



Report and Accounts 2009

Glas Cymru Cyfyngedig
Company Number: 3975719

WEDNESDAY



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Report and accounts 2009

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The photographs in this report have been taken by; staff from Welsh Water and its contract partners, under a project carried out with photojournalist Glenn Edwards; and winners of the Welsh Water Photography Bursary Award in 2005 and 2006.

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Introduction

Glas Cymru

The single purpose company formed in 2000 to own, finance and manage Welsh Water on behalf of today's customers and future generations. As a company limited by guarantee, Glas Cymru has no shareholders and any financial surpluses are retained or reinvested for the benefit of Welsh Water's customers or distributed as 'customer dividends'.

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

Welsh Water

The sixth largest of the 10 regulated water and sewerage companies in England and Wales. We provide an essential public service to more than 3 million people living in Wales and some adjoining parts of England. The water industry everywhere is capital intensive and Welsh Water employs a huge and complex network of often very long life assets – with a replacement cost of £19 billion, around £15,000 per household – to deliver water and sewerage services to our customers. It is our responsibility to operate, maintain and upgrade efficiently this large network of assets so as to ensure a safe and reliable supply of drinking water for our customers and to then carry away and deal with wastewater so that both public health and the environment are protected. Our ambition is to be recognised by our customers as the best water company in the UK.

Highlights

Protecting public health

- » Continued high level of water quality compliance – 99.95% mean zonal compliance
- » Good progress on delivering our enhanced drinking water quality protection programme

Safeguarding the environment

- » 100% compliance at wastewater treatment works
- » Category 1 and 2 pollution incidents reduced to 3

Meeting customers' expectations

- » Continued high levels of customer satisfaction, as measured by independent tracking research
- » Positive endorsement by customers of our 2010-15 draft business plan

Affordability and value for money

- » 'Customer dividend' in 2008-09 of £21 per customer totalling £27 million
- » New tariffs introduced to provide assistance for customers who experience difficulty in paying their water charges

Employer of choice

- » High level of employee satisfaction
- » 26% reduction in reportable accidents over the last 2 years

Responding to climate change

- » 3% reduction in energy use
- » 22% increase in renewable energy

Financing the business

- » Largest ever annual capital investment programme - over £355 million
- » Financial reserves or 'customer equity' exceeds £1 billion

Despite the increasingly difficult economic environment, I am pleased to report a year of continued good progress in operational and environmental performance and in serving customers in our area. We have responded positively to the challenges of the current economic recession and have put affordability at the heart of our plans. Having built up a strong financial position over the last 7 years we have been able to afford to press ahead with our largest ever capital investment programme.

Chairman's statement

It is clear that many of our household customers are now having real difficulties in paying their water bill. Our bills were kept down by the increase in our 'customer dividend', which deducted £21 from last year's bill for water and sewerage. Welsh Water is still the only regulated water company to pay a 'customer dividend' and the total sum returned to Welsh Water's customers to date now stands at £150 million. In addition, we have been able to help low income household customers by introducing a third assistance tariff, Welsh Water Assist, which puts a cap of £250 on the bill for some low income families with high water use. We estimate that around 9,000 customers could benefit from this tariff.

Affordability is also at the heart of our plans for the next regulatory period, making Welsh Water the only regulated water and sewerage company to have proposed that bills will be the same in real terms in 2015 as today.

Just as important is the quality and reliability of our service. Few things are as vital as safe drinking water and it is good to report that our compliance with standards for drinking water quality in 2008 was up with the best it has ever been at 99.95%. It was disappointing, therefore, that we also had to issue 2 precautionary Boil Water Notices in 2008, causing considerable inconvenience for more than 50,000 customers, at Penybont and Mynydd Llandygai, when our routine sampling picked up evidence of cryptosporidium.

Our priority is always to protect public health and there was no illness reported as a result of these two incidents.

To avoid such incidents in future we have commenced ahead of the next Price Review a £200 million investment programme on drinking water improvements throughout Wales. This will add an additional stage of treatment to 9 works, mostly in north Wales, which previously relied on single stage treatment of high quality source waters. Pending completion of this major programme we have since last September installed ultra violet treatment to protect against the risk posed by cryptosporidium.

Since the year end a further precautionary Boil Water Notice had to be issued affecting 70,000 customers following the detection of high levels of coliform bacteria at our Alwen works, serving north east Wales. In response we decided to bring forward a £14 million scheme from our AMP5 programme to refurbish this works which is now 20 years old.

Last year we delivered our highest ever capital expenditure on improving and maintaining our £19 billion network of assets, completing work on projects costing £355 million. This year we will invest a further £350 million - higher than originally planned, in part, because of the accelerated water treatment works improvement programme.

Dealing with the extremely cold weather in January was a major challenge for the business. The freezing temperatures caused operational problems right across our region, the most serious of which was the loss of supply in the area served by Maerdy water treatment works in the Rhondda. More generally, despite the fact that the number of bursts more than doubled and leakage rose by 50% in some areas, the highly effective response by our contract partners right across the region meant we were able to get total leakage back down by the year end and hit our Ofwat target.

For the first time in more than 10 years Welsh Water achieved 100% compliance with discharge 'look-up' consents at our wastewater treatment works. We also achieved a further reduction in the number of serious pollution incidents, bringing the number down to just 3, from 9 in the previous year and 17 in the year before that. This makes Welsh Water one of the best performers in the industry on a measure where we had previously lagged the rest of the sector.

We completed more than 150 schemes to reduce the risk of sewer flooding for 256 properties and cut the 'at risk register' from 365 to 265. However, the number of actual sewer flooding incidents increased from 319 to 392, in part as a result of last year's very wet summer. Despite the wet summer all but one of the 81 EU designated beaches around the coast of Wales passed the mandatory standard for coastal water quality, and for the 2009 summer season Wales has secured 43 Blue Flags, over a third of the total awarded to the UK, and 42 Green Coast beach awards.

Independent research showed that around 80% of our customers are satisfied with the service they get from Welsh Water. Further research carried out for Ofwat and others for the regulatory price review confirmed this high score and also showed that 78% of our customers felt that Welsh Water provides good value for money.

However, the number of written customer complaints did increase last year and we judge that around half of these are avoidable. In order to tackle some of the main causes of complaints we are at the implementation stage of a £90 million programme of 'IT-enabled change' to replace ageing systems and processes and allow us to respond more quickly and efficiently to customer jobs and enquiries.

Our Final Business Plan was submitted to Ofwat ahead of the current regulatory review which, in December 2009, will set prices and other targets for the next 5 years. Our Plan will deliver good progress towards the goals included in "Our Sustainable Future" – a document which sets out our vision for the water industry in Wales over the next 25 years. Our objective is to make sure, as far as possible, that what we do in the coming years delivers the optimal balance of benefits and costs for all our customers and for the environment – including reductions of 50% in our carbon footprint.

The water industry faces big challenges. In the immediate future we have to do all we can to help our customers afford the essential public service of safe drinking water and sanitation. Financing efficiency is the key to achieving this objective, by making sure investors regard the water industry in Wales as a 'safe home' for long term, low risk funding. Notwithstanding the impact of the recession on our business, we have been able to maintain our net debt as a percentage of regulatory asset value at 72%, down from the 93% when we acquired Welsh Water in 2001, and our credit ratings have risen to be amongst the best in the sector.

Looking further ahead, the water industry is on the 'front line' in dealing with the expected consequences of climate change, with the prospect of drier summers and more frequent severe storms throughout the year. So that it can meet these new challenges, government

and regulators are currently reviewing the structure of the industry and considering the possibility of breaking it up into competing 'for-profit' entities.

This is of particular concern for us since Glas Cymru's 'not-for-profit' structure is unique in the UK's water industry. It has allowed all our financial surpluses and efficiency savings to be reinvested in the Company for the benefit of our customers and has made it possible for us to introduce the 'customer dividend', helping to make this most essential public service as affordable as possible.

We are proud of the ethos of trusteeship and public service that the Glas Cymru structure is designed to safeguard. Nothing is more vital to public health than the secure delivery of safe drinking water and effective means of dealing with wastewater. We judge that this responsibility is best met in Wales and the rest of our area by an integrated company operating within a consistent and transparent regulatory regime.

On behalf of the Board I would like to thank all the staff who work for us in this important industry, both in Welsh Water itself and with our contract partners. Their continuing commitment and enthusiasm is essential for our success in serving our customers, and the way in which they have responded to the many challenges throughout the year is truly appreciated.



Lord Burns, Chairman

Our only purpose is to look after the water industry in our region on behalf of both today's customers and future generations and to deliver high quality and reliable drinking water and sewerage services at an affordable price.

How we deliver services

The water industry in England and Wales - and the important public service it is responsible for - is highly regulated.

Ofwat is the economic regulator and is responsible for setting an upper limit on the price that each regulated water and sewerage company can charge its customers and for promoting the interests of customers by incentivising efficiency and high standards of service and penalising inefficiency and poor service. The industry operates on a 5 year asset management cycle and Welsh Water's settlement for the current 5 year period that ends in March 2010 assumes total investment of £1.4 billion financed in part by bills rising on average by no more than 3.6% annually in real terms. Welsh Water has mitigated the allowed increase in bills by paying a growing 'customer dividend'.

Each year Ofwat assesses companies' overall delivery of service to customers via their overall performance assessment (OPA). The assessment serves 2 purposes. Firstly, it enables comparisons of the quality of the overall service companies provide to customers - which is taken into account at each price review. And secondly it informs customers (and other interested parties) about the overall performance of their local water company. The assessment reflects the broad range of services provided to customers including: water supply; wastewater services; customer service; and environmental impact.

The Drinking Water Inspectorate monitors drinking water quality while the Environment Agency regulates

Welsh Water's environmental performance, specifically with regard to the way in which it abstracts water from rivers and reservoirs and then discharges wastewater after it has been cleaned. The Countryside Council for Wales and, in England, Natural England oversees Welsh Water's management of designated sites for nature conservation and how the Company meets its obligation to conserve and improve biodiversity.

The Consumer Council for Water is the independent body established to represent the interests of customers. It investigates complaints, addresses particular customer concerns and audits Welsh Water's performance on customer service more generally as well as influencing policy.

The Welsh Assembly Government has a key role in determining water and environmental quality standards as well as setting the framework for other public policy matters.

All aspects of Welsh Water's water and wastewater operations are subject to extensive performance monitoring against standards and targets set by regulators and government. Each year, regulators publish reports that assess and compare the performance of the regulated water companies across a wide range of measures, including water quality, environmental quality, customer service, affordability and cost efficiency. Each has powers that can sanction Welsh Water in the event that performance falls short of required standards.

Welsh Water meets many of its obligations as a regulated water and sewerage undertaker through contract partners. Under these outsourced contracts Welsh Water retains ultimate control of all activities carried out by contract partners appointed following competitive procurement.

The contracts operate on a transparent basis so that Welsh Water retains access to all staff, information and knowledge required to meet legal and regulatory obligations. Welsh Water determines asset strategy and retains responsibility for decisions on key assets.

In all, some 85% of Welsh Water's operating and investment expenditure is covered by these contracts which are specified to incentivise contract partners to deliver the best possible combination of quality of service and cost efficiency. Each contract specifies performance measures that reflect the quality and service standards by which Welsh Water's performance is judged and the contracts reward sector leading performance and penalise under performance.

① Each year we report on Welsh Water's performance against a range of performance measures covering water quality, environment, customer service, health and safety and financial aspects. From this wide range of measures the Board has identified 8 key performance indicators (KPIs) to measure the overall success of the business and the progress of its key strategies. These include strategies to deliver long term financing efficiency and improve customer service while always ensuring that everyone who works for the water industry in our region is able to return home safely at the end of each day.

Further information regarding the definition, purpose and target for the 8 KPIs can be found on page 26 of this report.

Key performance measures

Year to 31 March 2009	Monitoring plan target ⁽³⁾	Previous performance 2007-08	Actual performance 2008-09	At or better than previous year
Water quality				
Overall water quality compliance 'at the tap' ^{(1)(C)}	n/a	99.9%	99.9%	✓
(i) Bacteriological compliance 'at the tap' ^(C) (see page 6)	n/a	99.6%	99.8%	✓
Iron compliance 'at the tap' ^(C)	99/1%	99.5%	99.4%	×
Operational Performance Index ^(C)	n/a	99.7%	99.9%	✓
Operational Performance Index (TIM) ^{(2)(C)}	n/a	99.8%	99.8%	✓
Environment				
Leakage (m ³ /km/day)	7.5	7.5	7.2	✓
Number of 'category 1 and 2' pollution incidents ^(C)	n/a	9	3	✓
Number of 'category 3' pollution incidents ^(C)	n/a	260	230	✓
Wastewater treatment works assessed as complying with 'look up' table ^(C)	n/a	99.1%	100%	✓
Sewage sludge recycled satisfactorily ^(C)	100%	100%	100%	✓
'Mandatory' coastal bathing water compliance at EU designated bathing beaches ^(C)	100%	99%	99%	✓
'Guideline' coastal bathing water compliance at EU designated bathing beaches ^(C)	'Stable'	86%	77%	×
Customer service				
(i) Customer satisfaction (see page 12)	n/a	81%	80%	×
Properties 'at risk' of receiving low pressure	242	220	197	✓
Unplanned water supply interruptions	1,080	3,848	894	✓
Properties 'at risk' of sewer flooding	308	365	265	✓
Properties flooded due to hydraulic overload	106	78	106	×
Properties flooded due to other causes	120	167	186	×
Billing enquiries answered within 5 days	100%	100%	100%	✓
Written complaints answered within 10 days	99.9%	99.2%	99.3%	✓
Number of written complaints received	n/a	10,586	12,486	×
Customer meters read within year	99.9%	99.9%	99.9%	✓
Telephone calls abandoned	1.3%	2.9%	4.7%	×
Telephone calls receiving engaged tone	0%	0.4%	0.04%	✓
Call handling satisfaction (score out of 5)	n/a	4.61	4.65	✓
People				
(i) Reportable accidents (see page 14)	n/a	35	34	✓
Finance				
(i) Bond credit rating ⁽⁴⁾ (see page 18)	n/a	Class B bonds A/A3/A		✓
(i) Customer dividend (see page 18)	n/a	£21	£22	✓
(i) Gearing (see page 20)	n/a	72%	72%	✓
(i) Interest cover (see page 21)	n/a	3.3	3.4	✓
Overall performance				
(i) Ofwat's OPA score (see page 4)	n/a	394	406 estimated	✓

(1) This measure is based on 'Mean Zonal Compliance'.

(2) Incorporates performance against turbidity, iron and manganese.

(3) 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.

(4) Standard & Poor's, Moody's and Fitch respectively.

(C) Calendar year 2008 all other figures are for the year ended 31 March 2009.

Our biggest responsibility is to protect public health by providing a safe and reliable drinking water supply to our customers at all times. This means that our tap water must be free from harmful chemicals and bacteria and have an acceptable taste.

Drinking water supply

We employ 67 water treatment works to supply on average 850 million litres of water a day to 1.2 million households and over 100,000 business customers through a network of 557 service reservoirs and over 27,000km of water mains.

Drinking water quality

Last year, in line with water industry regulations, we carried out almost 300,000 tests of water quality at all stages in our water supply system, from the treatment works to the customer tap. We test the quality of tap water against parameters for 39 health based standards that are derived from European Directives and national legislation and our compliance is regulated by the Drinking Water Inspectorate. This programme of random testing provides a good picture of the quality of the tap water we supply to our customers.

In 2008, the high quality of drinking water supplied to our customers was maintained overall. Bacteriological compliance at the tap improved to 99.77% (2007: 99.60%) while Mean Zonal Compliance was better with 99.95% of tests meeting the required standards (2007: 99.93%). On the Operational Performance Index our performance improved to 99.89% (2007: 99.71%) while performance on the Water Distribution Index was 99.83% (2007: 99.84%).

This year we will complete a £420 million 10 year programme to renew or refurbish over 4,000km of unlined iron water mains. This programme has significantly improved iron compliance at the tap and will extend the life of our water mains network.

Customer contacts are another measure of customer confidence in their tap water. Last year we reduced the number of contacts from 5 to 4.5 per 1,000 customers, which is closer to the 2007 industry average of 2.6.

Counting against this generally improving performance was the fact that we experienced 22 water quality 'incidents', up from the 16 in 2007. 2 of the 2008 'incidents' concerned precautionary Boil Water Notices affecting 50,000 customers in north Wales.

Last September, our routine sampling detected elevated levels of cryptosporidium in the source reservoir water for our Mynydd Llandygai water treatment works in Gwynedd, and in order to protect public health we issued a precautionary Boil Water Notice to some 45,000 household and business customers. We were able to lift this Notice after installing ultra violet treatment at Mynydd Llandygai and the £9 million scheme to add a coagulation treatment stage to this water treatment works is now progressing.

We also issued precautionary Boil Water Notice to 5,000 customers in Tywyn and Aberdyfi supplied by our Penybont water treatment works which lasted 4 days and followed an 8 hour period where the ultra violet treatment was unable to operate because of very wet weather. The £6 million scheme to upgrade Penybont water treatment works, which was on site at the time of this incident, was completed in December.

In recent years we have witnessed a gradual deterioration in the quality of the raw water we abstract for public water supply, possibly as a result of climate change, and this has challenged a number of our water treatment works, particularly those with relatively simple treatment like Mynydd Llandygai and Penybont. This fact, combined with a re-assessment of the risk posed to public health by even very low levels of cryptosporidium in drinking water, led the Board to decide to bring forward investment to add an additional or enhanced stage of treatment to 9 of our mostly smaller water treatment works, most of which are in north Wales where source water is generally of very high quality. The overall programme will cost £200 million and pending its completion by 2015 we have installed ultra violet treatment to protect against the risk posed by cryptosporidium.

In April this year we issued another precautionary Boil Water Notice to 70,000 customers in north east Wales supplied by our Alwen water treatment works. This followed evidence of bacteriological contamination in routine testing carried out at the treatment works. All testing downstream of the works was clear and the precautionary Notice was lifted after 6 days. Alwen water treatment works is 20 years old and a major £14 million refurbishment scheme is being accelerated and work will start on site during the course of this year. In the meantime, the disinfection process employed at Alwen has been bolstered.

Drinking Water Safety Plans

A priority in 2008 was the development of a Drinking Water Safety Plan for each of Welsh Water's 22 water supply zones. This has involved a detailed re-assessment of all potential risks to water supply and public health at all stages in the water supply chain – from catchment source, through the treatment stage, storage and distribution network to the customers' taps.

Public Health Partnership for Wales

This forum of water companies, regulators, local authorities, health authorities and public health experts meets regularly to improve working relationships and to achieve good management of water quality events so that public health is protected at all times.

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 work. Last year 894 properties suffered unplanned interruptions to supply lasting more

than 6 hours, compared with 3,848 in the previous year when severe summer flooding inundated our Whitbourne water treatment works. 411 properties suffered interruptions to supply lasting more than 12 hours.

In January, the freezing weather followed by a rapid thaw had a significant impact on our operations, with burst rates more than doubling in some areas. We had particular problems in the Rhondda where the freezing weather stripped manganese deposits from the raw water mains serving our Maerdy water treatment works, blocking the filters and causing intermittent supply interruptions to 7,000 customers.

A scheme to renew the raw water main will be completed by the end of this year.

We also monitor water pressure at the tap in each water distribution zone. Incidence of low pressure problems can change as new properties are connected to the water supply network or as a result of network re-configuration. Last year we dealt with possible low pressure problems for over 170 properties and at the end of the year there were 197 properties still at risk of having low pressure, a performance that keeps Welsh Water at or near the top of the industry league table for this measure.

