included in the accounting policies note on page 60. The numerical financial instrument disclosures as required by IAS 32 are set out below.

a) Interest rate risk

The effective interest rates at the balance sheet dates were as follows:

	2007	2006
Assets		
Cash and cash equivalents	5.4%	4.7%
Financial assets held to maturity	-	4.7%
Liabilities		
Bonds	5.4%	5.7%
Revolving credit facilities	-	4.9%
European Investment Bank loans	5.6%	4.7%
Local Authority loans	6.5%	6.2%
Finance lease obligations	4.5%	4.5%

Trade receivables and payables are non-interest bearing.

The effective interest rates ignore the effect of the interest rate and index-linked swaps set out on page 70.

Notes to the financial statements

b) Liquidity risk

GROUP - 2007	Within 1yr £m	1-2 years £m	2-5 years £m	> 5 years £m	Total £m
Assets					
Cash and cash equivalents	158 0	-	-	-	158 0
Trade and other receivables	91 8	-	-	-	91 8
	249 8	-	-	-	249 8
Liabilities					
Bonds	-	-	125 0	1,481 1	1,606 1
European Investment Bank loan	4 4	4 4	26 8	99 4	135 0
Local Authority loans	0 3	0 4	1 1	1 4	3 2
Finance lease obligations	4 7	5 8	24 9	731 4	766 8
Trade and other payables	101 5	0 4	1 1	1 0	104 0
	110 9	11 0	178 9	2,314 3	2,615 1

GROUP - 2006	Within 1yr £m	1-2 years £m	2-5 years £m	> 5 years £m	Total £m
Assets					
Cash and cash equivalents	14 0	-	-	-	14 0
Financial assets held to maturity	0 3	-	-	-	0 3
Trade and other receivables	86 7	-	-	-	86 7
	101 0	-	-	-	101 0
Liabilities					
Bonds	-	-	125 0	1,308 6	1,433 6
Revolving credit facilities	120 3	-	-	-	120 3
European Investment Bank loan	-	4 4	15 4	40 2	60 0
Local Authority loans	0 3	0 4	1 1	1 9	3 7
Finance lease obligations	3 7	4 6	21 0	710 8	740 1
Trade and other payables	118 5	-	-	-	118 5
	242 8	9 4	162 5	2,061 5	2,476 2

As at 31 March 2007 and 31 March 2006, the Bonds maturing between 2-5 years represent £125 million of sub-ordinated Bonds with an expected maturity date of 31 March 2011. If these Bonds are not redeemed on or before 31 March 2011, the interest rate will step-up from a fixed rate of 8.174% to a floating 3 - month LIBOR interest rate plus a margin 5.75%

The minimum lease payments under finance leases fall due as follows

	2007 £m	2006 £m
Not later than one year	39 4	31 1
Later than one year but not more than five	180 2	147 0
More than five years	1,336 1	1,289 4
	1,555 7	1,467 5
Future finance charges on finance leases	(763 5)	(708 4)
Present value of finance lease liabilities (including accrued interest)	792 2	759 1

c) Fair values

The fair values of the Group's derivative financial instruments are set out on page 70. The following table summarises the fair value and book value of the Group's bonds.

	2007		2006	
	Book value £m	Fair Value £m	Book Value £m	Fair Value £m
Bonds (note 13)	1,606.1	1,875.1	1,433.6	1,777.2

The fair value of all other financial instruments are equal to the book values.

d) Borrowing facilities

The Group has the following undrawn committed borrowing facilities available at 31 March in respect of which all conditions precedent had been met at that date.

	2007 £m	2006 £m
Expiring in more than 1 year		
Revolving credit facilities	345.0	259.8
European Investment Bank	-	75.0
	345.0	334.8

Dŵr Cymru (Financing) Limited also has a special liquidity facility of £150 million, which it is required to maintain in order to meet certain group interest and other obligations that cannot be funded through operating cashflow of the Group, in the event of a standstill being declared by the Security Trustee. A standstill would arise in the event that Dŵr Cymru Cyfyngedig defaults on its debt financing covenants. Dŵr Cymru Cyfyngedig also has a £20 million overdraft facility. Both of these facilities are renewable on an annual basis.

