

Registered Number 2366682

**YORKSHIRE WATER SERVICES LTD**

**ANNUAL REPORT AND FINANCIAL STATEMENTS**

For the year ended  
31 March 2012



**ANNUAL REPORT AND FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 MARCH 2012**

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# ***Business Review***

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## **CHAIRMAN'S REVIEW**

Yorkshire Water Services Ltd (Yorkshire Water) maintained its focus on delivering day-to-day operational excellence in 2011/12 while putting in place building blocks to support the company's long-term growth and success

The development and roll-out of new strategic business objectives, coupled with a root and branch review of the company's activities, has created alignment between performance and the delivery of the new company vision – 'Taking responsibility for the water environment for good'

Performance was delivered against a national backdrop of ongoing regulatory uncertainty, economic austerity and increased public awareness of water generated by the Government's long-awaited White Paper and the introduction of hosepipe bans in other parts of the UK

I am pleased to report that Yorkshire's water supply situation remained healthy throughout the year

With the idea of creating a national water grid being discussed in the media once more, the flexibility of our own grid system gave us the ability to balance stocks across the region while giving depleted groundwaters in the east time to recover

However another significant contributory factor was the success we achieved in driving down the level of leakage during the year

During 2011/12 we put significant additional resource into tackling leakage and reduced levels in our region to the lowest on record

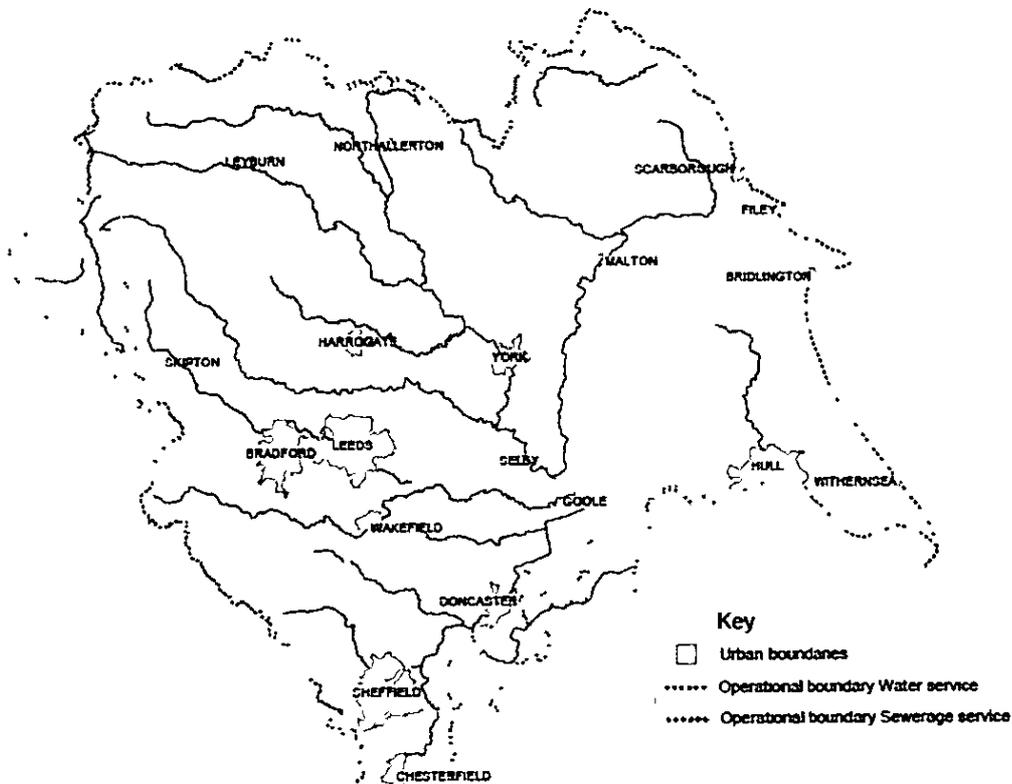
With one of our new strategic business objectives being to create a water efficient region, this is a significant area of focus, particularly as we engage with domestic and business customers

Over the next 12 months we will continue the dialogue we have started with our customers and stakeholders about the future of the water industry and show how we are turning our vision – 'Taking responsibility for the water environment for good' – into action

**Kevin Whiteman**  
**Chairman**

# Business Review

## OUR BUSINESS



We serve the Yorkshire region - from Whitby in the north to Chesterfield on the edge of Derbyshire in the south, and from Bridlington on the east coast to Ingleton in the west

Yorkshire Water manages the collection, treatment and distribution of the region's water. Yorkshire Water supplies around 1.3 billion litres of drinking water every day and then collects, treats and returns just less than 1 billion litres of waste water safely back into the environment.

We serve a population of approximately 4.9 million people, as well as around 130,000 businesses.

Our work in managing this natural resource for the benefit of our customers and the environment requires careful, long-term planning.

Over the period 2010 – 2015 we will spend around £3.5 billion on operating and improving the region's water and sewerage infrastructure, providing a major boost to the local economy.