99.95%

overall water quality compliance.

£200 million

to be investment in water treatment works.

4,000km

of unlined iron mains renewed in 10 years.

Water investment in the year	Spend £m
Water treatment works AMP4	25
Water treatment works AMP5	7
Water mains refurbishment	51
Meter installation	5
Leakage	5
New development	5
Maintenance	60
Other	20
Total	178

It is our responsibility to collect and treat our customers' wastewater – together, in many places, with highway and surface drainage that drains into the public sewer network – in a way that protects public health and safeguards the environment.

Safeguarding the environment today

We employ over 800 treatment works which treat wastewater collected by our 19,000km sewer network which has over 1,900 pumping stations and 3,200 combined sewer overflows. Because of our topography, we employ more assets per customer than elsewhere and our wastewater operations are characterised by an extensive network of relatively small assets. We collect for treatment some 5% of the industry's total wastewater flow yet operate 13% of its treatment works.

As a result of investment of more than £2 billion over the last 15 years or so, Wales now has some of the highest quality rivers and coastal waters in the British Isles and while we are proud of the part Welsh Water has played in securing this outcome we are just as mindful of the important job Welsh Water has to do to maintain this high quality environment.

As with drinking water, the importance of effective sewerage and wastewater treatment for public health means that Welsh Water's wastewater activities are tightly regulated. Much of what we do is governed by statutory requirements and our compliance with these is monitored by the Environment Agency. We manage the business against a range of regulatory and other measures of performance which together ensure the quality and reliability of service received by our customers and our compliance with environment standards.

Wastewater treatment compliance

All of Welsh Water's wastewater treatment works have discharge consents which are regulated by the Environment Agency. Just over 550 of our works have numeric consents where the treated water discharge is sampled over the course of the year and tested against a number of parameters, typically including biological oxygen demand, suspended solids and ammonia.

In 2008, for the first time in more than 10 years, all of Welsh Water's customers were served by wastewater treatment works that complied with their 'look-up' discharge consents. The number of works 'at risk' of failing also fell during 2008.

Reliability of sewer network

Ensuring that our sewerage network operates so that the environment is protected from pollution is one of our biggest challenges. The average age of Welsh Water's sewers is 60 years and around a third is more than 100 years old. Last year we dealt with 541 sewer collapses which remains one of the highest rates of asset breakdown in the industry.

Our sewer network was 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 or pollution incidents. We measure the risk of repeat flooding from hydraulically overloaded sewers and we also report actual sewer flooding

incidents and whether these have been caused by hydraulic overload or as a result of another cause, such as blockages or sewer collapse.

Last year we invested over £20 million on more than 150 schemes across our region to reduce the risk of repeat flooding from overloaded sewers for 131 properties, and as a result the number of properties still at risk of repeat flooding following very heavy rainfall was reduced from 365 to 265 at the year end. Flooding from sewers is the most serious service shortfall and is especially hazardous to public health, and continuing to reduce both the number of incidents and the number of properties at risk of repeat flooding from sewers is a high priority for Welsh Water.

We reduced the number of serious pollution incidents caused by breakdown or other problems on our sewer network to just 3 in 2008, down from 9 in 2007 and 17 in 2006. In addition, we reduced the number of less serious pollution incidents by 9%. Some 32% of all pollution incidents were 'self reported' by Welsh Water, up from 6% in 2007.

In part, this improvement in performance is due to the installation of 620 Hawkeye telemetry units on the sewerage network. Last year these units alarmed on average over 40 times a month which allowed staff to attend before there was a spillage and this pre-emptive action prevented more than 100 pollution incidents in 2008.

Coastal and river water quality

Welsh Water has one of the longest coastlines of any water and sewerage company in the sector. Having high quality coastal water quality is especially important for the Welsh tourism industry which employs 8% of the Welsh workforce and contributes £3 billion a year to Welsh economy.

Despite last year's very wet summer 80 of the 81 EU designated popular beaches passed the mandatory bathing water standard and 62 passed the much higher guideline standard. These results helped secure 43 Blue Flag beach and marina awards for the 2009 season, which once again means that Wales secured more than one third of the total number of Blue Flags awarded to the UK. In addition, Wales secured 42 Green Coast awards for rural beaches.

The quality of rivers in Wales continues to be amongst the best in the UK. The latest survey of river water quality published by the Environment Agency confirmed that over 95% of rivers in Wales were good

or excellent on the assessment for chemical quality and over 87% were good or excellent on the assessment for biological quality.

Water abstraction and leakage

In Wales we abstract for public water supply just 3% of effective rainfall compared with over 50% in parts of the south east of England. Moreover, in the last 10 years we have reduced our abstractions by a quarter as a result of halving leakage from our water supply network and falling demand for water from heavy industry.

Because of the big increase in bursts following the prolonged freezing weather in December and January, leakage increased sharply. During the first 2 weeks of January we completed over 1,000 repairs on our water supply network, compared to around 1,500 repairs in December. But by reallocating resources and by 7 day working, we were able to tackle the backlog of leaks on our water supply system and achieve the Ofwat target for leakage of 195MI/d.

£2 billion

invested over last 15 years.

43

blue flag beaches and marinas.

100%

compliant wastewater treatment works.

Wastewater investment in the year	Spend £m
Wastewater treatment works improvement	14
Combined sewer overflows	48
First time sewerage provision	3
Sewer flooding prevention	23
Sewerage maintenance	16
Wastewater asset maintenance	27
Sludge development	9
New development	6
Other	18
Total	164

As the provider of essential water and sewerage services our activities can have a significant impact on the environment. We aim to safeguard the environment by operating in a sustainable way and where an impact is unavoidable, in a way that mitigates any adverse environmental impact.

Safeguarding the environment for tomorrow

Managing water resources

We are committed to ensuring that in the future there will be sufficient water to meet the requirements of our customers. Our 25 year water resource strategy, a draft of which was published for consultation in January 2009, shows our plans for managing water resources across our supply area and maintaining the balance between supply and demand. In preparing this plan we have had to consider all the factors which could potentially impact upon either the availability of our supplies, or the demands made on our resources. This includes forecast changes in population and the amount of water we all use, the effects of climate change and changing legislation that may lead to us abstracting less water from the rivers in Wales. Although we have a relatively strong water resource position, through this process we have identified deficit zones where demand is exceeding (or forecast to exceed) supply and identified solutions to either increase supplies or to manage demand. This is complicated by the fact that Welsh Water has nearly half the industry's discreet water resource zones, which limits our ability to transfer water from one area to another and can create local supply problems during droughts and other extreme weather conditions.

We place a strong emphasis on managing water abstraction and leakage and on water efficiency, and we are working to both mitigate the expected

impact of climate change on our industry as well as reduce Welsh Water's carbon footprint.

Water efficiency

Promoting water efficiency is essential to encourage our customers to use water wisely and avoid waste in the interests of both our environment and customers generally. Small measures to save water can, when aggregated, help manage the effects of climate change and help to contain any increase in water consumption.

We promote water efficiency through our 'Be Waterwise' campaign, where our core message is: 'use as much drinking water as you need, but please don't waste it'. Under this campaign we provide customers with free water saving devices (cistern hippo-bags) and information via our website and publications on how to save water in the home and the garden. Last year, we also took to the road with a programme of road shows around our region, and promoted a 'Green plumbers of Wales' scheme, under which 60 plumbers passed a pilot module of plumbing training, which focuses on best practice in the installation and maintenance of water efficiency plumbing equipment.

Climate change and carbon emissions

Treating and transporting water and wastewater across a large region of variable terrain makes Welsh Water one of the top energy users and, therefore, carbon emitters in Wales. Each year there

is an upward pressure on energy use arising from investment in new assets and treatment processes to meet higher water quality and environmental standards. On top of this, in the past 3 years we have seen a much greater variability in weather conditions, and more extreme weather events, which may, or may not, be attributable to climate change, but are having a significant impact on the operation of Welsh Water's business.

Given this challenging operational environment, it is pleasing to report that in 2008-09 Welsh Water's carbon emissions fell slightly to some 252,000 tonnes of CO₂ equivalent (tCO₂) as measured under the DEFRA Guidelines 2007. This makes progress to meeting our carbon reduction target of 25% by 2015, as set out in "Welsh Water: Our Sustainable Future", which we published in 2007.

Energy management

80% of Welsh Water's carbon emissions relate to energy use so control of energy costs has both financial and environmental benefits. Last year energy use fell by around 3%, which is a good outcome in a year of difficult operating circumstances. We achieved this by close monitoring of the operational and energy efficiency of plant, especially pump efficiency as 70-80% of all energy use relates to our pumping water and wastewater. The replacement of inefficient pumps can deliver energy savings of up to 20%. Following a review of the aeration process at Cardiff wastewater treatment works, which identified energy savings of around 3.45Gwh, we are reviewing the application of aeration optimisation at a further 10 sites.

Last year Welsh Water generated 7.8Mwh of renewable energy, mainly from combined heat and power (CHP) schemes, which capture and burn 'waste' methane gas at 11 wastewater treatment works, which is some 22% more than in 2007-08. This excludes, however, over 30,000Mwh of hydro renewable energy generated

by third parties at Welsh Water sites under commercial leases that predate Glas Cymru's ownership of Welsh Water.

The renewable energy we generate will increase further by 2011 as we are investing £70 million to install advanced sludge digestion schemes at 3 wastewater treatment works, which will generate a further 7Mwh of green energy. This would save over 30,000tCO₂ of emissions and make a significant contribution to achieving our carbon reduction targets. A scheme at Eign in Herefordshire is being installed currently, and planning is advanced for similar schemes at our Cardiff and Afan works. Our sludge strategy will

3%

reduction in energy use.

also increase renewable capacity at our Five Fords works near Wrexham and see the decommissioning of less efficient digestion units at other sites.

Recycling waste

Each year Welsh Water uses some 120,000 tonnes of aggregate and needs to dispose of around 85,000 tonnes of construction waste. With our contract partners, Welsh Water has signed up to the government sponsored WRAP Utility Industry Agreement, which promotes good practice to minimise the unnecessary use of virgin aggregate resources and the deposit of construction waste to landfill. Recycling of construction waste and use of secondary aggregate has been

22%

increase in renewable energy generation.

established practice at major construction schemes for many years, but in 2008 we established a recycling hub at Merlins Bridge wastewater treatment works to explore the opportunity for reprocessing construction wastes from a number of smaller investment schemes in the Haverfordwest and Milford Haven area. This small trial resulted in reduced lorry journeys and avoided over 1,000 tonnes of excavated waste being deposited to landfill saving some 8tCO₂ in emissions, and the benefits of this regional approach are now being applied more widely.

£70 million

to be invested in advanced sludge digestion.

Further details on how we safeguard the environment are published in the "2009 Report of the Quality and Environment Committee", which is available on request or via our website.

We have over 1.2 million household customers and over 100,000 business customers and we want them all to feel confident that their water supply and sewerage services are well looked after. Our aim is to get things right first time, every time, and give our customers a prompt, courteous response every time they contact us.

Meeting customers' expectations

Improving customer service

We are nearing completion of a 3 year programme to update a number of key IT systems and working practices so that we can give our customers a much better day to day service. This involves an enormous commitment of resources and the total cost of the programme is £90 million. When it is fully rolled out all our front line staff will have more real time information available to them. This will mean we can give customers more accurate information and deal with their queries and problems more quickly.

Customer contact

The majority of our customers prefer to contact us by telephone and we continue to answer calls with a 'real person' straightaway, only using automation in emergencies. Last year we dealt with 1.2 million customer calls - slightly fewer than in the previous year. Over 75% of the calls we get are from customers wanting to pay their bill or who have a query about their bill or payment plan. We also received nearly 132,000 written queries about bills and payment options and we responded to 99.99% of these within 5 working days.

Only 0.04% of all calls coming into our contact centre got an engaged tone because all staff were already busy on another call. However, nearly 5% of all calls were abandoned, which is up from the previous year when less than 3% of calls were abandoned. This dip in performance was mainly due to unexpected changes to the pattern of calls and calls taking longer to deal with.

We have also experienced more customers contacting us as a result of the current difficult economic climate.

The quality of the response we give our customers is of great importance and calls to our contact centres are recorded to ensure high standards are met and to direct training as required.

All our customer publications are bilingual and we have a dedicated Welsh language telephone line for those customers who prefer to speak to us in Welsh. Last year there were some 39,000 calls to our Welsh language line.

Helping customers pay their bill

We have added a new assistance tariff called Welsh Water Assist to help household customers on low incomes and particular needs which caps the bill at £250. We estimate that around 9,000 customers can benefit from this tariff. Around 12,500 customers have already taken advantage of our other assistance tariff - Water Direct which reduces the bill by £25 when a customer opts to pay their water bill by direct deduction from benefits.

To date, 2,500 customers have benefited from our Customer Assistance Fund, run with the help of the Citizens Advice Bureau to help customers who have fallen into arrears with their bills. The value of this help had reached £2 million by the year end. All our assistance tariffs are designed to be self funding.

Additional Services

Some of our customers may have additional needs and we offer a range of additional services. These include large print or Braille bills, bottled water during emergencies, a password scheme for home visits and a 'knock and wait' service for those who need a little more time to answer the door. At the end of the year 3,600 customers were registered for one or more of these additional services.

Customer complaints

Last year we received 12,486 written complaints, 17% higher than the previous year. The number of written complaints received by email was 55% higher and email complaints now account for more than a quarter of all written complaints.

The biggest increase came from complaints about disputed consumption from metered household customers. 99.9% of metered customers received at least one bill last year based on an actual reading. We were unable to get a meter reading for just 419 customers out of 463,000 metered accounts.

We provided a substantive reply to 99.3% of these written complaints within 10 working days, which is marginally better than the previous year. We judge that around half of the complaints we get are 'avoidable' in that a customer has had to complain because we have not done what we promised to do or have not kept them informed.

Most of the remaining complaints are about disputed bills, charging policy or our debt recovery activities. Just under 5% of written complaints had to be escalated to a Director because a customer was not happy with our first reply.

Guaranteed Standards

We made 2,794 payments last year under the industry's Guaranteed Standards scheme at a total cost of some £200,000, most of which related to missed appointments.

Customer satisfaction

The industry regulator Ofwat carries out independent follow up research into customer satisfaction with call handling across the sector, and last year we scored 93% which is one of the best results in the industry and slightly better than the previous year's score. We carry out independent market research to track customer views and satisfaction levels on a range of issues and services, including satisfaction with drinking water quality, coastal environmental quality and how our customers judge Welsh Water's value for money when compared to other utilities. The latest research shows that satisfaction with drinking water quality remains high at 86%.

2,500

customers benefit from
Customer Assistance Fund.

As part of the regulatory review that will set price limits for the next 5 years, Ofwat carried out extensive customer research in all regions of the water industry in England and Wales. This research showed that not only did 93% of customers in our region support the plans and priorities put forward by Welsh Water, but 70% rated Welsh Water's current bill and service level as representing good value for money. Only one other company achieved a higher score on either count.

Following the precautionary Boil Water Notice we issued to some 45,000 customers in Gwynedd in September last year we carried out independent research to find out how well customers felt we

1.2 million

calls received.

had dealt with the problem and how the Boil Water Notice had affected their view of Welsh Water and the service we provide. The research showed that 79% of customer were 'satisfied' with the way we dealt with the boil notice, with 28% being 'very satisfied'. Furthermore, 81% of customers felt that their opinion of Welsh Water had not changed as a result of the boil notice and 86% felt they were well informed about what they needed to do as a result of the boil notice.

93%

of customers endorse
draft business plan.

We want everyone who works for the water industry in our region, either directly for Welsh Water or for 1 of our service partners, to recognise the importance of the job we do for the 3 million people who rely on Welsh Water.

Employer of choice

Welsh Water

The people directly employed by Welsh Water are principally responsible for financial management, strategic asset planning and investment, managing regulatory interfaces and ensuring outsourced working arrangements deliver an efficient and high quality service to Welsh Water's customers.

Our annual staff survey shows that 86% of Welsh Water staff understand the vital purpose of Welsh Water and their role in achieving this purpose, and 83% feel they accomplish something worthwhile at work. It also shows that 96% of staff regard Welsh Water as a good employer.

Every member of staff has a personal development plan which is reviewed annually to assess individual development and training needs. We keep staff informed about the company's performance and the challenges we face, through monthly team meetings and every quarter the Managing Director meets all staff in a series of briefings, where they can choose the topics to be discussed.

Last year we made a number of key appointments to strengthen our senior team, especially in the fields of water quality and asset strategy. In addition, 35 staff received management development training and we reintroduced our graduate recruitment programme to bring in potential leaders for the future, with skills in the engineering and scientific disciplines.

Senior managers mentor these individuals and over a 2 year programme they will be exposed to all key parts of the business. We have also strengthened our ties with a number of universities to enable us to attract strong candidates from the disciplines we most need.

Asset Management Alliance

The Welsh Water Asset Management Alliance (AMA) is a partnership between Welsh Water and 13 operational and capital contract partners which seeks to set new standards in partnership working. The overall approach we take is collaborative, with all parties working together to deliver a common set of business objectives. The AMA supports these objectives by ensuring a safe working environment for our staff, by focusing on continuous improvement in customer service standards, by being environmentally responsible and aware of the impact we can have on people and communities outside of the company.

Through our £90 million programme of IT enabled change we will fundamentally change the way we deliver services to customers and our levels of service. Last year some 1,200 staff received over 3,000 days of training on the new systems as we deployed mobile and 'tough book' technology to provide access to asset and customer data to staff in the field. 300 staff also received over 600 days training on new IT and business support systems.

We also increased the number of Welsh Water contract managers who hold a NEBOSH accredited health and safety qualification to 20, significantly strengthening our capability in this key area.

Each month we recognise excellence in customer service or operational performance and efficiency through an AMA award of employee and team of the month with the winners going forward to an annual awards celebration in Cardiff. In 2008-09 colleagues nominated 65 individuals and 71 teams for these awards.

Health and safety

The health, safety and welfare of our staff is of the utmost importance, so it is pleasing to report a further reduction in the number of reportable accidents, especially as last year we delivered our largest ever annual capital investment programme, and the average size of the workforce last year was significantly higher.

In 2008-09 there were 34 reportable accidents which is 1 less than the previous year, and some 26% lower than 2 years ago. Our service partners delivered 150 risk based initiatives and we launched a new occupational health nurse service, part of promoting awareness of good occupational health practice across the AMA.

Over the past 5 years the level of near hit reporting (i.e. an event that could have caused injury to staff but which did not on this occasion) has more than doubled. This provides important learning for our 'Journey to Zero' strategy and reflects positively on the no blame safety culture we have established across the AMA.

All contract partners are independently audited by Connaught Limited, at least once every 2 years. This tests compliance with the 2007 CDM (Construction, Design and Management) Regulations, the delivery of improvement plans, and the quality of accident reporting and investigation and occupational health service provision. 8 partners were audited last year, but all partners were involved in a programme of 47 cross-partner AMA audits. Connaught have confirmed that our contract partners work to some of the best safety standards they had encountered both inside and outside of our industry, with some in the top 10% of companies they have audited.

This contributed to our achieving certification to the OHSAS 18001:2007 international standard for occupational health and safety management with an extended scope of service for work relating to the 'business and administration of strategic management of waters service provision, including contract management'. This certification encompasses all activities undertaken in the AMA and was achieved in February 2009, just 11 months after we secured certification to the earlier 2001 standard for Welsh Water's own health and safety management arrangements.