During the year, the Company reduced its revolving credit facility with the Fortis Bank from £75 million to £40 million.

All the above facilities, including the liquidity facility, are at floating rates of interest.

16 Provisions

GROUP	Restructuring provision £m	Uninsured loss provision £m	Total £m
At 1 April 2006	5.3	4.5	9.8
(Released)/Charged to Income Statement	(3.9)	4.3	0.4
Utilised in year	(0.3)	(1.3)	(1.6)
At 31 March 2007	1.1	7.5	8.6

The parent company has no provisions at 31 March 2007 (2006: nil).

Restructuring provision

This provision is in respect of payments to be made relating to estimated dilapidation costs at leased properties, which will be utilised over the next three years.

Provision for uninsured losses

This provision is in respect of uninsured losses and where insurance cover does not cover a deductible amount. The utilisation period of these liabilities is uncertain due to the nature of the claims but is estimated to be five years.

Notes to the financial statements

17 Deferred tax

Deferred tax is calculated in full on temporary differences under the liability method using a tax rate of 30% (2006 30%)

The movement in the deferred tax provision is as shown below

	GROUP		COMPANY	
	2007 £m	2006 £m	2007 £m	2006 £m
At 1 April	374.2	380.4	-	-
Charged/(Credited) to Income Statement	14.2	(6.2)	-	-
At 31 March	388.4	374.2	-	-

Deferred tax assets have been recognised in respect of all tax losses and other temporary differences giving rise to deferred tax assets because it is probable that these assets will be recovered

	GROUP		COMPANY	
	2007 £m	2006 £m	2007 £m	2006 £m
Effect of tax allowances over depreciation	429.4	394.6	-	-
Other tax differences	(41.0)	(20.4)	-	-
Provision for deferred tax	388.4	374.2	-	-

18 Cash generated from operations

Reconciliation of operating profit to cash generated from operations

	GROUP	
	2007 £m	2006 £m
Operating profit	153.5	194.8
Adjustments for		
Depreciation and amortisation	111.8	97.5
Profit on disposal of fixed assets	-	(0.8)
Changes in working capital		
Increase in trade and other receivables	(3.4)	(17.9)
Decrease in trade and other payables	(14.0)	(13.2)
Decrease in retirement benefit obligation	(1.1)	(1.2)
(Decrease)/increase in provisions	(1.2)	0.1
Cash generated from operations	245.6	259.3

19 Analysis and reconciliation of net debt

a) Net debt at the balance sheet date may be analysed as

	GROUP		COMPANY	
	2007 £m	2006 £m	2007 £m	2006 £m
Cash and cash equivalents	158 0	14 0	0 1	0 1
Financial assets – held to maturity	-	0 3	-	-
	158 0	14 3	0 1	0 1
Debt due after one year	(1,739 6)	(1,497 0)	-	-
Debt due within one year	(4 7)	(120 6)	-	-
Finance leases	(766 8)	(740 1)	-	-
Accrued interest	(81 0)	(19 0)	-	-
Unamortised bond issue costs	6 3	7 2	-	-
	(2,585 8)	(2,369 5)	-	-
Net debt	(2,427 8)	(2,355 2)	0 1	0 1

b) The movement in net debt during the period may be summarised as

	GROUP		COMPANY	
	2007 £m	2006 £m	2007 £m	2006 £m
Net debt at of start period	(2,355 2)	(2,246 3)	0 1	0 1
Increase/(decrease) in net cash	144 0	(221 0)	-	-
Decrease in financial assets	(0 3)	(33 6)	-	-
(Increase)/decrease in debt	(130 9)	215 3	-	-
Decrease/(increase) in net debt arising from cashflows	12 8	(39 3)	-	-
Movement in accrued interest	(62 0)	(1 3)	-	-
Amortisation of debt issue costs	(0 9)	(2 7)	-	-
Amortisation of bond issue premium	0 5	0 3	-	-
Foreign currency movement on dollar bond	-	(48 5)	-	-
Indexation of index-linked debt	(23 0)	(17 4)	-	-
Movement in net debt during the period	(72 6)	(108 9)	-	-
Net debt at end of period	(2,427 8)	(2,355 2)	0 1	0 1

Notes to the financial statements

20 Employees and Directors

a) Staff costs for the Group during the year

	2007 £m	2006 £m
Wages and salaries	8 0	7 7
Severance programme and termination costs	0 2	-
Social security costs	0 9	0 7
Other pension costs	2 6	1 0
	11 7	9 4

Of the above, £4.7 million (2006: £3.7 million) has been charged to capital. Other pension costs include £nil (2006: £0.4 million) in respect of the severance programme and termination costs. Other pension costs include £0.4m (2006: £0.5m) in respect of the Directors' unfunded pension liabilities.