Further details of our health and safety performance and approach are available in our "2009 Health and Safety Report" which is available on our website.

26%

reduction in reportable accidents over last 2 years.

£90 million

I.T. investment.

20 managers

hold NEBOSH accreditation.

We have a clear and firm commitment to environmental responsibility and in being a good neighbour and trusted partner in the communities we serve.

Responsible business

Minimising the impact of our activities

We cannot deliver essential water and sewerage services, or complete an annual investment programme of more than £300 million a year, without having an impact on the community. We have to dig up roads to lay and refurbish pipes, and we add to the volume of heavy traffic on our roads as materials are delivered to construction sites and waste is removed. But we always look to minimise the disruptive impact of our activities. This has been recognised with a number of our schemes securing a national 'considerate construction scheme' award, under which construction sites are independently audited for the effectiveness of its public safety and community impact and liaison arrangements.

Supporting education

In the last academic year around 18,000 children took part in education activities under our Living and Learning With Water programme, almost 14,000 of who visited 1 of our 4 environmental education centres. This service is provided free of charge and is designed and delivered by qualified teachers, which ensures that the service meets the changing needs of the national curriculum and is relevant to schools. Since our first centre opened in 1997 over 100,000 children have visited 1 of our education centres.

Our education website (www.livingandlearningwithwater.com), provides materials and information to support teachers in the classroom and explains the way we work with our 'Education Partners': the National Botanic Garden of Wales, Techniquest in Cardiff, the Hereford Waterworks Museum, The National Wetlands Centre - Llanelli, the Elan Valley Trust, and Keep Wales Tidy (Eco-Schools).

Our education programme also plays a central role in communicating key messages on water conservation and public safety into the wider community. 2 years ago we employed a peripatetic teacher to make our service more accessible to schools and community groups unable to visit one of our centres. In the last academic year this service delivered 135 community based sessions, reaching an additional 1,100 young people and over 260 adult learners. It also delivered key messages to nearly 2,000 participants in water theme weeks at our education partner sites.

Working with Eco-Schools we sponsor a water efficiency award for schools, we have issued over 820 water efficiency packs and around 1,630 schools receive advice from us through the Eco-Schools handbook.

Controlled trials at 18 schools in north Wales, in an area where there is little surplus water, has shown that by involving schoolchildren in water efficiency measures and adopting water efficient devices, both primary and secondary schools can reduce metered consumption by between 20% and 40%.

Managing our community assets

Welsh Water owns over 40,000 hectares of land and is custodian of some of the most scenic areas of Wales, which is rich in both biodiversity and heritage and provides significant opportunity for public recreation. We recognise that we have a duty to manage this 'national asset' responsibly.

Each year almost a million people visit one of the 17 major reservoir sites at which we provide a variety of sporting, recreational and leisure resources. This encourages public health and well being, but also makes a valuable contribution to tourism and the local economy. Last year the visitor centre at Llyn Brenig remained open over the winter months, doubling the number of winter visitors to this site to 80,000. Learning from this successful trial will be extended to other locations where there is sufficient visitor demand.

In addition to facilities for recreational and competition fishing, including facilities for disabled anglers, our reservoir programmes offer guided walks, bird and other species watching safaris, and wildlife boat trips. At designated sites we also provide facilities for individuals who wish to sail or canoe, both through organised clubs and privately.

We encourage conservation best practice across the business. Our major reservoirs have a site specific habitat and species plan, we support the delivery of biodiversity action plans of local authorities and we provide habitats surveys, data and information to the Welsh Biodiversity Local Record Centres. We also work with the Countryside Council for Wales's environmental and wildlife crime officers to provide training for our staff and to promote wildlife crime awareness.

Last year we also signed a memorandum of understanding with the 4 Welsh archaeological trusts to provide a framework for how we will work together to protect our archaeological heritage.

100,000

children visited
education centres.

Supporting community projects

We do not engage in corporate sponsorship. Instead we focus on supporting staff in community schemes. Many Welsh Water staff contribute to a 'World of Work' scheme which provide business mentoring and interview support for young people about to leave school. Participants in our management development programme also take part in a volunteer project to enhance skills learned on the course and help the community. In one recent challenge 12 middle managers spent 2 days working with a social enterprise body that provides outdoor training for groups of 16-18 year old excluded youths.

1,000,000

visitors to 17 major
reservoir sites.

WaterAid

We support WaterAid, the international charity, which brings sustainable water and sanitation schemes and hygiene education to some of the world's poorest communities in Africa and Asia. Last year, we sponsored our peripatetic teacher to visit Africa to see first hand how donations from Wales were benefiting poor communities, and learning from this has been used to refresh the global citizenship aspect of our education service. This was the third in a series of annual visits by Welsh Water staff.

£150 million

raised for WaterAid.

While Glas Cymru has not been immune to the impact of the severe economic recession, we have delivered a sound financial performance during the year to 31 March 2009. It has been a year of continued investment and our ongoing commitment to the 'customer dividend' has helped customers to cope during the downturn.

Financial review

Appointed revenue has grown due to regulatory price increases which support our extensive capital investment and the delivery of better customer service. Despite the impact on operating profits of reduced demand and higher operational expenditure, we increased the 'customer dividend' in the year to £21 per customer.

Capital investment in our regulated water and wastewater operations including infrastructure renewals expenditure ('IRE') amounted to £355 million during the year. This is 18% higher than last year, and represents a record level of investment spend for Glas Cymru.

The group has a strong liquidity position, with capital investment pre-funded through to 31 March 2010. This was enhanced recently by the signing of a £100 million loan facility with the European Investment Bank and a £60 million finance lease with HSBC. In spite of the impact of the recession and these additional borrowings, gearing has been maintained at 72% which sustains continued access to capital markets.

Revenue

Glas Cymru's turnover in the year to 31 March 2009 was £657 million (2008: £623 million), an increase of 5.5% on last year. This increase primarily reflects the price increase of 7.6%, however our 'customer dividend' policy means that our total charges in the year were some £27 million lower than if we had applied the full price increase determined by Ofwat (2008: £26 million lower). Additional revenue from new

customers has been offset by household customers switching to metered charging. The impact of reduced consumption amounts to £3 million, with demand from our business customers down some 3%.

During the year we introduced a new tariff - Welsh Water Assist - broadening our existing range of assistance tariffs to help support customers who have difficulty paying their water bills.

Operational expenditure

Glas Cymru's total operating costs (excluding IRE and depreciation) were £267 million (2008: £234 million), representing an increase in real terms of some 11% due to higher power costs and an increase in the provision for bad debts.

Around two thirds of operating costs relate to outsourced service contracts. Our major contracts are with United Utilities Operating Services (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 include a target cost mechanism aimed at enhancing operating efficiency to the end of the current regulatory period in 2010.

All water and sewerage companies need to draw on significant energy resources, particularly for water treatment and pumping processes, and Welsh Water - with its network spread across Wales's undulating topography - is no exception. This year we have experienced increases in energy prices which have driven power

costs up by over 40% to £42 million (2008: £29 million). Improved working practices and investment in energy efficient schemes can only partly offset price increases, and, under the target cost arrangements, the residual upward cost pressures are not borne in full by our service partners.

Customer debt recovery continues to be a high priority for Welsh Water and our billing and income contract partner, Veolia Water. In a challenging economic environment, in which water companies have no sanction to disconnect supplies to non-paying domestic customers, cash collection performance has deteriorated somewhat. The bad debt charge for the year of £19 million (2008: £13 million) represents around 3% of annual turnover (2008: 2%), and reflects an increase in the provision based on a review of historical collections and having regard to the deterioration experienced towards the end of the year.

Investment income and finance expense

Reported net interest payable of £166 million is £7 million higher than last year - the impact of lower interest rates has been offset by a higher indexation charge in respect of the index-linked bonds (calculated using July 2007 to July 2008 RPI). The average cost of debt during the period was 6.6% (2008: 6.3%).

In response to the crisis in the banking markets, the Company has tightened its criteria for investing cash deposits, such that maximum deposits with any single counterparty are reduced and the maximum term limited to 1 month. Consequently, the average interest receivable rate has fallen (from 6.0% to 3.9%) further than the average 3 month LIBOR over the same period (from 6.1% to 4.4%).

Glas Cymru has a number of swap contracts and, while these are effective commercial hedges, they do not qualify for hedge accounting under IAS 39.

Although there is no impact on cash flows, there is increased volatility in the income statement and fair value losses in 2008-09 are significantly higher than last year as tumultuous markets throughout 2008-09 have led to daily variances in interest rate expectations. This has resulted in a total liability of £158 million in the balance sheet but, assuming that the swaps are held to maturity, this will ultimately reduce to nil.

Loss before taxation

Excluding fair value movements, the loss before taxation was £11 million (2008: profit before taxation of £11 million). This loss was made after funding the 'customer dividend' of £21 for all

customers receiving both water and wastewater services, at a total of £27 million (2008: £20 per customer, totalling £26 million). Bills for the current year have been reduced by a higher dividend of £22 per customer.

Taxation

The taxation charge for 2008-09 will have no impact on cash flows and is primarily the effect of a deferred tax credit at 28% of the loss before taxation for the year, offset by a £37 million charge following the abolition of Industrial Buildings Allowances.

Liquidity

Glas Cymru aims to offer a secure, low risk investment to long term investors. By building and maintaining a strong financial position, we aim to keep our borrowing costs low, enabling us to finance future investment in the business efficiently, whilst retaining the scope to return money to our customers and keep bills affordable through our progressive 'customer dividend' policy.

£355 million

largest ever annual capital investment programme.

£21

'customer dividend' for every customer in 2008-09.

£1 billion

'customer equity'.

Net debt and reserves

As at 31 March	2009 £m	2008 £m
Regulatory Capital Value (RCV)	3,626	3,529
Net debt	(2,625)	(2,531)
'Reserves' RCV less net debt)	1,001	998
Gearing (net debt/RCV)		
Senior debt	69%	68%
Senior debt + class C bonds	72%	72%
Total debt	72%	72%

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	129	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.dwrcymru.com

* Swapped to an effective index-linked rate of 1.35%.

Credit ratings of Glas Cymru bonds

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

The ratings of the Class A bonds, which have the benefit of a financial guarantee from MBIA, are the higher of the underlying ratings of these bonds (A3/A/A) and the ratings of MBIA (B3/BBB+/-).

In addition to cash generated from ongoing business operations, Welsh Water has undrawn committed liquidity facilities of £420 million (2008: £345 million). £305 million relates to a committed syndicated revolving credit facility available to be drawn until 30 September 2011. There is also a bilateral facility of £40 million available to be drawn until 30 June 2012, and the balance of £75 million on the European Investment Bank loan facility (see below). In view of the high level of liquidity totalling £559 million (2008: £469 million), the business has not raised further bond finance during the year.

Gearing and financial reserves

On Glas Cymru's acquisition of Welsh Water in May 2001, gearing stood at 93%. Since then, its financial position has improved steadily, such that gearing had fallen to 72% as at 31 March 2009 and 'financial reserves' (RCV less net debt) had reached £1 billion for the first time.

Credit ratings and bond spreads

Glas Cymru's listed bonds have continued to be valued at wide spreads over Government gilts as a consequence of the difficult conditions in the banking and capital markets. However, this has typically been at margins below those of many equivalent water sector bonds of similar maturities.

The continued strong credit quality of the business is reflected in stable credit ratings, which are amongst the highest in the water sector.

Debt financing and interest rate management

Despite very difficult conditions in the borrowing and capital markets, Glas Cymru has raised £100 million additional finance from the European Investment Bank during the year to help fund its current five year AMP4 capital investment programme to 2010. £25 million of this facility was drawn on 15 December 2008, while the remaining £75 million remains available to be drawn until 22 April 2010.

On 27 March 2009, Welsh Water secured a further £60 million via a long funding lease of plant and equipment with a leasing subsidiary of HSBC Bank plc which will be repaid over the period to March 2017.

To protect Glas Cymru's high credit quality, the Board has always adopted prudent financial policies, predominantly covering the fixing of interest rates and the investment of cash balances. Glas Cymru's policy is to minimise its exposure to movements in market rates, with a minimum of 85% of its liabilities being fixed rate, index-linked to the UK Retail Price Index ('RPI') or matched by cash balances. The Board considers that linking debt to UK RPI inflation is particularly appropriate, as Welsh Water's revenues and Regulatory Capital Value are also linked to RPI through the regulatory system operated by Ofwat. Implementation of the policies is delegated to a small team of specialists which operates to ensure that Welsh Water meets the requirements of its licence, and therefore undertakes no speculative trading. As at 31 March 2009, approximately 58% of gross debt was index-linked via bonds and derivatives (2008: 56%).

The expected maturity of the outstanding fixed rate and index-linked bonds ranges from 2011 to 2057, with not more than 20% falling due in any 2 year period, in accordance with our refinancing policy.

Capital investment

Glas Cymru's strong financial position has been built up over the last 7 years, and provides a stable base from which it can respond positively to the challenges of the current economic recession and drive forward its largest ever capital programme. Nearly £1.2 billion has been invested since April 2005, bringing high value and long term improvements to customer service, drinking water quality and the environment.

Total capital expenditure by Welsh Water during the year (including IRE) was £355 million (2008: £301 million), bringing the total expenditure over the first 4 years of the 5 year AMP4 period to £1,162 million, some 77% of the total AMP4 programme. Welsh Water works with an alliance of capital investment partners to deliver the investment programme at the best value for money for customers. In 2008-09, annual capital investment exceeded £350 million for the first time ever for Welsh Water, and building on this achievement Welsh Water is planning to invest a further £350 million to the end of the current AMP period in 2010.

Looking ahead

The Board's policy is to reduce gearing to around 70%, and maintain it at around this level. A key part of our strategy is to minimise customer bills in the long term and the Board judges that this level of gearing will enable the Company to efficiently fund the AMP5 investment programme which will run to 2015.

Welsh Water's published plan for the period 2010 to 2015 proposes a sustained high level of capital investment, including key projects to enhance the protection of drinking water quality, mitigate the worst impacts of sewer flooding, reduce the environmental impact of the business and improve customer service. All this is to be achieved with the average household customer's bill in 2015 being the same in real terms as it is today. According to Ofwat research, over 90% of Welsh Water's customers endorsed its draft business plan which was released last summer.

Achievement of our financial objectives is threatened mainly by upward cost pressures and the risk of RPI deflation. Welsh Water has sought to minimise the risk of cost increases by securing in advance the resources for a long-term programme of work, and by maximising the efficiency of programme design and working practices.

Disclaimer

This Report contains certain forward looking statements with respect to the future business 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.

72%

gearing - reduced
from 93% in 2001.

£1.7 billion

of finance raised since 2001.

A3

corporate family rating
from Moody's.

The water industry is a long term and capital intensive industry, and our job is to look after the water industry in the region served by Welsh Water on behalf of both today's customers and future generations. The decisions we make today on investment in our £19 billion network of assets will be felt for tens of years to come.

Planning for the future

Every 5 years Ofwat carries out a Periodic Price Review to set an upper limit on the amount water and sewerage companies can charge their customers. The last Review was completed in November 2004 and set prices for the 5 years 2005-10. The current Review will determine price limits for the 5 years 2010-15 and Ofwat will be making its 'Final Determination' in December 2009.

Customer bills and investment

In deciding what needs to be done in the years ahead, a balance has to be struck between affordability on the one hand and the quality and reliability of service on the other. The water industry everywhere is very capital intensive and Welsh Water employs a network of reservoirs, treatment works, pumping stations, and mains and sewers which has a replacement value of some £19 billion - around £15,000 per customer.

Much of what Welsh Water does day to day to deliver a high quality and reliable customer service involves operating and maintaining this large network of often very long life assets. Network performance is therefore key to the service we give our customers as well as our ability to protect the environment from pollution. It follows that the key trade-off is between affordability and investment in our network of assets.

Final Business Plan

Our Final Business Plan, published in April this year and submitted to Ofwat for the 2009 Periodic Price Review, sets out what we want to achieve over the coming 5 years.

Our goal is to make sure, as far as possible, that what we do in the coming years comprises the best possible package of outcomes and delivers a public service that our customers would accept as being good value for money.

It makes steady progress towards the goals set out in "Our Sustainable Future", published in 2007, which set out our long term vision for the water industry in our region.

- » **Protecting public health.** Our biggest responsibility is to provide a safe and reliable drinking water supply to our customers at all times. In the next 5 years we plan to undertake significant refurbishment and upgrade work at about a third of our water treatment works, including the installation of enhanced treatment to deal with deteriorating source water quality and other risks identified in our Drinking Water Safety Plans.
- » **Safeguarding the environment.** We are targeting zero serious pollution incidents and a significant reduction in minor incidents caused by breakdowns on our sewer network plus additional treatment stages at some 50 sites to protect river and coastal water quality.
- » **Responding to climate change.** By improving energy efficiency, including advanced sludge digestion at 3 sites, we are seeking methods to achieve a 25% reduction in our 'carbon footprint' by 2015. We will also complete a number of Sustainable Urban Drainage schemes to reduce the risk of flooding from overloaded sewers and added protection at some 15 critical sites most at risk of flooding.

- » **Meeting our customers' expectations.** By improving the reliability of our networks, reducing the risk of sewer flooding, tackling over 450 known and forecast problems, and using the latest technology to anticipate and therefore prevent service failures we will improve customer service by giving first time resolution to day to day problems.
- » **Looking after our assets.** We will use our Strategic Investment Planning System to prioritise and inform long term investment decisions and maintain our £19 billion network of long life assets.
- » **Financing the business.** We are targeting gearing at around 70% and an 'A grade' corporate rating, which we will achieve by further efficiencies in operating costs and in delivering a £1.4 billion investment programme.
- » **Employer of choice.** We will maintain a highly skilled team of people, committed to high quality customer care and looking after this long term industry for future generations.
- » **Affordability and value for money.** Affordability will always be a top priority for us and our Final Business Plan proposes that average household bills will be no higher in 2015 than today, having allowed for changes in RPI inflation.

AMP5 capital investment programme

Our Final Business Plan provides for investment over the AMP5 period 2010-15 of £1.4 billion, similar in scale to AMP4 investment in the 5 years 2005-10.

Highlights of our AMP5 investment programme include:

- » improved facilities at 23 water treatment sites to address risks to the quality of drinking water;
- » enhanced treatment at 14 wastewater sites to protect coastal water quality;
- » advanced sludge digestion at 3 sites to reduce energy costs and our carbon footprint;

- » renewal of over 500km of water mains which cause repeated interruptions to supply;
- » an initial programme to start to remove surface water from our sewer network
- » ongoing investment to reduce the number of sewer flooding incidents;
- » phase 2 of our IT enabled change programme to improve efficiency and customer service; and
- » new infrastructure to supply new housing and support economic development.

Asset maintenance represents nearly 70% of the planned AMP5 programme compared with just under 50% of the AMP4 programme.

Significant refurbishment and upgrade work at a third of our water treatment works.

Welsh Water employs assets with a value of some £19 billion and the planned AMP5 investment on maintenance is equivalent to less than 1% of this figure annually meaning that our network of assets will continue to get older over the AMP5 period 2010-15.

Impact on customer bills

By targeting further efficiencies in operating costs and by maintaining financing efficiency, our Final Business Plan shows that we can deliver the £1.4 billion AMP5 investment programme with average household bills moving broadly in line with inflation over the 5 years to 2015.

25% target reduction in our carbon footprint by 2015.

Welsh Water was the only regulated water and sewerage company to propose no real increase in average household bills in the period 2010-15.

Welsh Water's bill is still higher than the UK average bill, but only because Welsh Water, with its long coastline, employs more wastewater treatment assets per customer than most other companies. Moreover, average household incomes are lower in Wales than elsewhere. We have been able to mitigate this disadvantage through our growing 'customer dividend', and keeping our bills affordable in the years ahead, especially for our least well off customers, remains a key consideration in our plans.

Zero serious pollution incidents targeted.

Water supply (all in 2007-08 prices)

Functional area	AMP3	AMP4	AMP5
	2000-05 £m	2005-10 £m	2010-15 £m
Water resources and leakage	63	93	99
Water treatment	90	142	266
Water distribution	309	408	258
Business support	14	53	66
Total	476	696	689

Ofwat regulatory accounting	AMP3	AMP4	AMP5
	2000-05 £m	2005-10 £m	2010-15 £m
Maintaining base service	276	392	462
Enhanced service levels	0	0	6
Quality	150	408	258
Supply demand	50	52	83
Total	476	696	689

Sewerage and wastewater treatment (all in 2007-08 prices)

Functional area	AMP3	AMP4	AMP5
	2000-05 £m	2005-10 £m	2010-15 £m
Sewerage	414	411	251
Wastewater treatment	363	245	262
Biosolids	21	14	106
Business support	15	63	48
Total	813	733	667

Ofwat regulatory accounting	AMP3	AMP4	AMP5
	2000-05 £m	2005-10 £m	2010-15 £m
Maintaining base service	190	283	456
Enhanced service levels	42	67	41
Quality	565	335	97
Supply demand	16	48	73
Total	813	733	667

Glas Cymru cannot diversify into activities unrelated to those of a regulated water and sewerage business in the region served by Welsh Water, but otherwise we face the same risks as any other company in the UK utility sector, and no company is insulated from the impact of economic recession, climate change or a changing regulatory environment.

Managing risk

The Company is affected by certain risks, not wholly within our control, which could have a material impact on our long-term performance. Many of the risk factors affecting the Company are business risks that can be effectively mitigated by ensuring that appropriate controls are in place. However, some are inherent risks based upon the nature of our business and other external factors and the most important of these are described below. This section should be read in conjunction with the internal control and risk management section of this report found on page 36.

The assessment and mitigation of risk is a key priority for the Board, which has overall responsibility for ensuring that there is an effective framework operating for risk management and internal control. All risk is assessed in terms of its potential to prevent the Company from achieving its objective of providing high quality and affordable drinking water and wastewater services to Welsh Water's customers and of looking after the water industry in the region served by Welsh Water for today's customers and future generations.

Regulatory risk

Regulatory risk can arise from Ofwat's price control determinations, from the requirement to comply with Ofwat's extensive data requirements and more generally from changes in the regulatory environment.

There is a risk surrounding Ofwat's 'final determination' of price limits for the next regulatory period 2010-15 both with respect to its assumption about the cost of capital allowance, and the regulatory assumptions it makes in respect of operating costs, required capital investment or revenue forecasts. These could affect the ability of the Company to secure funding at a cost and maturity that is efficient. Welsh Water's Final Business Plan has sought to mitigate this risk by, inter alia, including challenging targets for further efficiency savings and by proposing that the household bill in 2015 will be no higher in real terms than now.

The transfer of private sewers would increase our sewer network by more than 70% and we judge that the condition of these private sewers is poor and below the standard of assets that the industry is generally required to operate. The Welsh Assembly Government has indicated that this transfer will take place some time after April 2011.

The Environment Agency has indicated that we may have to plan for major reductions in the volumes of water we abstract from a number of rivers, mostly in south Wales, in order to comply with the EU Habitats Directive. There is also a possibility that stretches of the north east Irish Sea might be designated as 'sensitive waters' under the Urban Wastewater Treatment Directive, which would require Welsh Water to extend a number of coastal wastewater treatment works.

These potential changes to our obligations, which together could require a very large increase in investment expenditure, are not included in our Final Business Plan and if confirmed may fall to be funded through an 'interim determination' by Ofwat of price limits, the outcome of which would be uncertain.

Welsh Water has to provide extensive data to regulators each year in respect of all aspects of our business. Failure to provide reliable, accurate and complete data will trigger regulatory sanction and fines. All regulatory data submitted is subject to comprehensive scrutiny and due diligence. In spring 2008, our process of data collation and verification was accredited to ISO 9001:2000, and this accreditation was retained in spring 2009.

Ofwat has a duty to promote competition where it judges it to be in the best interests of customers. Ofwat recently granted an inset appointment to a new entrant in the water industry in Wales, a decision we have taken steps to challenge by seeking judicial clarification of an important point of principle. The effect of this inset will be to cause customers' bills outside the inset area to be higher than they would have been had the inset not been granted, and we do not believe this to be in the interests of Welsh Water's customers. Should more insets be granted by Ofwat, we judge that risk may be higher due to, inter alia, the changes in responsibilities and nature of working that would follow.

Ofwat is proposing that the industry accounts for each element in the 'value chain' separately as a possible precursor to legal separation of distinct activities. The latter will require changes to the current legal framework. The Welsh Assembly Government has indicated that it will consult on the conclusions of the Cave Review of competition and innovation in water markets, and the extent to which these should be included

in the Floods and Water Management Bill, which has been published in draft. Some of the conclusions of the Cave Review would, if adopted, lead to a change in the structure of the industry and could have serious implications for the Company. We will engage in the consultation process to ensure that, as far as possible, we protect the long term interests of the Company and Welsh Water's customers.

Operational risk

We have reassessed operational risk following the experience of the last 2 years where we have experienced more frequent and extremes of weather, particular storms.

More generally, 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 (such as 'acts of God' or more extreme weather events as a consequence of climate change) or from third party interference with Welsh Water's assets and equipment;
- » changes in environmental, consumer protection and public health and safety law and regulation, which typically require ever higher standards of performance;
- » the health and safety risk associated with the operation of a large and complicated network of assets;
- » the risk of losing and failing to recruit key people in Welsh Water to ensure we have the competencies and experience needed to meet our long-term obligations; and
- » the changes associated with our programme of IT enabled change which is upgrading old IT systems and introducing simplified and more robust business processes to enable a more efficient delivery of services to customers.

Policies and operational strategies exist to mitigate each of the risks that could create an adverse effect on the reputation, operating results and financial position of Welsh Water. Business risk is mitigated by the availability and terms of insurance - covering property, business interruption, public liability, environmental pollution and employer's liability.

Financial risk

Welsh Water is exposed to a number of financial risks, many of which are heightened at a time of economic recession. These include:

- » revenue risk, such as a reduction in metered demand, and the loss of large business customers;
- » the collection of customer charges and non-recovery of customer debt;
- » failure by Welsh Water to achieve targets set by Ofwat at price reviews for operating and capital efficiency, or to deliver the capital investment programme on time and within budget;
- » external cost pressures, for example the impact of changes in power prices, which could prevent the business from achieving operating and capital cost efficiency targets;
- » deflation and the impact on both revenues and regulatory asset value from a negative Retail Price Index; and
- » access to capital markets while the business remains cashflow negative with continuing large capital investment programmes.

The overall financial risk is that Glas Cymru 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 (that is, customers' bills) and the raising of finance from the capital markets.

Under our Common Terms Agreement we are required to ensure that the business has sufficient committed facilities

available to meet at least 12 months anticipated net cash requirement. The Glas Cymru group's financial position at 31 March 2009 shows a significant balance of cash and undrawn borrowing facilities available, which gives the business a high degree of liquidity. The impact of deflation is mitigated by the high proportion of index-linked debt issued by the Company.

Procurement risk

This is a particular risk for Welsh Water, with some 85% of annual operating and capital expenditure being undertaken by outsourced service partners working for Welsh Water under contract. Our framework for competitive outsourcing is described in our Procurement Plan, which is available on our website.

Current contract arrangements for water and wastewater services were put in place following a competitive re-tendering in 2004, and provide for contract partners to work with Welsh Water for up to 15 years. These working arrangements are kept under regular review and every 5 years they are subject to a price and performance review to ensure that Welsh Water's customers continue to receive high quality and best value for money services. This review will take place in the current year to align with Ofwat's Final Determination. Contracts have been designed to encourage first tier suppliers to view their involvement with Welsh Water on a long term basis, thereby reducing the risk of short term conflict of interest and encouraging greater investment in the resources, people and systems needed to continue to deliver high levels of service to Welsh Water customers. In addition, Welsh Water retains the ability to take direct control of activities carried out under contract should performance deteriorate, or risk falling below the standards required by Welsh Water.

Definition, purpose and target for each KPI

Measure	Purpose	Source	Target	Progress to Target
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. We achieved 99.77% compliance in 2008-09.	x
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 level of customer satisfaction. This has been maintained in 2008-09.	✓
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. This target was achieved in 2008-09.	✓
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 are independently determined by three rating agencies: Standard & Poor's, Moody's and Fitch Lovell.	Corporate credit rating of 'A' grade. This was maintained in 2008-09	✓
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. This has been maintained – the 'customer dividend' was increased to £21 in 2008-09 (2007-08: £20). It was further increased to £22 for the financial year that commenced on 1 April 2009.	✓
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's 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%. At 31 March 2009 gearing was 72% (2008: 72%)	✓
Interest cover Strategy: Financing	Meeting interest cover covenants is key to maintaining investor confidence and to keeping Welsh Water's 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. This has been maintained in 2008-09	✓
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. We believe this has been achieved in 2008-09 in which we scored 406 OPA points.	✓

The measures of performance reported on page 5 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.dwr.cymru.

The Directors

Lord Burns Chairman^(M)

Appointed Non-Executive Chairman in July 2000, Lord Burns (65) is chairman of Abbey National Plc and a Non-Executive director of Banco Santander and Pearson Group Plc. Formerly he was Chairman of the National Lottery Commission and of Marks and Spencer Group plc, and a Non-Executive Director of Legal & General Group Plc and The British Land Company Plc. A former Chief Economic Adviser and Permanent Secretary to HM Treasury, he was made a life peer in 1998.

Nigel Annett Managing Director^{(Q)(R)(M)}

Appointed Managing Director in January 2005, Mr Annett (50) 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 (45) 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. He is a Non-Executive Director of the Principality Building Society, a Member of the Board of the Institute of Welsh Affairs and Deputy Chairman of The Prince's Trust - Cymru.

Peter Perry Operations Director^(Q)

Appointed Operations Director in July 2006, Mr Perry (47) 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. He is also a Director (representing Wales) at The Water Regulations Advisory Service, the national body specifying standards for materials and workmanship used in potable water supply.

John Bryant Non-Executive Director^{(Q)(R)(M)}

Appointed a Non-Executive Director in March 2001, Mr Bryant (65) 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.

Geraint Talfan Davies Non-Executive Director^{(A)(R)(M)}

Appointed a Non-Executive Director in July 2000, Mr Davies (65) is a former journalist whose career spanned both public and private sector broadcasting (including Controller of BBC Wales throughout the 1990s). He is Chairman of the Institute of Welsh Affairs and of Welsh National Opera, a member of the board of Wales Millennium Centre and a trustee of The Media Standards Trust. He is also a former Chairman of The Arts Council Wales.

Dame Deirdre Hine Non-Executive Director^{(Q)(R)(M)}

Appointed a Non-Executive Director in March 2001, Dame Deirdre (71) is Chairman of the BUPA Foundation, Chairman of the Public Inquiry into the outbreak of clostridium difficile in hospitals in Northern Ireland and President of the Royal Medical Benevolent Fund. She is a past President of the British Medical Association and The Royal Society of Medicine, a former Chairman of the Commission for Health Improvement, and a former Chief Medical Officer for Wales. Dame Deirdre was awarded the DBE in 1996 for services to medicine.

Tony Hobson Non-Executive Director^{(A)(R)(M)}

Appointed a Non-Executive Director in February 2001, Mr Hobson (61) is the Chairman of The Sage Group plc and of Northern Foods Plc. A Chartered Accountant, he was Group Finance Director of Legal & General Group Plc for fifteen years until his retirement in 2001.

James Strachan Non-Executive Director^{(A)(R)(M)}

Appointed a Non-Executive Director in June 2007, Mr Strachan (55) is a Non-Executive Director of Legal & General Group Plc, Care UK Plc, Sarasin and Partners LLP and Social Finance Limited. Among his previous roles he has been Chairman of the Audit Commission and of RNID (the disability charity), a Board Member of Ofgem (the energy regulator), a Non-Executive Director of the Bank of England, the DTI Business and Energy Boards and the National Lottery Community Fund, and a Disability Rights Commissioner. Earlier in his career Mr Strachan was a Managing Director of Merrill Lynch, the international investment bank.

Bob Ayling Non-Executive Director^{(Q)(R)(M)}

Appointed a Non-Executive Director in April 2008, Mr Ayling (62) is Chairman of the International Dispute Resolution Centre and Vice-Chairman of Dyson Limited. A solicitor by profession, with 20 years in the City of London and as a senior government legal advisor at the Department of Trade and Industry, he was Managing Director and Chief Executive of British Airways plc from 1993 to 2000. He is also a former Chairman of Holidaybreak plc and Non-Executive Director of Royal & Sunalliance Insurance Group.

Membership of Board Committees

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

Full colour version available from our website, dwrcymru.com

Top left to right: Lord Burns, Nigel Annett, Chris Jones, Peter Perry, and John Bryant.

Bottom left to right: Geraint Talfan Davies, Dame Deidre Hine, Tony Hobson, James Strachan, and Bob Ayling.

The Members

There are presently 82 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 the 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 (Glas Cymru) for the year ended 31 March 2009.

Principal activities

Glas Cymru is a company limited by guarantee and is the holding company of the Glas Cymru group. Dŵr Cymru Cyfyngedig (Welsh Water) is the sixth largest of the 10 regional water and sewerage companies in England and Wales and is the principal trading company.

Following its acquisition by Glas Cymru in 2001, Welsh Water is the only UK utility to be operated under a 'not-for-profit' business model, whereby all financial surpluses are retained in the business as reserves, invested in additional quality or service improvements or returned to customers in the form of an annual 'customer dividend'. Glas Cymru exists only for one purpose - to create the financing and operating conditions for Welsh Water that will allow the company to provide high quality water and sewerage services to more than 3 million people at the least cost.

Welsh Water's primary purpose and responsibility is to operate, maintain and upgrade the company's network of assets so as to ensure a safe and reliable supply of drinking water and to deal effectively with wastewater in order to protect public health and the natural environment.

The Board's approach to governance

As a single purpose company, our long term success has only one measure - the extent to which we deliver value for the customers of Welsh Water. As Glas Cymru has no shareholders, when exercising judgement and discretion, Directors seek to enhance customer value and take decisions in the long term interests of the customers of Welsh Water. The key governance structures and internal controls operated in Glas Cymru are described in the governance report on page 33 of this report. Through these mechanisms the Board aims to apply high standards of corporate governance and to meet the spirit of the Combined Code in a manner framed to suit our single purpose business model.

Business review

The Companies Act 1985 requires that the Directors' Report should include a Business Review which gives a fair review of the development and performance of the business and a description of the principal risks and uncertainties that it faces.

The operational performance of the business and our approach to sustainability and corporate responsibility are described on pages 5 to 17 of this report. The financial performance is described in the Financial Review on page 18. A statement of the principal risks of the business can be found on page 24. The information contained in these sections is incorporated into this Directors' Report by reference to the extent necessary to fulfil the requirements of a Business Review.

The Business Review includes a description of our key stakeholders. Consideration of the interests of these stakeholders and other factors likely to impact on the success of the business is an integral part of the Board's decision-making process.

The 2009 Annual Report (including this Directors' Report) has been prepared for the Members of Glas Cymru. It contains certain information of a forward looking nature, which has been provided by the Directors in good faith using knowledge and information available up to the date of this report. Forward looking statements should be regarded with caution because of the inherent uncertainties in economic trends and business risks.

Financial performance and 'customer dividend'

In 2008-09, customers benefited from a 'customer dividend' of £27 million, or £21 per customer served by Welsh Water (£10.50 for water and £10.50 for wastewater services). For the financial year 2009-10, for which bills have been issued, the 'customer dividend' was increased to £22 per household (£11 for water and £11 for wastewater services), a total of £28 million.

After payment of the 'customer dividend', the loss before tax for the financial year ended 31 March 2009 (excluding the fair value movement on derivative financial instruments) was £11m (2008: profit £11 million). At 31 March 2009 net debt as a percentage of regulatory capital value of Welsh Water was 72% (2008: 72%) and we had a robust liquidity position with £559 million of cash and undrawn bank facilities, meaning that the business is funded to 2010 and beyond.

In April 2009 Welsh Water published its investment plans and priorities for the period 2010 to 2015. These propose to maintain a high level of capital expenditure, similar to the period 2005 to 2010, and include important investment to enhance the protection of drinking water quality, mitigate the worst impacts of sewer flooding, substantially reduce the carbon footprint of its activities and improve customer service. Under Welsh Water's preferred plan the average household bill in 2015 would be no higher in real terms than it is today.

Directors

The names and brief biographical details of the Directors are given on page 28. With the exception of Bob Ayling who was appointed on 3 April 2008, 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. The Board has not been requested to use, and has not used, its discretion under Article 57 of Glas Cymru's Articles of Association which allows the approval of a potential conflict of interest.

At the Annual General Meeting on 10 July 2009 ('2009 AGM') Peter Perry, James Strachan and Geraint Talfan Davies will retire by rotation and seek re-election as Directors in accordance with the Articles of Association. The Board has endorsed the effectiveness and commitment (and, where appropriate, the independence) of these Directors and recommends each for re-election. Further details are set out in the Notice of 2009 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 2009 on page 38. A resolution will be proposed at the 2009 AGM to approve this 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 a director has not acted fraudulently or dishonestly. The indemnity is a qualifying indemnity for the purpose of the Companies Act and is for the benefit of all Directors.

Details of our internal control and governance arrangements are set out in the Governance Report on page 36.

Members

At the date of this report, Glas Cymru has 72 Members excluding the Directors of the Company who are also Members. Further 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 37. Further information on this, along with brief details of the current Members, is available on request or may be obtained from our website.

Employees

At 31 March 2009 Welsh Water employed 192 people (2008: 178). Other than the Directors of the Company, Glas Cymru has no employees.

Having a highly committed and motivated staff is crucial to achieving Glas Cymru's sole purpose. A key part of delivering continuous improvement in the performance of the business and the level of service received by Welsh Water's customers is an ongoing investment in our people at all levels. We are committed to equality of opportunity and aim to treat all employees (including disabled persons) fairly in every aspect of employment, including recruitment, training, career development and promotion. Those who seek employment with Welsh Water are considered solely on their skills and abilities.

Further information on our strategies to support staff is contained in the Business Review on page 14.

Welsh Water's employee pay and benefits package compares favourably with the local employment market and the UK Industrial and Services market benchmarks. All staff share in the success of the business via a staff incentive scheme, which pays an annual bonus linked to the relative financial and customer service performance of Welsh Water, as measured by Ofwat's Overall Performance Assessment. All staff received an annual total pay and benefits statement.

Under 'Working Together', the framework agreement with trade unions and staff representatives that has successfully operated since the early 1990's, in April 2009 staff received a general pay award of 3%. Given the current economic climate, however, the Remuneration Committee and the Board agreed that the pay of Executive and Non-Executive Directors and certain senior managers would be unchanged for 2009-10.

Occupational health and safety

The Board is committed to achieving high standards of occupational health and safety. Nothing is more important than the health and safety of the people who work for us, and those we affect through our work.