	2007 Number	2006 Number
Average monthly number of people (including executive Directors) employed by the Group		
Regulated water and sewerage activities	159	136

b) Parent Company

The parent company had no employees (2006: nil) in the year.

Full details of the directors' remuneration are included in the Directors' Remuneration Report set out on pages 37 to 42, which form part of these Financial Statements.

21 Pension commitments

Following the acquisition of Dŵr Cymru Cyfyngedig by Glas Cymru Cyfyngedig, a new funded defined benefit pension scheme for current employees (based on final pensionable salary and pensionable service) was introduced on 1 December 2001, the DCWW Pension Scheme. The assets of the scheme are held in a separate trustee administered fund.

The DCWW Pension Scheme was closed to new members from the 31 December 2005 and a new defined contribution scheme, the Dŵr Cymru Defined Contribution Scheme, was introduced from the 1 January 2006.

Total pension costs in the year were as follows

	2007 £'000	2006 £'000
Defined contribution scheme	150	24
Defined benefit scheme – excluding actuarial gains/losses	1,518	2,447
	1,668	2,471
Net actuarial losses/(gains) recognised in year	921	(1,497)
	2,589	974

The total charge of £2,589m (2006: £0,974m) is included within operating costs.

Defined benefit scheme

A full actuarial valuation of the scheme was undertaken as at 31 March 2006 by Quantum Advisory Limited, an independent and professionally qualified actuary, using the attained age method. This valuation was updated at 31 March 2007 and the principal assumptions made by the actuaries were

	2007	2006
Rate of increase in pensionable salaries	4.00%	3.75%
Rate of increase in pensions in payment	3.00%	2.75%
Discount rate	5.40%	5.10%
Inflation assumption	3.00%	2.75%

Life expectancy assumptions are based on those in published actuarial tables 'PA92', projected to 2020

The major categories of plan assets, as a percentage of total assets and the expected rates of return thereon, were as follows

	2007		2006	
	Expected long term return	Percentage of total assets	Expected long term return	Percentage of total assets
Equities	7.00%	57%	6.50%	55%
Bonds	5.50%	36%	5.00%	35%
Other	4.50%	7%	4.50%	10%

Pensions and other post-retirement obligations

The amounts recognised in the income statement are as follows

	2007	2006
	£'000	£'000
Current service cost (excluding members contribution)	1,083	1,271
Interest cost	1,927	1,779
Expected return on plan assets	(1,858)	(1,502)
Past service cost	366	899
Total excluding net actuarial losses/(gains)	1,518	2,447
Net actuarial losses/(gains) recognised in year	921	(1,497)
Total included within staff costs	2,439	950

The amounts recognised in the balance sheet are determined as follows

	2007	2006
	£'000	£'000
Present value of funded obligations	(41,009)	(37,197)
Fair value of plan assets	35,520	30,561
Net liability recognised in the balance sheet	(5,489)	(6,636)

Notes to the financial statements

Changes in the present value of the defined benefit obligation are as follows

	2007 £'000	2006 £'000
At 1 April	37,197	32,406
Current service cost (including members contribution)	1,421	1,612
Past service cost	366	899
Interest cost	1,927	1,779
Benefits paid	(594)	(1,452)
Actuarial losses	692	1,953
31 March	41,009	37,197

Changes in the fair value of plan assets are as follows

	2007 £'000	2006 £'000
At 1 April	30,561	24,637
Expected return on plan assets	1,858	1,502
Contributions (including members contribution)	3,924	2,424
Benefits paid	(594)	(1,452)
Actuarial (loss)/gain on plan assets	(229)	3,450
31 March	35,520	30,561