Last year we reported that Welsh Water's process of health and safety management had achieved accreditation to the OHSAS 18001:1999 standard. In February 2009, Welsh Water achieved certification to the OHSAS 18001:2007 international standard for occupational health and safety management with an extended scope of service for work relating to the 'business and administration of strategic management of water services provision including contract management'.

In 2008-09 Welsh Water and its contract partners maintained a trend of year on year reduction in the number of reportable accidents. Full details of our health and safety performance in 2008-09 and our current challenges and goals are described in our 2009 Health and Safety Report. A copy of this report is available on request or on our website.

Water quality and the environment

If we are to achieve our goal for Welsh Water to be consistently recognised by its customers as the best water company in the UK, we must continuously improve our water quality and environmental performance and how we manage the direct and indirect environmental impacts of the business. This is essential to the future success of the business. With this in mind the Board has set challenging ambitions and targets for the next 25 years and these are set out in "Welsh Water: Our Sustainable Future", which is available from our website.

The Quality and Environment Committee of the Board (QEC) meets each month to monitor quality and environmental performance. QEC tracks the development of key operational strategies, as we aim to develop a more sustainable water and wastewater business based on developing best practice and knowledge. QEC also reviews the cause of and Welsh Water response to all major water quality and environmental incidents. A copy of the 2009 QEC Report is available on our website.

Directors' report

Research and development

Welsh Water monitors and selectively participates in water industry research initiatives, most notably through membership of UK Water Industry Research Limited, which manages and coordinates the research interests of UK water companies. Where appropriate, we also sponsor private companies and university research departments to undertake relevant investigations into issues that relate to our business objectives and priorities for the operational region. The findings from all research initiatives are disseminated through Welsh Water and its outsourced contract partners under a reciprocal sharing arrangement.

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 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 2008-09, the average payment period for the Glas Cymru group was 49 days (2008: 53 days). Regulations require that in calculating this we include within trade creditors monies retained under contract in respect of Welsh Water capital investment projects. The level of retentions varies from year to year and affects the average payment period for the year.

Corporate social responsibility

We have a clear and firm commitment to environmental responsibility and in being a good neighbour and trusted partner in the communities we serve. To earn this trust we have to show that we behave fairly and responsibly in the interests of customers, that we use resources wisely, and that we make an appropriate contribution to community.

This approach to 'responsible business' is an essential part of our not for profit business model and further information is provided on page 16 of this report.

During the year, charitable donations amounted to £44,212 (2008: £18,559). There were 8 beneficiaries of awards of above £500 ranging from £750 to £11,500.

It is Board policy not to make donations to political parties or to incur political expenditure, and during 2008-09 no donations or payments have been made which are required to be disclosed under section 366 of the Companies Act 2006.

Welsh language scheme

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. Our Welsh Language Scheme is an approved scheme under the provisions of the Wales Language Act 1993.

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 is published on our website or is available on request from the Company Secretary.

Going concern

The Directors are satisfied that the business has adequate resources to continue in business for the foreseeable future. Accordingly, the financial statements for the year ended 31 March 2009 have been prepared on a going concern basis.

Auditors

PricewaterhouseCoopers LLP (PwC) acted as the auditors to Glas Cymru for the accounts for the year ended 31 March 2009. 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.

A resolution to re-appoint PwC will be put to Members at the 2009 AGM.

Events after the financial year-end

There have been no post balance sheet events.

Annual general meeting

The 2009 AGM will be held on Friday 10 July 2009. The business of the 2009 AGM includes the approval of the Directors' Report and Financial Statements and the Remuneration Report for the year ended 31 March 2009, the re-election of 3 Directors, a resolution to authorise the Company to make donations to EU political organisations and/or incur EU political expenditure up to defined limits and a resolution to reappoint the auditors. These resolutions are matters of ordinary business for the 2009 AGM. In addition there will be a resolution to amend certain provisions in the Articles of Association of the Company. Further information in respect of all resolutions is provided in the Notice of 2009 AGM sent to the Members of Glas Cymru with this report.

By order of the Board



Richard Curtis LLB, ACIS
Company Secretary
5 June 2009

All documents which are stated as available on the Company's website can be obtained from:
www.dwrcymru.com

Corporate governance

Glas Cymru is committed to high standards of corporate governance. This is critical if we are to be regarded as a well-managed provider of an essential public service in the eyes of Welsh Water's customers and regulators, bondholders and other stakeholders.

This report explains the key features of the Company's governance structure and how it complies with the Combined Code on Corporate Governance 2008 (the Combined Code), which sets the standard for good practice for UK listed companies. Not all of the provisions of the Combined Code apply to Glas Cymru as a company limited by guarantee, however, 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 37.

The Board

The Board comprises 10 Directors: a Chairman, 3 Executive Directors and 6 Non-Executive Directors. Directors collectively provide a broad base of experience and expertise appropriate to oversee the business and to maximise the effectiveness of the Board, ensuring that all matters are fully debated and that no individual or group dominates the Board's decision making process. No Non-Executive Director has any business or other relationship that could materially interfere with the exercise of their judgement, and the Board considers each of the Non-Executive Directors to be independent of the Company and each other.

The roles of the Chairman and Managing Director are separate and clearly defined. The Chairman is responsible for ensuring the effective operation of the Board and that the information it receives is sufficient to make informed judgements, and for ensuring that constructive relationships are maintained with key stakeholders. As part of its regular evaluation, the Board considers the Chairman's availability and capacity to undertake the role against the background of his other commitments. The Board remains satisfied that the Chairman fulfils his role effectively and has the capacity to be available when unforeseen circumstances arise.

The Managing Director is responsible for the day-to-day management of the business and for the implementation of the strategy, policies and procedures adopted by the Board. The Managing Director is supported by 2 Executive Directors and by an executive team comprising heads of specialist functions.

The Non-Executive Directors have access to all information relating to the business; 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.

Each of the Executive Directors has a written service contract subject to termination by the Company on 12 months notice. The Chairman and each of the Non-Executive Directors have a written letter of appointment subject to termination by the Board on 3 months notice. A copy of each of these agreements is available for inspection at the Company's registered office and at the annual general meeting.

Any new Director must stand for election at the first annual general meeting following his or her appointment, and each Director is

subject to re-appointment by the Members of Glas Cymru at intervals of not more than 3 years. The Directors standing for re-appointment at the 2009 AGM are named on page 30 of this report.

Board proceedings

The Board met 9 times in 2008-09, including 2 two day meetings, to collectively set the strategic direction of the business and to review the operating and financial performance and risk management 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.

The table below summarises the number of Board and committee meetings held in 2008-09 and the level of attendance at each.

	Board	Nominations(N)	Audit(A)	QEC(Q)	Remuneration(R)
Number of meetings held in 2008-09	9	1	4	12	4
Lord Burns (N)	9*	1*			
Nigel Annett (Q, N)	9	1		12	
Chris Jones	9				
Peter Perry (Q)	9			11	
John Bryant (R, Q, N)	9	1		12	4*
Geraint Talfan Davies (A, R, N)	9	1	4		4
Dame Deirdre Hine (R, Q, N)	9	1		11*	4
Tony Hobson (A, R, N)	8	1	4*		4
James Strachan (A, R, N)	8	1	4		4
Bob Ayling (R, Q, N) (Appointed 03/04/08)	8	1		9	4

*Denotes committee Chairman.
QEC: Quality and Environment Committee.

Corporate governance

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 support meaningful debate and effective decision making. The Company Secretary also advises the Board on corporate governance. To support the independence of Non-Executive Directors, and to enable them to discuss more freely the performance of the executive management team, there is regular opportunity for the Chairman and the Non-Executive Directors to meet privately.

New Directors: Induction and training
Appointments to the Board are made following recommendation from the Nominations Committee. Each new Director receives an induction programme to familiarise him or her with the business, the risks and strategic challenges, and the economic, competitive, legal and regulatory environment in which it operates. Introductory visits are arranged to company sites and to key suppliers (contract partners) and other stakeholders.

A programme also exists to ensure that all Directors have the opportunity to continually update their skills and business knowledge. This can take the form of visits to strategic operational assets or meetings with stakeholders, by the provision of information and presentations to the Board on key strategic issues, and by a Director's occasional attendance on an external course.

Evaluation of the Board

Directors participate in an annual evaluation process to assess the effectiveness of the collective performance of the Board, the performance of the Chairman and of the principal committees of the Board. The conduct of this process is overseen by the Chairman and comprises questionnaires completed by 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.

Following review in previous years a private website was established for the dissemination of information to Directors and for holding board papers and other reference material, more informal dinners have been held to allow discussion of strategic issues outside of the formal boardroom environment; and additional Board meetings held over two days were scheduled, to enable Directors to meet and build relationships with key senior managers and staff below Board level. The most recent evaluation in March 2009 raised no material weaknesses or failings, but highlighted certain minor aspects for consideration to further improve the effectiveness of the Board.

The Board, without the Chairman present, reviews and evaluates 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 4 principal committees of the Board. Each has a written term of reference that defines the role and responsibilities of the committee and which is reviewed annually. These are the Nominations Committee, the Audit Committee, the Quality and Environment Committee, and the Remuneration Committee. The Board also has an ad-hoc Finance Committee to approve financing and treasury transactions where a decision is required between formal meetings of the Board.

The membership of each committee is intended to make best use of the independent challenge and skills and experience of the Non-Executive Directors. After each committee meeting a summary of matters discussed is reported to the Board, and the Board subsequently receives the formal minutes. Each committee 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 and membership of the Nominations Committee, the Audit Committee, and the Quality and Environment Committee is set out below. The work of the Remuneration Committee is described in the 2009 Remuneration Report on page 38. 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), legal (Bob Ayling) and government and regulation (Lord Burns).

Nominations Committee

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

It is the responsibility of the Nominations Committee to ensure that plans are in place for orderly succession for appointment to the Board. Its role is therefore to review the size, structure and composition of the Board (i.e. the skills, knowledge and experience around the Board table) and, where appropriate, to recommend candidates for Board appointment. In planning for Board succession, in 2008-09 the Nomination Committee has been advised by Russell Reynolds & Associates.

The Combined Code requires that the majority of Directors shall be independent of the company (i.e. that they are individuals who the Board determines to be independent in character and judgement and who have no relationships or circumstances which are likely to affect, or could appear to affect, the Director's judgement). The Board of Glas Cymru meets this requirement and would, if called on, provide a statement of reasons to support its view that any named Director is independent.

Glas Cymru was established in 2000 and 4 of the 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. Last year we reported that the Nominations Committee and the Board have agreed in principle that, in these circumstances, it would be in the best interests of the Company (and of the customers of Welsh Water) to consider extending the term of office of some of the Non-Executive Directors beyond nine years. This would allow greater continuity on the Board as Welsh Water moves into the next regulatory investment period (AMPS: 2010-2015) and in the first review of contract pricing under Welsh Water's outsourced procurement arrangements. The volatility in the UK's economic climate in the past year has provided additional reason to consider extending the continuity of the Board.

No decision has been made on this to date, but as required by the Combined Code any Non-Executive Director whose appointment was extended beyond 9 years would become subject to annual re-appointment by the Members of Glas Cymru. The Chairman of the Board would ensure that any Non-Executive Director to be appointed beyond 9 years is independent in character and judgement.

Audit Committee

The members of the Audit Committee are independent Non-Executive Directors: Tony Hobson (Chairman), 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, Internal and External Auditors and selected other senior managers. The Company Secretary acts as secretary to the Committee. The Board considers that Tony Hobson, a Chartered Accountant and former Group Finance Director of Legal & General Group plc, has the significant 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 internal and external auditors, and in particular:

- » to review and advise the Board on Glas Cymru's interim and annual financial statements, its accounting policies and on the control of its financial and business risks;
- » to 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;
- » to review and advise the Board on the effectiveness of the internal control environment in the business, including the 'Whistleblowing' procedures;
- » to make recommendations on the appointment and remuneration of external auditors and to monitor their performance; and
- » to approve and monitor the policy for non-audit services provided by the external auditors to ensure that the independence of the auditors is not compromised.

The Audit Committee meets on at least 4 occasions each year. 2 of the meetings focus on review of the annual and interim reports and associated preliminary and interim results announcements, and related areas of judgement and significant accounting policies. Time is allocated at other meetings to review the findings of the external and internal audit programme and to assess the processes for the management and control of financial and business risks, including challenge to the Executive Director's assessment of those risks and their mitigation strategies and action plans to manage those risks. Significant reports and issues arising from Welsh Water's risk based audit programme are discussed at every meeting of the Committee.

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. On the basis of this work, and regular meetings with executive management, the Audit Committee is able to assess the ongoing effectiveness of internal and external audit.

The role of internal audit is to provide independent and objective assurance and to advise management and the Board on the extent to which systems of internal control are effective and 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 to ensure that it is focused on areas of greatest risk to the business, and is approved by the Audit Committee.

During 2008-09, external auditor services were provided by PricewaterhouseCoopers LLP and the conduct, but not the management, of internal audit activity was outsourced to Grant Thornton UK LLP. The Company also significantly increased the resourcing of its internal Business Assurance team, which since 1 April 2009 has taken over delivery of the internal audit work plan following the surrender of the internal audit contract by Grant Thornton.

Corporate governance

The Audit Committee has reviewed the policies of the external auditor to ensure their independence and that of their engagement partner and that Board policy on non-audit fees has been met. This provides that the external auditor will not be used for internal audit services, and that all non-audit work above a threshold of £25,000 will be subject to prior competitive tendering and approval by the Audit Committee. Total external auditor remuneration is analysed between audit and non-audit work in Note 4 to the Accounts on page 58.

The terms of reference of the Audit Committee include all matters required by the Combined Code. 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 3 Non-Executive Director members (Dame Deirdre Hine, Chairman, John Bryant and Bob Ayling) and 2 Executive Director members (Nigel Annett and Peter Perry). QEC is advised by 2 independent experts on the public health and operational aspects of water supply and environmental management, and by Welsh Water's Head of Water Quality and Head of Operational Performance and Customer Service who, with the Company Secretary, attend all meetings.

QEC was established in 2001 to play a central role in the governance of Welsh Water, recognising that a major element of Glas Cymru's business model is its out sourcing strategy, under which some 85% of Welsh Water's operating and capital expenditure is incurred by third party partners through competitively let contracts.

The role of QEC is to oversee Welsh Water performance, which targets 'top quartile' overall performance on key regulatory measures for water quality, customer service and efficiency and environmental performance, while delivering the best available combination of cost efficiency, value for money and quality of service. Through its oversight QEC provides assurance to the Board that Welsh Water's obligations as a water and sewerage undertaker are not compromised or put at risk by its outsourcing strategy.

In particular, QEC:

- » advises the Board on matters of operational policy and practice, and routinely reviews the performance of Welsh Water 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;
- » reviews 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;
- » reviews executive management's assessment of operational and quality risk; and
- » assesses Welsh Water's management of and response to significant water quality or environmental incidents, and any weakness identified under the internal audit quality programme of work.

QEC produces an annual report to the Board, which is published on our website.

Internal control and risk management

The Board has overall responsibility for ensuring that the business maintains a sound system of internal control and risk management and for monitoring its effectiveness. The system is designed to manage risk of failure to achieve business objectives. It comprises audited policies, procedures and processes designed to identify, evaluate and manage the significant risks faced by the business, and provide reasonable 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, particular risk issues. No system can eliminate risk entirely.

Key features of the system are:

- » the Board sets parameters of acceptable risk and key risks and hazards are identified, measured and managed to an acceptable level;
- » clear accountability for risk management is embedded in the business, and supported by regular risk reporting;
- » controls that recognise that the nature and balance of risk changes and evolves continuously and provide a framework within which to manage this;
- » assurance is provided by independent audit and assessment of internal quality management systems. All audit activity is conducted under a broad risk based programme approved by the Audit Committee and QEC, designed to ensure that management information is accurate, timely and relevant and reflects the true position of the business;
- » procedures exist 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; and
- » the system of internal control is reviewed by Welsh Water's Reporter who submits an annual report to the Board and to Ofwat to confirm compliance with Ofwat's guidance for the UK water industry on internal control.

Business risk is routinely reassessed 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 contract partners, and includes areas such as public health, environment, business ethics, employment, occupational health and safety and business continuity. The risk management group encourages staff to participate in 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 Committee and QEC receive an update on our principal risks and process of risk management every 6 months, and this is reviewed annually at the Board.

In judging the effectiveness of the business's system of internal controls, the Board considers periodic reporting from the risk management group, the Audit Committee and QEC. The Board also routinely monitors key performance indicators and monthly reports of financial and operational performance, which flag variances against the agreed business plan and budget. By so doing, the Board reviews the effectiveness of the internal control system over the course of the year.

Members 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 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.

The Board appoints the Members, 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 72 Members, excluding the Directors of the Company. Subsequent to the financial year end, and following evaluation and recommendation by the panel, the Board has approved the reappointment of 15 Members whose term of office would otherwise expire at the end of the 2009 AGM. 1 member elected not to seek re-appointment.

Further details of the Membership Policy and the Members of Glas Cymru can be obtained from the Company Secretary or from our website.

Communication with stakeholders

The Board attaches high importance to maintaining good relationships with Members and investors. The Members of Glas Cymru have regular opportunity to meet with Directors at the 2 Members' Meetings held each year. At these meetings, Directors, including the chairmen of the key Board committees, are available to answer questions. All Members, including those unable to attend any meeting, receive a written brief of issues discussed at each meeting.

For investors, Glas Cymru hosts an annual event in London, and immediately following the announcement of interim and preliminary results for any period there are informal meetings with major bondholders and other investors, who may also request a meeting with an independent Non-Executive Director at any time. The Board receives a report following meetings with investors. 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
5 June 2009

All documents which are stated as available on the Company's website can be obtained from: www.dwrwymru.com

Remuneration report 2009

Compliance

This report has been prepared in accordance with the provisions of the Companies Act 1985 and, in line with the Board's commitment that Glas Cymru shall report as if it were a listed company, in accordance with the Directors' Remuneration Report Regulations 2002. The report has been approved by the Board and will be put to Members for approval at the 2009 Annual General Meeting (2009 AGM).

The Directors' emoluments table, long-term performance related bonus table and pension table on pages 41 and 42 have been audited by PricewaterhouseCoopers LLP. The remainder of the report has been reviewed by them.

Remuneration Committee

The Remuneration Committee (the 'Committee') is chaired by John Bryant and comprises all the Non-Executive Directors. A copy of the terms of reference of the Committee is available on the Company's website. The Chairman of the Board and the Managing Director, attend meetings of the Committee only by invitation. The Company Secretary acts as secretary to the Committee. The Committee met on 4 occasions in 2008-09.

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, and
- » to determine incentive arrangements that encourage and recognise good performance and reward individuals in a fair and responsible manner for their contribution to the success of the Company.

The Committee has sought independent external advice on certain aspects of remuneration policy and best practice.

The firms named below advised the Committee in 2008-09, and have been reappointed to advise the Committee in 2009-10:

- » Hewitt 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, and
- » Linklaters & Alliance, who provide legal advice to the Committee on Directors' service contracts and pension matters.

In 2008-09 the Committee also received pensions information and advice from Quantum Actuarial LLP.

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

Remuneration Policy

The Committee considers the principles and provisions of the Combined Code when setting policy and believes it is fully compliant. The Committee also has regard to pay awards to other employees and to broader social, environmental and governance issues when setting remuneration terms.

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 relatively high proportion of Executive Directors' remuneration is dependent on Welsh Water's performance in terms of water quality, protecting the environment and customer service.

The executive remuneration package comprises 4 elements: base salary and benefits; an annual performance related bonus; a longer term performance related incentive; and a pension.

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

- » 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;
- » water and environmental quality, 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 shall be fair and competitive when compared to the relevant market and the organisation generally;
- » a significant proportion of the Directors' remuneration should be variable and dependent on the achievement of stretching performance targets;
- » an appropriate combination of fixed and variable pay will ensure that the interests of management are suitably aligned with the longer term objectives of Glas Cymru and the customers of Welsh Water; and
- » there will be a claw back of variable rewards (including long term incentives) where those rewards were made on the basis of performance which subsequently proved to be misstated.

When setting remuneration, the Remuneration Committee considers remuneration in the UK water companies (both quoted and unquoted) taking into account, amongst others, turnover and business complexity (e.g. regulatory versus non regulatory business and international exposure) of the comparator companies. In addition, reference is made to remuneration practice in the FTSE 250.

The Committee has reviewed the appropriateness of this comparator group and agreed it remained relevant for setting remuneration in 2009-10.

Bonus Policy: Annual Performance Related Bonus

In 2007-08 the Committee reviewed the incentive arrangements to ensure that they supported the above principles, but found that the quantum of maximum potential remuneration available for the Executive Directors had fallen behind relevant market benchmarks. To address this, and taking into account practice in the listed water companies and other water companies of comparable size, the Committee increased the annual bonus potential for Executive Directors for 2008-09 to 100% of salary, with receipt of the additional bonus of 20% dependent on delivery against specific operational measures determined by the Committee on an annual basis. The Committee agreed these additional measures would be structured as absolute measures and as such dependent on improved performance by Welsh Water, and not simply good relative performance.

The change addressed 2 issues: improving the market positioning of the current remuneration arrangements; and supporting the principle that Welsh Water delivers consistently strong operational performance. To earn the maximum bonus, Executive Directors would need to show evidence of significant improvement in performance in each of the selected operational measures, with no element of this additional bonus being payable if performance against each respective measure failed to show progress.

To achieve maximum additional bonus in any year, performance against the selected operational measures would need to match the best achieved by a company in the sector. The Committee has agreed that the maximum annual bonus for 2009-10 should be maintained at 100%.

For 2008-09, the maximum annual cash bonus payable was 100 percentage points of base salary ('PPBS'), with payment of the maximum bonus divided across three components: customer service performance (40 PPBS), financial performance (40 PPBS) and performance against four specific operational measures (20 PPBS, 5 PPBS per measure).

Target bonus for 2008-09 for the customer service and financial performance elements of this bonus was set at the same as in 2007-08, i.e. 50 PPBS. The Committee has agreed that this allocation of bonus remains appropriate and that it will be applied in the financial year 2009-10.

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 for this element) 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:** including drinking water quality compliance, interruptions to supply and restrictions on supply;
- » **sewerage measures:** including sewage flooding incidents and a quality of effluent discharges to the environment that meets legal and regulatory standards; and
- » **customer service performance:** including 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 up or down by up to 10 PPBS to reflect identifiable and significant aspects of customer service performance not captured by OPA. The Committee did not adjust bonus paid in respect of the financial year 2007-08, which was paid in November 2008.

The financial component of the annual performance related bonus 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 for this element) 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 measures selected by the Committee to comprise the 'operational measures' component of the annual performance related bonus for 2008-09 are set out below. The Committee set challenging targets to be met to earn this element of bonus with no bonus being payable for performance at or below performance in 2007-08 and (except for measure (a) below) and to earn maximum bonus would have required performance equal to or better than the best ever performance in the sector.

- (a) Avoidable customer complaints, being complaints that relate to a service failure by Welsh Water, which shall not include complaints as regards matters of Board policy or activity relating to the collection of customer charges. To receive maximum bonus against this measure, in 2008-09 the number of avoidable complaints would have needed to reduce by more than 50%.
- (b) Sewer flooding attributed to 'other causes' – i.e. other than due to hydraulic overload of the sewer network.
- (c) Category 3 pollution incidents. Any environmental damage caused by Welsh Water's operations is a concern and each of these less significant pollution events is investigated as 'near-hit' for a more significant pollution event to ensure that lessons are learned.
- (d) The Operational Performance Index ('OPI'), which is a Drinking Water Inspectorate performance index used by Ofwat as a key measure to assess overall drinking water quality.

Remuneration report 2009

The 2008-09 Accounts include an accrual of £333,960 (equivalent to 50.6 PPBS) reflecting the Committee's current estimate of Welsh Water's relative performance for the year ended 31 March 2009. The Committee will make its final assessment of bonus payable for 2008-09 in the Autumn 2009, following publication by Ofwat of its annual Levels of Service Report.

Performance delivered in 2008-09 earned Executive Directors 4PPBS of the maximum 20PPBS, 2PPBS in category (a) and 2PPBS in category (d). This reflects the fact that the target levels set by the Committee, if achieved, would have delivered sector leading performance.

The Committee has agreed that the operational measures applied in 2008-09 remain valid for 2009-10 and that the targets applied in 2008-09 will be carried forward.

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 2 years), which while capable of revision at any time was intended to operate for a 5 year period ending on 31 March 2010. The maximum bonus payable under RLTIS is 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 9 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 2 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 the underlying rating of 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 3 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 10 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 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 3 years in advance, save where a shorter period is necessary to reflect the timing of Ofwat's regulatory price reviews. 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 requires that Welsh Water outperforms 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 is disclosed in the next annual remuneration report.

The 2008-09 Financial Statements include an accrual of £211,200 (equivalent to 32.0 PPBS) reflecting the Committee's current estimate of Welsh Water's relative performance for the three-year period ended 31 March 2009. The Committee will make its final assessment of bonus payable under the RLTIS for 2008-09 in the Autumn 2009 following publication by Ofwat of its Levels of Service Report for the year.

The Committee, advised by Hewitt New Bridge Street, has commenced discussion regarding the shape and components of a long term incentive scheme that would be appropriate for the next 5 year period (2010-15), and an update on the Committee's view on this will be presented to the Members of Glas Cymru at the 2009 AGM. Proposals for a long term incentive scheme for the period commencing on 1 April 2010 will be submitted for approval at the 2010 AGM.

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. In the current economic climate it was agreed, that there would be no change in the fees of the Chairman and the Non-Executive Directors in 2009-10, but that a 2 year benchmark review would be undertaken in February 2010, which would inform the review of fees for the following financial year in March 2010.

The fees payable for the financial year 2009-10 are: Chairman £180,000 (2008: £180,000) Non-Executive Directors £52,500 (2008: £52,500).

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. The Chairman and the Non-Executive Directors are appointed under letters of appointment, terminable by either party on 3 months' written notice.

Remuneration: Executive Directors Salary

Consistent with the decision of the Committee in respect of the Chairman's fees, the Committee agreed that there would be no change in the salaries of the Executive Directors for 2009-10, but that a 2 year benchmark review would be undertaken in February 2010 which would inform the review of remuneration for the following financial year.

At 1 April 2009 the base salaries of the Executive Directors were as below:

Nigel Annett (Managing Director)
£260,000 (2008: £260,000)
Chris Jones (Finance Director)
£205,000 (2008: £205,000)
Peter Perry (Operations Director)
£195,000 (2008: £195,000)

Annual performance related bonus

In Autumn 2008 Executive Directors received an annual incentive bonus for the year ended 31 March 2008 equivalent to 54.6PPBS, of which 14.6PPBS related to performance against customer service targets and 40.0PPBS to meeting financial targets. This compared to an accrual in the 2007-08 Accounts of 51.6PPBS.

Rolling Long Term Incentive Scheme

In Autumn 2008 Executive Directors received payment under the RLTI in respect of the period ended 31 March 2008 equivalent to 30.7PPBS, of which 7.5PPBS related to performance against customer service targets and 23.2PPBS to meeting financial targets. This compared to an accrual in the 2007-08 Accounts of 30.4PPBS.

Pensions

The Executive Directors are all members of the Welsh Water Pension Scheme, a defined benefit scheme. Their normal retirement age under this scheme is 60 and 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. The scheme also provides life cover of 4 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 are also entitled to participate in a private health and medical insurance scheme.

Directors' Emoluments (excluding pension benefits and long term performance related bonus)

The table on page 42 reports emoluments in respect of the year ended 31 March 2009, and includes a best estimate of the performance related annual bonus relating to customer service performance for 2008-09. The annual performance related bonus is ordinarily paid in the Autumn, following publication by Ofwat of its Levels of Service Report, which sets out the comparative performance of the 10 water and sewerage companies of England and Wales and the OPA data for the financial year. 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 of emoluments adopted in the table on page 42 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 pension benefits earned by the Directors during the year are shown in the table below.

	Accrued Pension (per annum) at 31 March 2009	Real increase in accrued pension in the year (net of inflation)	Transfer value at 31 March 08	Transfer value equivalent of increase in accrued pension	Transfer value at 31 March 09	Contributions paid by Director	Transfer value of real increase in accrued pension, net of member contributions
NC Annett*	£102,021	£8,726	£961,846	£331,914	£1,293,760	£15,600	£95,093
CA Jones*	£64,102	£7,556	£455,105	£182,256	£637,361	£12,300	£62,824
PD Perry**	£73,021	£10,383	£551,638	£242,517	£794,155	£11,700	£101,222

* Accrued pensions include previous service in Hydel Water and United Utilities Pension Schemes.

** The accrued pension and transfer value at 31 March 2008 and 31 March 2009 allow for Peter Perry's augmented benefits at those dates. The augmentation is based on the reinstatement, over a five-year period, of a full salary link to benefits transferred into the scheme from his previous employer.

Remuneration report 2009

Directors' Earnings: Rolling Long Term Incentive Scheme

In addition to the disclosed emoluments, provision is made in the Financial Statements for the payment under the 3 year rolling long term incentive scheme (RLTIS) which is payable in Autumn 2009.

The provision of £211,200 equates to 32.0PPBS, and has been estimated on the basis that the performance in Ofwat's Overall Performance Assessment for the 3 year period 2006-07 to 2008-09 will be fourth, as follows:

Nigel Annett	£83,200
Chris Jones	£65,600
Peter Perry	£62,400

The final amount to be paid will be determined when Ofwat publishes its OPA results for 2008-09 in Autumn 2009, and could be higher or lower than the provision made.

For the 3 year period ended 31 March 2008 ranked Welsh Water joint third in OPA performance of the 10 water and sewerage companies. Following publication of this report, in November 2008 payments were made to Executive Directors totalling £347,820 (equivalent to 52.7PPBS): Nigel Annett £137,020, Chris Jones £108,035 and Peter Perry £102,765. These payments were 1.1PPBS higher than the provision made in the 2007-08 Accounts.

Service contracts

The Executive Directors have service contracts that are subject to 1 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.

The following emoluments were earned by the Directors in respect of the financial year ended 31 March 2009.

2008-09 ⁽¹⁾	Lord Burns	NC Annett	CA Jones	P Perry	RJ Aytling	JM Bryant	GT Davies	DJ Hine	AJ Hobson	JM Strachan	Total
Salary	£190,000	£260,000	£205,000	£195,000	-	-	-	-	-	-	£660,000
Bonus 2008-09											
Provision annual bonus ⁽²⁾	-	£131,560	£103,730	£98,670	-	-	-	-	-	-	£333,960
Benefits in kind ⁽³⁾	-	£554	£532	-	-	-	-	-	-	-	£1,086
Fees	-	-	-	-	£52,163	£52,500	£52,500	£52,500	£52,500	£52,500	£504,663
Total emoluments relating to 2008-09	£190,000	£392,114	£309,262	£293,670	£52,163	£52,500	£52,500	£52,500	£52,500	£52,500	£1,499,710

The following emoluments were earned by the Directors in respect of the financial year ended 31 March 2008.

2007-08	Lord Burns	NC Annett	CA Jones	P Perry	JM Bryant	GT Davies	DJ Hine	AJ Hobson	JM Strachan	AJ Carmwath	Total
Salary	-	£240,000	£185,400	£185,400	-	-	-	-	-	-	£610,800
Bonus 2007-08											
Annual bonus provision ⁽⁴⁾	-	£123,840	£95,666	£95,666	-	-	-	-	-	-	£315,172
2007-08 bonus adjustment	-	£7,920	£6,118	£6,118	-	-	-	-	-	-	£20,156
Total bonus ⁽⁵⁾	-	£131,760	£101,784	£101,784	-	-	-	-	-	-	£335,328
Benefits in kind ⁽³⁾	-	£486	£486	-	-	-	-	-	-	-	£972
Fees	£180,000	-	-	-	50,000	£50,000	£50,000	£50,000	£41,667	£18,297	£439,964
Total emoluments relating to 2007-08	£180,000	£372,246	£287,670	£287,184	£50,000	£50,000	£50,000	£50,000	£41,667	£18,297	£1,387,064

(1) Changes of Director in 2007-08 and 2008-09: JM Strachan was appointed a Director on 1 June 2007; A Carmwath resigned as a Director on 13 August 2007; RJ Aytling was appointed a Director on 3 April 2008.

(2) The financial statements for the year ended 31 March 2009 include a provision of £333,960 (50.6PPBS of base salary) for annual cash bonus potentially payable to Executive Directors for performance in the financial year 2008-09. This provision has been estimated on the basis that performance in Ofwat's Overall Performance Assessment for 2008-09 will be 4th. The final amount to be paid to each Director will be determined when Ofwat publishes OPA results for 2008-09 in the autumn of 2009, and could be higher or lower.

(3) Benefits in kind relate to receipt of private medical insurance, ill health cover and life insurance.

(4) An annual performance bonus of £315,172 was provided for in the Report and Accounts for 2007-08 and was estimated on the basis that OPA performance on 2007-08 would be 4th.

(5) The actual annual performance bonus in respect of 2007-08 totalled £335,328 and was paid in November 2008, following publication of Ofwat's OPA report for 2007-08, which confirmed Welsh Water's position as joint 3rd.

The highest paid Director in 2008-09 was NC Annett who received emoluments of £392,114 (2008: NC Annett £372,246).

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. Chris Jones is a Non-Executive Director of the Principality Building Society, in respect of which he retains a fee of £30,600 per annum.

Recommendation

The Committee believes that the Remuneration Policy continues to provide the right balance of fixed and variable pay to retain and reward Executive Directors for the attainment of the challenging goals the Board has set for the Company. Accordingly, the Committee recommends the Members of Glas Cymru to approve this 2009 Remuneration Report.



John Bryant
Chairman: Remuneration Committee
5 June 2009

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; and
- » 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
5 June 2009

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 2009 which comprise the Consolidated Income Statement, the Consolidated Statement of Recognised Income and Expense, the Consolidated 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 Business 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 Business and Financial Review, the Corporate Governance Statement and all of the other information set out on the contents page. 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 2006 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 to form an opinion on the effectiveness of the company's corporate governance procedures or its risk and control procedures.

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 2009 and of its loss 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 2009.
- » 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.

Priscilla Jones
Chartered Accountants and Registered
Auditors, Cardiff | 5 June 2009

Primary statements

Consolidated Income Statement for the year ended 31 March 2009

	Note	£m	2009 £m	As restated 2008 £m
Revenue			657.2	622.9
Operating costs:				
- Operational expenditure	4		(266.9)	(234.2)
- Infrastructure renewals expenditure	4		(101.1)	(97.5)
- Depreciation and amortisation	4		(133.5)	(122.3)
- (Loss)/profit on disposal of fixed assets	4		(0.8)	0.8
Operating profit			154.9	169.7
Financing costs:				
- Interest payable and similar charges	3a	(174.3)		(171.4)
- Interest receivable	3a	8.6		12.2
- Fair value losses on derivative financial instruments	3b	(86.5)		(47.9)
			(252.2)	(207.1)
Loss before taxation	4		(97.3)	(37.4)
Taxation (charge)/credit	5a		(5.6)	39.3
(Loss)/profit for the year			(102.9)	1.9

The comparative has been restated to reflect the impact of the accounting policy change in respect of defined benefit pension costs (see note 1).

	2009 £m	As restated 2008 £m
(Loss)/profit before taxation and fair value adjustments		
Loss before taxation per income statement	(97.3)	(37.4)
Effect of fair value losses on derivative financial statements	86.5	47.9
(Loss)/profit for the year before taxation and fair value adjustments	(10.8)	10.5

Primary statements

Consolidated Statement of Recognised Income and Expense for the year ended 31 March 2009

	Note	2009 £m	As restated 2008 £m
(Loss)/profit for the year		(102.9)	1.9
Actuarial (loss)/gain recognised in the pension scheme	19	(10.4)	3.3
Movement on deferred tax asset relating to pension scheme	5a	2.9	(1.0)
Total recognised (losses)/gains for the year		(110.4)	4.2

The comparative has been restated to reflect the impact of the accounting policy change in respect of defined benefit pension costs (see note 1).

Consolidated Statement of Changes in Reserves for the year ended 31 March 2009

	2009 £m	2008 £m
Reserves at 1 April	(41.7)	(45.9)
Total recognised (losses)/gains for the year	(110.4)	4.2
Reserves at 31 March	(152.1)	(41.7)

There were no changes in reserves of the parent company during the year (2008: none).

Consolidated Balance Sheet as at 31 March 2009

	Note	2009 £m	2008 £m
Assets			
Non-current assets			
Property, plant and equipment	6	2,980.0	2,893.4
Intangible assets	7	46.2	25.1
Investments	8a	-	-
Financial assets:			
- derivative financial instruments	13	-	2.5
Retirement benefit obligations	19	-	2.0
		3,026.2	2,923.0
Current assets			
Trade and other receivables	9	102.2	118.3
Financial assets:			
- derivative financial instruments	13	26.0	6.9
Cash and cash equivalents	10	139.3	124.1
		267.5	249.3
Liabilities			
Current liabilities			
Trade and other payables	11	(129.5)	(123.9)
Financial liabilities:			
- borrowings	12	(20.0)	(25.1)
- derivative financial instruments	13	(2.1)	(3.3)
		(151.6)	(152.3)
Net current assets		115.9	97.0
Non-current liabilities			
Trade and other payables	11	(3.0)	(2.3)
Financial liabilities:			
- borrowings	12	(2,739.7)	(2,623.4)
- derivative financial instruments	13*	(181.7)	(77.4)
Retirement benefit obligations	19	(7.8)	-
Provisions	15	(9.2)	(8.5)
		(2,941.4)	(2,711.6)
Net assets before deferred tax		200.7	308.4
Deferred tax - net	5b	(352.8)	(350.1)
Net liabilities		(152.1)	(41.7)
Deficit		(152.1)	(41.7)

The financial statements on pages 45 to 76 were approved by the Board of directors on 5 June 2009 and were signed on its behalf by:



N C Annett
Managing Director



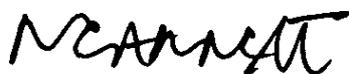
C A Jones
Finance Director

Primary statements

Parent Company Balance Sheet as at 31 March 2009

	Note	2009 £m	2008 £m
Assets			
Non-current assets			
Investment in subsidiaries	8b	-	-
Trade and other receivables	9b	3.4	3.4
		3.4	3.4
Current assets			
Cash and cash equivalents	10	0.1	0.1
		0.1	0.1
Liabilities			
Current liabilities			
Trade and other payables	11	(3.5)	(3.5)
		(3.5)	(3.5)
Net assets			
		-	-
Reserves			
Retained earnings		-	-
Total reserves		-	-

The financial statements on pages 45 to 76 were approved by the Board of directors on 5 June 2009 and were signed on its behalf by:



N C Annett
Managing Director



C A Jones
Finance Director

Consolidated Cash Flow Statement for the year ended 31 March 2009

	Note	2009 £m	2008 £m
Cash flows from operating activities			
Cash generated from operations	16a	309.1	268.8
Interest received		9.8	11.0
Interest paid	16b	(129.4)	(212.3)
Net cash inflow from operating activities		189.5	67.5
Cash flows from investing activities			
Purchase of property, plant and equipment		(257.0)	(190.9)
Grants and contributions received		13.6	17.7
Proceeds from sale of property, plant and equipment		(0.8)	0.8
Net cash used in investing activities		(244.2)	(172.4)
Net cash outflow before financing activities		(54.7)	(104.9)
Cash flows from financing activities			
Long term loans and finance leases received		85.0	85.0
Revolving credit facility and term loan repayments		(4.4)	(4.4)
Capital element of finance lease payments		(10.4)	(9.3)
Other loan repayments		(0.3)	(0.3)
Net cash generated from financing activities		69.9	71.0
Increase/(decrease) in net cash	17	15.2	(33.9)
Net cash at 1 April		124.1	158.0
Net cash at 31 March	10	139.3	124.1

The parent company had no cash flows during the year (2008: none).