Analysis of the movement in the balance sheet liability

	2007 £'000	2006 £'000
At 1 April	6,636	7,769
Total expense as above	2,439	950
Contributions paid (excluding members contribution)	(3,586)	(2,083)
31 March	5,489	6,636

	2007 £'000	2006 £'000
Expected return on plan assets	1,858	1,502
Actuarial (loss)/gain on plan assets	(229)	3,450
Actual return on plan assets	1,629	4,952

	2007	2006	2005	2004
Experience adjustments arising on scheme assets				
Amount (£m)	(0.2)	3.5	0.9	2.0
Percentage of scheme assets	1%	11%	4%	11%
Experience adjustments arising on scheme liabilities				
Amount (£m)	(2.0)	0.3	(0.3)	-
Percentage of the present value of scheme liabilities	5%	1%	(1%)	0%
Present value of scheme liabilities (£m)	41.0	37.2	32.4	26.7
Fair value of scheme assets (£m)	35.5	30.6	24.6	18.9
Deficit (£m)	(5.5)	(6.6)	(7.8)	(7.8)

The contributions paid in the year to 31 March 2007 include a special contribution of £2.0 million. The contribution expected to be paid during the financial year ended 31 March 2008 amounts to £5.8 million.

22 Operating lease commitments – minimum lease payments

GROUP	LAND AND BUILDINGS	
	2007 £m	2006 £m
At 31 March 2007 there were revenue commitments, in the ordinary course of business in the next year for the payment of rentals on non cancellable operating leases expiring after five years	-	0.4

The parent company has no lease commitments (2006: £nil)

23 Capital and other financial commitments

The Group's business plan at 31 March 2007 shows net capital expenditure and infrastructure renewals expenditure of £293m (2006: £280m) during the next financial year. While only a portion of this amount has been formally contracted for, the Group is effectively committed to the total as part of its overall capital expenditure programme approved by its Regulator.

24 Related party transactions

In accordance with the exemption afforded by IAS 24 there is no disclosure in the consolidated financial statements of transactions with entities that are part of the Glas Cymru Cyfyngedig group.

25 Status of the company

The Company is limited by guarantee and does not have any share capital. In the event of the Company being wound up, the liability of the members is limited to £1 each.

26 Directors' and officers' loans and transactions

No loans or credit transactions with any Directors, officers or connected persons existed during the year or were outstanding at the balance sheet date.

Notes to the financial statements

27 Subsequent events

In April 2007 Dŵr Cymru (Financing) Limited took advantage of market conditions to terminate £433 million of surplus floating to fixed interest swaps at a cost of £32.5 million. This cost is reflected within the fair value of the derivative financial instruments at 31 March 2007.

HM Government have proposed to amend the rate of corporate tax from 30% to 28% with effect from 1 April 2008 in the Finance Bill 2007. It has also announced prospective changes to the capital allowances regime from 1 April 2008, to be included in next year's Finance Bill. The impact of these changes, and in particular the effect on the Group's deferred tax liability, will be reflected in the financial statements when these proposals become law.

28 Elan Valley Trust Fund

In 1984 Welsh Water Authority entered into a conditional sale and purchase agreement with Severn Trent Water Authority for the sale of the aqueduct and associated works by which the bulk supply to Severn Trent reservoirs is conveyed.

HM Government have proposed to amend the rate of corporation tax from 30% to 28% with effect from 1 April 2008 in the Finance Bill 2007. It has also announced prospective changes to the capital allowances regime from 1 April 2008, to be included in next year's Finance Bill. The impact of these changes, and in particular the effect on the Group's deferred tax liability, will be reflected in the financial statements when these proposals become law.

The sum of £31.7 million, representing the consideration for the conditional sale, was invested in a trust fund. The principal function of the fund was to provide an income to Welsh Water Authority, whilst preserving the capital value of the fund in real terms. Welsh Water Authority's interest in this fund was vested in Dŵr Cymru Cyfyngedig under the provisions of the Water Act 1989.

The assets of the fund are not included in these financial statements.

Interest receivable includes £2.7 million (2006 £2.1 million) in respect of the Elan Valley Trust Fund.