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.

In the current year, Glas Cymru has applied the following Interpretations which are or have become effective:

- IFRIC 12 Service Concession Arrangements
- IFRIC 14 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction.

The application of these Interpretations has no material effect on the preparation or presentation on the results or financial position for the current or prior accounting periods, and accordingly no prior period adjustment has been required.

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:

- IAS 1 Presentation of Financial Statements (revisions)
- IAS 16 Property, Plant and Equipment (revision)
- IAS 19 Employee Benefits (revision)
- IAS 20 Government Grants and Disclosure of Government Assistance (revision)
- IAS 23 Borrowing Costs (revisions)

- IAS 27 Consolidated and Separate Financial Statements (revisions)
- IAS 28 Investments in Associates (revisions)
- IAS 29 Financial Reporting in Hyperinflationary Economies (revision)
- IAS 31 Interests in Joint Ventures (revisions)
- IAS 32 Financial Instruments: Presentation (revision)
- IAS 36 Impairment of Assets (revision)
- IAS 38 Intangible Assets (revision)
- IFRS 1 First-time Adoption of International Financial Reporting Standards (revision)
- IFRS 2 Share-based Payment (revision)
- IFRS 3 Business Combinations (revision)
- IFRS 5 Non-current Assets Held for Sale and Discontinued Operations (revision)
- IFRS 8 Operating Segments
- IFRIC 13 Customer Loyalty Programmes
- IFRIC 15 Agreements for the Construction of Real Estate
- IFRIC 16 Hedges of a Net Investment in a Foreign Operation
- IFRIC 17 Distributions of Non-cash Assets to Owners

The application of the revisions to IAS 23 – Borrowing Costs will be required in Glas Cymru's financial statements for the year ending 31 March 2010. The revisions remove the option of immediately recognising as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale. An entity is, therefore, required to capitalise borrowing costs as part of the cost of such assets. The revised standard will require a change to Glas Cymru's existing policy – it is likely that some borrowing costs which are currently expenses as incurred will need to be capitalised and then amortised over the useful economic lives of the related assets.

The presentational impact of the other standards and interpretations is being assessed, but 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.

Change of accounting policy

The group has changed its accounting policy in respect of defined benefit pension scheme costs. The group's defined benefit scheme service cost is included in operating costs and the expected return on scheme assets and interest on scheme liabilities are included in financing costs, while actuarial gains and losses are recognised in full in the consolidated Statement of Recognised Income and Expense (SORIE). Previously, all actuarial movements had been reflected in full in the Income Statement as permitted under IAS 19. The comparative year's Income Statement and SORIE have therefore been restated to reflect this presentational change; there is no impact on the balance sheet.

The impact of this restatement is to reduce the reported profit after tax for the year ended 31 March 2008 by £2.3m, and to reduce the reported loss after tax for the year ended 31 March 2009 by £7.5m.

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 2009

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been applied consistently 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 value is included in revenue. See the critical accounting estimates section for further details.

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 and 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).

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.

Infrastructure assets

Infrastructure assets comprise principally impounding reservoirs and a network of underground water and wastewater systems. 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 principally from 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 and 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 amortised 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 and equipment' with the corresponding liability to the lessor included within 'financial 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.

Notes to the financial statements

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 revalued periodically 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. This was used as a 'deemed cost' for the group's fixed assets under the transitional rules available on first time adoption of 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 receivables/payables arising from these contracts is to recognise gain payables over the period to which the charge relates, and pain receivables as income only when final agreement with the relevant service partner has been reached.

Trade receivables and their impairment

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost less provision for impairment. They 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 assessed collectively for impairment based on their ageing. Movements in the provision for impairment 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

i) Defined benefit scheme

A majority of the group's employees belongs to the group's defined benefit pension scheme, which is funded by both employer's and employees' contributions. 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.

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.

The group's defined benefit scheme service cost, being the increase in the present value of the liabilities expected to arise from employee service in the period, is included in operating costs. The expected return on scheme assets and interest on scheme liabilities are included in financing costs in the income statement. Actuarial gains and losses on experience adjustments and changes in actuarial assumptions are recognised in full in the period in which they occur in the consolidated statement of recognised income and expense.

ii) Defined contribution scheme

The group also operates a defined contribution scheme for those employees who are not members of the defined benefit scheme. Obligations for contributions to the scheme are recognised as an expense in the Income Statement in the period in which they arise.

Financial liabilities

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.

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.

Derivative financial instruments

Derivative instruments utilised by the group are interest rate, inflation and currency 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 subsequently re-measured at fair value (based on market price data from relevant counterparties).

During the year to 31 March 2009, none of the group's derivatives qualified for hedge accounting under IAS 39 (2008: none). These instruments are carried at fair value with changes in fair value being recognised immediately in the income statement.

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 (2009 and 2008: 28%).

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 Dŵr 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

The group has a prudent policy for investing cash and short term bank deposits ('cash investments'). Counterparties for cash investments must meet minimum short term and/or long term credit ratings as published by Standard & Poor's ('S&P'), Moody's Investor Service Limited ('Moody's') and Fitch Ratings Limited ('Fitch'). The minimum short term rating, for cash deposits of up to one year, is A1/P1/F1 and the minimum long term rating, for cash deposits over one year, is AA-/Aa3/AA- each for S&P, Moody's and Fitch respectively. The Board reviews counterparties for cash investments and the credit limit assigned to each annually.

The group has continued to follow a cautious policy for investing cash deposits as a response to the situation in the banking market. In consequence, with the exception of the group's clearing bank (which has a long-term rating of A+/A3/AA-), all new cash investments must meet the minimum long term rating and have a maximum investment period of one month. The maximum cash investment with a single counterparty was £69m (2008: £25m).

Interest rate and currency risk

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 floating rate interest 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 exposes 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.

Notes to the financial statements

The group analyses its interest rate exposure on a dynamic basis. Various scenarios are simulated taking into consideration refinancing, renewal of existing positions, alternative financing and hedging. Of total borrowings of £2,760m as at 31 March 2009 (2008: £2,649m), only £156m related to floating rate debt (2008: £162m). The group therefore considers overall interest rate exposure at the balance sheet date to be minimal.

As at 31 March 2009, 94% (2008: 94%) of the group's gross debt was at fixed or index-linked ('RPI') rates of interest after taking into account interest rate and RPI swaps. The 'hedges' 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. Accordingly, all movements in the fair value of derivatives are reflected in the income statement.

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. There were no foreign currency borrowings as at 31 March 2009 (2008: £nil).

Refinancing risk

Refinancing 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 of £2,760m can fall due in any 24 month period.

Liquidity risk

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

Under the Common Terms Agreement which governs the group's obligations to its bond holders and other financial creditors, the group is required to have cash available to fund operations for a duration of 18 months. As at 31 March 2009, the group had committed undrawn borrowing facilities of £420m (2008: £345m) and cash and cash equivalents (excluding debt service payments account) of £124m (2008: £112m).

There is also a special liquidity facility of £150m; this is required 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.

Capital risk management

The group's objective when managing capital is to safeguard its ability to continue as a going concern. Given the regulatory environment in which the group operates, the group monitors capital on the basis of the gearing ratio. This is calculated as net debt (as defined in the group's borrowing covenants) as a proportion of its Regulatory Capital Value (RCV) as linked to movements in the Retail Price Index and determined by Ofwat.

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 operate at a level of gearing of around 70%.

In respect of the risks detailed above, further quantitative disclosures are provided in note 14.

Critical accounting estimates

The preparation of financial statements which conform to 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.

Provision for impairment of trade receivables

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 provision for impairment would increase or decrease by £5.0 million (2008: £4.3 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 £0.7 million (2008: £0.8 million).

Measured income accrual

Revenue includes an accrual for unbilled charges at the year-end. The accrual is estimated using a defined methodology based upon the weighted average water consumption by tariff, which is calculated using 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 (2008: £2.2 million).

2 | Segmental information

The directors consider that there is only one reporting segment, being the operation of 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 has only 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

a | Net interest before fair value losses on derivative financial instruments

	GROUP	
	2009 £m	As restated 2008 £m
Interest payable on bonds	(86.1)	(84.6)
Indexation on index-linked bonds	(41.4)	(30.4)
Interest payable on finance leases	(37.1)	(46.1)
Other loan interest	(7.4)	(8.5)
Other Interest payable and finance costs	(2.5)	(1.9)
Interest credit on pension scheme liabilities	0.2	0.1
Interest payable	(174.3)	(171.4)
Interest receivable	8.6	12.2
Net interest payable before fair value adjustments	(165.7)	(159.2)

The comparative has been restated to reflect the impact of the accounting policy change in respect of defined benefit pension costs (see note 1).

b | Fair value losses on derivative financial instruments

Derivative financial instruments are held for economic hedging purposes although they do not qualify as accounting hedges under IAS 39. Consequently, the group's interest rate and index-linked swaps are fair valued at each balance sheet date with the movement (net loss or gain) disclosed in the income statement. Over the life of these swaps, if held to maturity, these fair value adjustments will reverse and reduce to zero. (See note 13 in respect of derivative financial instruments held on the balance sheet.)

	GROUP	
	2009 £m	2008 £m
Fair value losses on interest rate swaps	(28.3)	(4.0)
Fair value losses on index-linked swaps	(58.2)	(43.9)
Total fair value losses on derivative financial instruments	(86.5)	(47.9)
Deferred tax effect at 28% (2008: 28%) of fair value losses	24.2	13.4
Net of tax impact of fair value losses	(62.3)	(34.5)

During the year to 31 March 2008, swaps with a nominal value of £433m were closed out with a payment of £32.5m.

4 | Loss before taxation

The following items have been included in arriving at the loss before taxation:

	GROUP	
	2009 £m	As restated 2008 £m
Operating charges from outsourced activities		
- Operating services agreements	138.4	116.1
- Customer services agreement	19.5	19.0
- Laboratories and analytical services	6.7	6.3
- Other contracts	14.2	13.9
	178.8	155.3
Employee costs (note 18)		
- Wages and salaries	10.7	9.2
- Social security	1.0	1.0
- Pension costs (excluding actuarial (loss)/gain)	1.0	1.7
	12.7	11.9
Research and development expenditure	0.5	0.5
Trade receivables impairment	18.8	13.4
Rates	25.5	24.1
Environment Agency charges	14.9	14.3
Fees paid to auditors (see below)	0.2	0.2
Staff costs capitalised	(5.7)	(5.2)
Other operating charges	21.2	19.7
Total operational expenditure	266.9	234.2
Infrastructure renewals expenditure	101.1	97.5
Depreciation and amortisation		
- Owned assets	89.1	81.2
- Under finance leases	40.7	40.2
- Amortisation of intangible assets	3.7	0.9
	133.5	122.3
Loss/(profit) on disposal of fixed assets	0.8	(0.8)
	502.3	453.2

Notes to the financial statements

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	
	2009 £'000	2008 £'000
Non-discretionary audit fees		
Statutory audit of parent company and consolidated financial statements	11	11
Statutory audit of subsidiary companies	75	72
Total statutory audit fees	86	83
Review of interim financial statements	21	20
Regulatory audit services pursuant to legislation	33	29
Review of draft business plan (required by Ofwat)	81	-
Total audit fees	221	132
Other services		
Tax advisory services	10	27
Other	2	4
Total other services	12	31
Total cost of services provided by the group's auditor	233	163

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

In addition to the above services, PricewaterhouseCoopers LLP acted as auditor to the DCWW 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 £13,000 (2008: £11,000).

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

a | Taxation (charge)/credit

Analysis of (charge)/credit in the year

	GROUP	
	2009 £m	2008 £m
Deferred tax		
- Current year movements	30.3	9.2
- Adjustment in respect of prior years	4.0	3.4
- Effect of tax rate change	-	25.7
- Effect of abolition of Industrial Buildings Allowances	(37.0)	-
Taxation (charge)/credit	(2.7)	38.3
Analysed as:		
(Charge)/credit to Income Statement	(5.6)	39.3
Credit/(charge) to Statement of Recognised Income and Expense	2.9	(1.0)
	(2.7)	38.3

The effective rate of tax for the year is higher (2008: lower) than the standard rate of corporation tax in the UK (2009: 28%, 2008: 30%). The differences are explained below:

	GROUP	
	2009 £m	2008 £m
Loss before tax	(97.3)	(37.4)
Loss before tax multiplied by the corporation tax rate in the UK of 28% (2008: 30%)	(27.2)	(11.2)
Effects of:		
- Adjustments in respect of prior years	(4.0)	(3.9)
- Other permanent differences	(0.2)	0.4
- Effect of tax rate change	-	(24.6)
- Effect of abolition of Industrial Buildings Allowances	37.0	-
- Movement on deferred tax asset relating to pension scheme	(2.9)	1.0
Total taxation charge/(credit)	2.7	(38.3)

The charge of £37m provides for the phasing out of Industrial Buildings Allowances announced in the 2007 budget.

b | Deferred tax

Deferred tax is calculated in full on temporary differences under the liability method using a tax rate of 28% (2008: 28%)

The movement in the deferred tax provision is as shown below:

	GROUP		COMPANY	
	2009 £m	2008 £m	2009 £m	2008 £m
At 1 April	350.1	388.4	-	-
Charge/(credit) to Income Statement	5.6	(39.3)	-	-
(Credit)/charge to Statement of Recognised Income and Expense	(2.9)	1.0	-	-
At 31 March	352.8	350.1	-	-

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	
	2009 £m	2008 £m	2009 £m	2008 £m
Effect of:				
Tax allowances in excess of depreciation	443.7	395.1	-	-
Capital gains rolled over	41.6	46.5	-	-
Deferred tax on tax losses carried forward	(80.1)	(65.8)	-	-
Deferred tax on losses on derivative financial instruments	(44.7)	(19.9)	-	-
Pensions	(2.9)	(0.9)	-	-
Other tax differences	(4.8)	(4.9)	-	-
Provision for deferred tax	352.8	350.1	-	-

Notes to the financial statements

6 | 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 2008	33.0	1,457.4	2,232.5	222.9	3,945.8
Additions net of grants and contributions	1.4	55.7	150.9	67.4	275.4
Disposals	-	-	-	(64.1)	(64.1)
At 31 March 2009	34.4	1,513.1	2,383.4	226.2	4,157.1
Accumulated depreciation					
At 1 April 2008	16.3	98.8	772.9	164.4	1,052.4
Charge for the year	0.5	32.4	86.5	10.5	129.9
Released on disposal	-	-	-	(5.2)	(5.2)
At 31 March 2009	16.8	131.2	859.4	169.7	1,177.1
Net book value					
At 31 March 2009	17.6	1,381.9	1,524.0	56.5	2,980.0

The net book value of property, plant and equipment includes £160.9m in respect of assets in the course of construction (2008: £158.1m).

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 2007	32.9	1,412.7	2,118.1	218.2	3,781.9
Additions net of grants and contributions	0.1	133.7	114.4	4.7	252.9
Disposals	-	(89.0)	-	-	(89.0)
At 31 March 2008	33.0	1,457.4	2,232.5	222.9	3,945.8
Accumulated depreciation					
At 1 April 2007	15.9	71.2	691.1	156.8	935.0
Charge for the year	0.4	31.6	81.8	7.6	121.4
Released on disposal	-	(4.0)	-	-	(4.0)
At 31 March 2008	16.3	98.8	772.9	164.4	1,052.4
Net book value					
At 31 March 2008	16.7	1,358.6	1,459.6	58.5	2,893.4

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 2008	611.8	598.1	1,209.9
Additions	-	60.0	60.0
At 31 March 2009	611.8	658.1	1,269.9
Accumulated depreciation			
At 1 April 2008	43.9	187.5	231.4
Charge for the year	7.7	33.0	40.7
At 31 March 2009	51.6	220.5	272.1
Net book value			
At 31 March 2009	560.2	437.6	997.8
GROUP	Infrastructure assets £m	Operational structures £m	Total £m
Prior year			
Cost			
At 1 April 2007	526.8	598.1	1,124.9
Additions	85.0	-	85.0
At 31 March 2008	611.8	598.1	1,209.9
Accumulated depreciation			
At 1 April 2007	36.7	154.5	191.2
Charge for the year	7.2	33.0	40.2
At 31 March 2008	43.9	187.5	231.4
Net book value			
At 31 March 2008	567.9	410.6	978.5

The parent company owns no property, plant or equipment.

Notes to the financial statements

7 | Intangible assets

Intangible assets comprise computer software and related system developments.

GROUP	Cost £m	Amortisation £m	Net book value £m
Current year			
At 1 April 2008	76.7	(51.6)	25.1
Additions	24.8	(3.7)	21.1
At 31 March 2009	101.5	(55.3)	46.2
Prior year			
At 1 April 2007	57.7	(50.7)	7.0
Additions	19.0	(0.9)	18.1
At 31 March 2008	76.7	(51.6)	25.1

The net book value of intangible assets includes £18.1m in respect of assets in the course of construction (2008: £19.0m).

The parent company owns no intangible fixed assets.

8 | Fixed asset investments

a | Group

Cost and net book value	2009 £m	2008 £m
At 1 April and 31 March	-	-

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

	Principal activity	Country of incorporation	Holding
Water Research Centre (1989) Plc	Water research	England and Wales	'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%

9 | Trade and other receivables

	GROUP		COMPANY	
	2009 £m	2008 £m	2009 £m	2008 £m
a Amounts falling due within one year				
Trade receivables	109.4	101.0	-	-
Less provision for impairment of receivables	(70.6)	(58.8)	-	-
Trade receivables - net	38.8	42.2	-	-
Prepayments and accrued income	62.0	62.9	-	-
Other receivables	1.4	13.2	-	-
	102.2	118.3	-	-
b Amounts falling due after more than one year				
Amounts owed by group undertakings	-	-	3.4	3.4
			3.4	3.4
Total trade and other receivables	102.2	118.3	3.4	3.4

All non-current receivables are due within five years from the balance sheet date.

As at 31 March 2009, based on a review of historical collection rates it was considered that £70.6m of trade receivables were impaired and these have therefore been provided for (2008: £58.8m). The impaired receivables mainly relate to measured and unmeasured water supply debtors.

The ageing of receivables was as follows:

	Total £m	Provided for £m	Net £m
Current year			
Trade receivables			
Under one month	10.1	(3.4)	6.7
Between one and six months	18.0	(8.2)	9.8
Between six months and one year	21.4	(7.2)	14.2
Between one and two years	21.9	(16.3)	5.6
Between two and three years	15.9	(13.6)	2.3
Over three years	22.1	(21.9)	0.2
	109.4	(70.6)	38.8
Prior year			
Trade receivables			
Under one month	14.2	(3.4)	10.8
Between one and six months	18.7	(7.1)	11.6
Between six months and one year	17.3	(6.2)	11.1
Between one and two years	20.9	(14.3)	6.6
Between two and three years	13.3	(11.2)	2.1
Over three years	16.6	(16.6)	-
	101.0	(58.8)	42.2

Notes to the financial statements

Movements on the provision for impairment of trade receivables are as follows:

	2009 £m	2008 £m
At 1 April	58.8	53.0
Charge to Income Statement	18.1	13.0
Receivables written off during the year as uncollectable	(6.3)	(7.2)
At 31 March	70.6	58.8

The creation and release of provision for impaired receivables have been included in operational expenditure.

The other classes within trade and other receivables do not contain impaired assets. All trade and other receivables are denominated in sterling.

10 | Cash and cash equivalents

	GROUP		COMPANY	
	2009 £m	2008 £m	2009 £m	2008 £m
Cash at bank and in hand	3.0	2.9	0.1	0.1
Short-term deposits	136.3	121.2	-	-
	139.3	124.1	0.1	0.1

The effective interest rate on short-term deposits as at 31 March 2009 was 0.6% (2008: 5.5%) and these deposits have an average maturity of 8 days (2008: 13 days). All cash and cash equivalents were held in sterling.

11 | Trade and other payables

	GROUP		COMPANY	
	2009 £m	2008 £m	2009 £m	2008 £m
Current				
Trade payables	28.2	16.1	-	-
Capital payables	53.4	55.6	-	-
Amounts due to group undertakings	-	-	3.5	3.5
Other taxation and social security	0.4	0.4	-	-
Accruals and deferred income	47.5	51.8	-	-
	129.5	123.9	3.5	3.5
Non-current				
Deferred income	3.0	2.3	-	-

12 | Financial liabilities – borrowings

	GROUP		COMPANY	
	2009 £m	2008 £m	2009 £m	2008 £m
Current				
Interest accruals	6.9	12.4	-	-
Unamortised bond premium	0.5	0.5	-	-
Unamortised bond issue costs	(0.7)	(0.7)	-	-
European Investment Bank loan	4.4	4.4	-	-
Local authority loans	0.3	0.3	-	-
Finance lease obligations	8.6	8.0	-	-
	20.0	24.9	-	-
Non-current				
Interest accruals	35.0	29.7	-	-
Bonds	1,664.5	1,623.0	-	-
Unamortised bond premium	11.8	12.4	-	-
Unamortised bond issue costs	(4.2)	(4.9)	-	-
European Investment Bank loan	146.8	126.3	-	-
Local authority loans	2.3	2.6	-	-
Finance lease obligations	883.5	834.5	-	-
	2,739.7	2,623.6	-	-

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.

The group's Class A Bonds of £902.3m (2008: £875.8m) benefit from a guarantee from MBIA UK Insurance Limited ('MBIA'). MBIA's credit rating has been reduced to B3 and BBB+ by Moody's and Standard and Poor's respectively, and is no longer rated by Fitch Ratings. The credit rating of the Class A bonds has therefore defaulted to the higher underlying rating of these bonds, of A3/A/A from Moody's, Standard & Poor's and Fitch Ratings respectively. The underlying rating reflects the standalone credit quality of these bonds without the benefit of the MBIA guarantee, and is the same as the credit ratings of the group's Class B bonds of £637.2m (2008: £622.2m).

Notes to the financial statements

13 | 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 (see note 3b).

GROUP - 2009	FAIR VALUES	
	Assets £m	Liabilities £m
Current		
Index-linked swaps	18.6	(1.4)
Interest rate swaps	7.4	(0.7)
	26.0	(2.1)
Non-current		
Index-linked swaps	-	(119.7)
Interest rate swaps	-	(62.0)
	-	(181.7)
Total	26.0	(183.8)

GROUP - 2008	FAIR VALUES	
	Assets £m	Liabilities £m
Current		
Index-linked swaps	6.9	(1.4)
Interest rate swaps	-	(1.9)
	6.9	(3.3)
Non-current		
Index-linked swaps	2.5	(52.3)
Interest rate swaps	-	(25.1)
	2.5	(77.4)
Total	9.4	(80.7)

In accordance with IAS 39, 'Financial instruments: Recognition and measurement', the group has reviewed all contracts for embedded derivatives that are required to be accounted for separately if they do not meet certain requirements set out in the standard. The group 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 2009 the interest rate swaps fix the interest rate on £192 million (2008: £192 million) of floating rate liabilities held by the group. The maturity date of the swap is 31 March 2031 and the quarterly fixed interest rate is 5.67%.

In addition £568 million (2008: £571 million) of finance lease liabilities are converted from 3 month to 12 month floating for a period of one year; the swaps expire on 31 March 2010.

Index-linked swaps

Finance lease swaps

The index-linked swaps have the effect of index-linking the interest rate on £617 million (2008: £622 million) of finance lease liabilities by reference to the retail price index ('RPI').

The notional amount of the swaps as at 31 March 2009 is £563 million (2008: £571 million), representing the average balance on the finance leases subject to floating interest rates for the year to 31 March 2010. The notional amount amortises over the life of the swaps to match the average floating rate balances of the leases. These swaps are matched against the same liabilities as the finance lease interest rate swaps noted above.

The principal terms are as follows:

Notional Amount:	£563 million (amortising)
Average swap maturity:	24 years
Average interest rate:	1.64% (fixed) plus RPI

Bond swap

The index-linked swaps have the effect of index-linking the interest rate on £100 million of fixed rate bonds by reference to the RPI.

The principal terms are as follows:

Indexed notional Amount:	£111 million
Swap maturity:	48 years
Interest rate:	1.35% (indexed by RPI)

14 | Financial risk management

The policies of the group in respect of financial risk management are included in the accounting policies note on page 53.

The numerical financial instrument disclosures as required by IFRS 7 are set out below.

a | Interest rate risk

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

	2009	2008
Assets		
Cash and cash equivalents	0.6%	5.5%
Liabilities		
Bonds	5.6%	5.5%
European Investment Bank loans	2.1%	6.1%
Local authority loans	5.3%	5.8%
Finance lease obligations	4.8%	5.6%

Trade and other receivables and payables are not interest-bearing.

Notes to the financial statements

The effective interest rates ignore the effect of the interest rate and index-linked swaps set out in note 13. They also exclude the indexation charge applicable to the index-linked bonds.

b | Liquidity risk

GROUP - 2009	Within 1yr £m	1- 2 years £m	2-5 years £m	> 5 years £m	Total £m
Assets					
Cash and cash equivalents	139.3	-	-	-	139.3
Trade and other receivables	102.2	-	-	-	102.2
	241.5	-	-	-	241.5
Liabilities					
Bonds	0.5	125.6	1.8	1,548.9	1,676.8
European Investment Bank loan	4.4	8.9	40.4	97.5	151.2
Local authority loans	0.3	0.3	1.0	1.0	2.6
Finance lease obligations	8.6	9.9	51.1	822.5	892.1
Trade and other payables	129.5	0.3	0.3	1.4	131.5
	143.3	145.0	94.6	2,471.3	2,854.2

GROUP - 2008	Within 1yr £m	1- 2 years £m	2-5 years £m	> 5 years £m	Total £m
Assets					
Cash and cash equivalents	124.1	-	-	-	124.1
Trade and other receivables	118.3	-	-	-	118.3
	242.4	-	-	-	242.4
Liabilities					
Bonds	0.5	0.5	126.7	1,508.2	1,635.9
European Investment Bank loan	4.4	4.4	35.9	86.0	130.7
Local authority loans	0.3	0.3	1.0	1.3	2.9
Finance lease obligations	8.0	7.0	33.1	794.4	842.5
Trade and other payables	123.9	0.3	0.3	1.7	126.2
	137.1	12.5	197.0	2,391.6	2,738.2

As at 31 March 2009, the Bonds maturing between 1-2 years represent £125 million of subordinated 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 of 5.75%.

The minimum lease payments under finance leases fall due as follows:

	2009 £m	2008 £m
Gross finance lease liabilities		
Within one year	30.9	55.8
Between two and five years	175.9	205.3
After five years	1,165.5	1,388.2
	1,372.3	1,649.3
Future interest	(480.2)	(806.8)
Net finance lease liabilities	892.1	842.5
Net finance lease liabilities are repayable as follows		
Within one year (note 12)	8.6	8.0
Between two and five years	61.1	40.1
After five years	822.4	794.4
Total over one year (note 12)	883.5	834.5

c | Fair values

The fair values of the group's derivative financial instruments are set out in note 13. The following table summarises the fair value and book value of the group's bonds.

	2009		2008	
	Book value £m	Fair value £m	Book value £m	Fair value £m
Bonds (note 12)	1,676.8	1,603.1	1,635.9	1,778.3

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

d | Borrowing facilities

As at 31 March 2009, the group had available undrawn committed borrowing facilities of £420m expiring in more than one year, in respect of which all conditions precedent had been met (2008: £345m).

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.

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

Notes to the financial statements

e | Capital risk management

Gearing ratios

	2009 £m	2008 £m
Total borrowings	(2,759)	(2,649)
Less: cash and cash equivalents	139	124
Net debt	(2,620)	(2,525)
RCV	3,626	3,529
Total capital	1,006	1,004
Less: unamortised bond costs	(5)	(6)
Total capital per bond covenants	1,001	998
Gearing ratio	72%	72%

As set out on page 54, the group monitors its capital structure based on a regulatory gearing ratio which compares its net debt to the Ofwat-determined RCV.

15 | Provisions

	GROUP		Total £m
	Restructuring provision £m	Uninsured loss provision £m	
At 1 April 2008	1.2	7.3	8.5
Charged to income statement	0.2	2.5	2.7
Utilised in year	-	(2.0)	(2.0)
At 31 March 2009	1.4	7.8	9.2

The parent company has no provisions at 31 March 2009 (2008: nil).

Restructuring provision

This provision relates to estimated dilapidation costs, which will be incurred over the next two years.

Provision for uninsured losses

This provision is in respect of uninsured losses and instances where insurance does not cover a deductible amount.

The utilisation period of these liabilities is uncertain due to the nature of claims, but is estimated to be five years.

16 | Net cash inflow from operating activities**a | Cash generated from operations**

Reconciliation of operating profit to cash generated from operations:

	GROUP	
	2009 £m	As restated 2008 £m
Operating profit	154.9	169.7
Adjustments for:		
- Depreciation and amortisation	133.5	122.3
- Loss/(profit) on disposal of fixed assets	0.8	(0.8)
- Changes in working capital:		
Decrease/(increase) in trade and other receivables	11.1	(24.3)
Increase/(decrease) in trade and other payables	8.1	6.1
Pension contributions in excess of operating costs	-	(4.1)
Decrease in provisions	0.7	(0.1)
	19.9	(22.4)
Cash generated from operations	309.1	268.8

The comparative has been restated to reflect the impact of the accounting policy change in respect of defined benefit pension costs (see note 1).

b | Interest paid

	GROUP	
	2009 £m	As restated 2008 £m
Interest payable per income statement	174.3	171.4
Less non-cash items:		
- Indexation on index-linked bonds	(41.4)	(30.4)
- Amortisation of bond issue costs	(0.7)	(0.7)
- Interest credit on pension scheme liabilities	0.2	0.1
- Amortisation of bond issue premium	0.5	0.5
- Decrease in prepayments	(3.7)	-
- Decrease in accruals	0.2	38.9
Swap termination payment	-	32.5
	(44.9)	40.9
Interest paid	129.4	212.3

31 March 2007 fell on a Saturday and in consequence a majority of the annual finance lease and bond interest payments in respect of the year ended 31 March 2007 were due and actually paid on 2 April 2007, i.e. during the following year.

31 March 2008 was a Monday and all annual finance lease and bond interest payments due for the year were made by this date. A further £32.5m was paid in April 2007 on termination of swaps no longer required. As a result, interest paid in the comparative year was significantly higher than in the current year.

Notes to the financial statements

17 | Analysis and reconciliation of net debt

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

	GROUP		COMPANY	
	2009 £m	2008 £m	2009 £m	2008 £m
Cash and cash equivalents	139.3	124.1	0.1	0.1
Debt due after one year	(1,821.2)	(1,759.2)	-	-
Debt due within one year	(4.5)	(4.7)	-	-
Finance leases	(892.1)	(842.5)	-	-
Accrued interest	(41.9)	(42.1)	-	-
	(2,759.7)	(2,648.5)	-	-
Net debt	(2,620.4)	(2,524.4)	0.1	0.1

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

	GROUP		COMPANY	
	2009 £m	2008 £m	2009 £m	2008 £m
Net debt at start of year	(2,524.4)	(2,427.8)	0.1	0.1
Increase/(decrease) in net cash	15.2	(33.9)	-	-
Increase in debt	(69.9)	(71.0)	-	-
Increase in net debt arising from cashflows	(54.7)	(104.9)	-	-
Movement in accrued interest	0.2	38.9	-	-
Indexation of index-linked debt	(41.4)	(30.4)	-	-
Other non-cash movements	(0.1)	(0.2)	-	-
Movement in net debt during the year	(96.0)	(96.6)	-	-
Net debt at end of period	(2,620.4)	(2,524.4)	0.1	0.1

18 | Employees and directors

a | Staff costs for the group during the year

	2009 £m	2008 £m
Wages and salaries	10.7	9.2
Social security costs	1.0	1.0
Other pension costs	1.0	1.7
	12.7	11.9

Of the above, £5.7 million (2008: £5.2 million) has been charged to capital.

	2009 Number	2008 Number
Average monthly number of people (including executive directors) employed by the group		
Regulated water and sewerage activities	187	173

b | Parent company

The parent company had no employees (2008: nil) in the year. Full details of the directors' remuneration are included in the Directors' Remuneration Report set out on pages 38 to 42, which forms part of these Financial Statements.

19 | Pension commitments

The group operates a funded defined benefit pension scheme for current employees (based on final pensionable salary and pensionable service), 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 31 December 2005 and a new defined contribution scheme, the Dŵr Cymru Defined Contribution Scheme, was introduced from 1 January 2006.

Total pension costs in the year were as follows:

	2009 £'000	2008 £'000
Defined contribution scheme	122	591
Defined benefit scheme - excluding actuarial (loss)/gain	927	1,065
	1,049	1,656
Net actuarial (loss)/gain recognised in year	10,400	(3,339)
	11,449	(1,683)

Defined benefit scheme

A full actuarial valuation of the scheme was undertaken as at 31 March 2006 by Robert Davies of Quantum Advisory, an independent, professionally qualified actuary, using the attained age method. This valuation was updated at 31 March 2009 and the principal assumptions made by the actuaries were:

	2009	2008
Discount rate	6.2%	6.3%
Inflation assumption	2.7%	3.0%
Rate of increase in pensionable salaries	3.7%	4.0%
Rate of increase in pensions in payment	2.7%	3.0%
Post retirement mortality (life expectancy):		
- Current pensioners aged 65 - males	87.0 years	84.9 years
- Current pensioners aged 65 - females	89.9 years	87.9 years
- Future pensioners aged 65 (currently aged 45) - males	88.1 years	86.1 years
- Future pensioners aged 65 (currently aged 45) - females	90.9 years	89.1 years

Post retirement mortality assumptions are based on those in published actuarial tables 'PA92', relevant to members' year of birth with medium cohort adjustments.

Notes to the financial statements

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

	2009		2008	
	Expected return	Percentage of total assets	Expected return	Percentage of total assets
Equities	8.0%	59.0%	7.0%	59.5%
Bonds	5.0%	39.8%	6.0%	38.5%
Other	3.0%	1.2%	4.5%	2.0%

The amounts recognised in the Income statement are as follows:

	2009 £'000	2008 £'000
Current service cost (excluding member contributions)	878	1,074
Past service cost	151	125
Effect of curtailments or settlements	99	-
Total included within staff costs	1,128	1,199
Interest cost	2,353	2,273
Expected return on plan assets	(2,554)	(2,407)
Total included within interest payable and similar charges	(201)	(134)
Total recognised in the Income Statement	927	1,065

Note that the defined contribution scheme charge of £122,000 (2008: £591,000) has also been included within staff costs.

The amounts recognised in the Statement of Recognised Income and Expense are as follows:

	2009 £'000	2008 £'000
Actuarial loss on plan assets	(9,301)	(4,704)
Actuarial (loss)/gain on defined benefit obligation	(1,099)	8,043
Total recognised in the Statement of Recognised Income and Expense	(10,400)	3,339

The total recognised in the Balance Sheet is made up as follows:

	2009 £'000	2008 £'000
Present value of funded obligations	(40,577)	(37,416)
Plus unrecognised prior service costs	526	677
Fair value of plan assets	32,283	38,786
Net (liability)/asset recognised in the balance sheet	(7,768)	2,047

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

	2009 £'000	2008 £'000
At 1 April	37,416	41,009
Current service cost (including member contributions)	1,241	1,421
Past service cost - vested benefits	-	125
Past service cost - non vested benefits	-	677
Interest cost	2,353	2,273
Benefits paid (net of transfers in)	(919)	(46)
Settlement	(613)	-
Actuarial loss/(gain)	1,099	(8,043)
At 31 March	40,577	37,416

Changes in the fair value of plan assets are as follows:

	2009 £'000	2008 £'000
At 1 April	38,786	35,520
Expected return on plan assets	2,554	2,407
Contributions (including member contributions)	1,875	5,609
Benefits paid (net of transfers in)	(919)	(46)
Settlement	(712)	-
Actuarial loss on plan assets	(9,301)	(4,704)
At 31 March	32,283	38,786

Analysis of the movement in the amount recognised on the balance sheet:

	2009 £'000	2008 £'000
At 1 April	(2,047)	5,489
Total charge to income statement	927	1,065
Total charge/(credit) to statement of recognised income and expense	10,400	(3,339)
Contributions paid (excluding member contributions)	(1,512)	(5,262)
At 31 March	7,768	(2,047)

	2009	2008	2007	2006	2005
Experience adjustments arising on scheme assets					
Amount (£m)	(9.3)	(4.7)	(0.2)	3.5	0.9
Percentage of scheme assets	(29%)	(12%)	(1%)	11%	4%
Experience adjustments arising on scheme liabilities					
Amount (£m)	(1.1)	8.0	(0.7)	(2.0)	(0.9)
Percentage of the present value of scheme liabilities	(3%)	22%	(2%)	(5%)	(3%)
Present value of scheme liabilities (£m)	40.1	36.8	41.0	37.2	32.4
Fair value of scheme assets (£m)	32.3	38.8	35.5	30.6	24.6
Surplus/(deficit) (£m)	(7.8)	2.0	(5.5)	(6.6)	(7.8)

The contributions paid in the year to 31 March 2009 include a special contribution of £nil (2008: £4.0m). The contribution expected to be paid during the financial year ended 31 March 2010 amounts to £1.5m.

Notes to the financial statements

20 | Capital and other financial commitments

The group's business plan at 31 March 2009 shows net capital expenditure and infrastructure renewals expenditure of £352m 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.

21 | 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.

22 | 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.

23 | 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.

24 | 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.

The sum of £31.7m, 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 £2.3m (2008 £2.1m) in respect of distributions from the Elan Valley Trust Fund.