# Business Review

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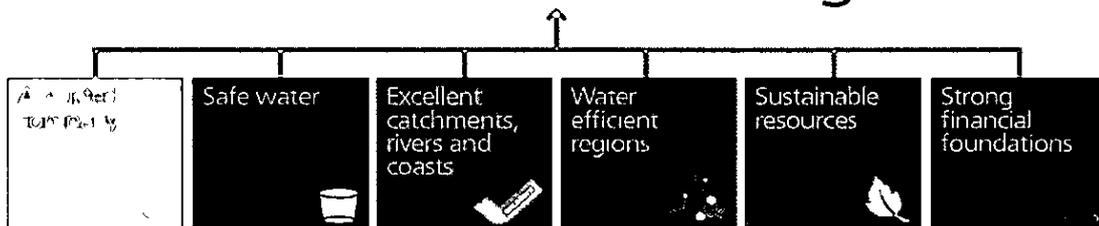
## BUSINESS STRATEGY

Water and serving water customers is what we do. It's our job to look after this precious natural resource from source to sea. The long-term sustainability of water is fundamental to the long term sustainability of our business.

To this end, our vision is 'Taking responsibility for the water environment for good'

Our strategic objectives:

“Taking responsibility for the water environment for good”



These are our six strategic objectives, that shape everything we do

**A trusted company** – The way we do business means our products, services and promises are trusted by all our stakeholders, now and in the future

**Safe Water** – We protect public health and make sure water is safe to drink. We ensure that water does not harm our customers or communities at any point in the process.

**Excellent catchments, rivers and coasts** – We maintain and improve the water environment from source to sea.

**Water efficient regions** – The way we operate and influence others creates water efficient regions.

**Sustainable resources** – The business uses sustainable resources, gets the most out of them and reduces emissions and waste.

**Strong financial foundations** – We deliver our services to customers at a price they are willing and able to pay, whilst providing investors with returns that attract long-term investment.

# Business Review

## BUSINESS PERFORMANCE

### Key performance indicators

	Target	Current year	Previous year
Overall customer satisfaction	77	77	76
Total leakage	297 MI/d	274 MI/d	325 MI/d
Overall drinking water quality	99.96%	99.95%	99.97%
Waste water treatment works compliance	100%	97.31%	99.68%
Accidents - major and over 3 day	9	23	15

Explanation of measures provided in Appendix to Business Review on pages 14 and 15

Yorkshire's water resource situation was healthy in 2011/12, with the region's reservoirs fully recharged in the spring after the harsh winter of 2010

There were no restrictions on customers' water supplies in Yorkshire during the year. There have now been no hosepipe bans in Yorkshire since November 1996 and this is largely due to the flexibility of the regional water supply system, our continuing efforts to drive down leakage and our work with customers to promote water conservation.

Yorkshire Water invested a total of £38m in leakage in 2011/12, which saw the company comfortably over achieve the leakage target of 297ML/d and achieve the lowest ever levels of leakage during the year.

Drinking water quality in Yorkshire continues to be excellent, with Yorkshire Water finishing joint top in the Drinking Water Inspectorate's annual performance assessment for 2011.

During the year, significant additional investment was also required to manage the implementation of the Government's transfer of private sewers into water company ownership.

As a result of new Government legislation, on 1 October 2011 Yorkshire Water became responsible for approximately an extra 22,000kms of sewers and lateral drains, with the transfer of several thousands of private pumping stations due to take place by October 2016. The transition was managed effectively, without disruption to customer service.

For the second year running there were no Category 1 pollution incidents attributable to Yorkshire Water, disappointingly however there were 15 recorded Category 2 pollution incidents.

To improve our performance in this area Yorkshire Water has launched a major pollution prevention campaign which involves improving our policies and procedures, additional

## **Business Review**

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capital investment at 142 problem locations and the targeted use of an innovative process known as biological dosing to tackle blockages caused by fat, oils and grease

Yorkshire Water ended the 2011 reporting calendar year with eight waste water treatment works failing their consents against a target of three. The operational and compliance performance of high risk sites is reviewed as part of weekly Seasonal Planning risk management meetings during 2011/12 and appropriate action taken

**Strategic Initiative: Customer Engagement** – The way we interact with our customers and the way we manage our relationships with them is a key part of our business.

In September, the Consumer Council for Water (CC Water) published a report focusing on complaints handling within the water industry in the previous year, 2010/11

Yorkshire Water recorded the second lowest number of complaints of all the water companies in 2010/11

In 2011, Yorkshire Water was ranked 4<sup>th</sup> out of all the water and sewerage companies in Ofwat's qualitative Service Incentive Mechanism (SIM). A new customer services strategy has now been developed to further improve the way customers are dealt with

In April 2011, Yorkshire Water also published our own views on the future of the water industry, calling on the Government to give water companies greater responsibility in the role of surface water management

Our contribution sparked widespread stakeholder discussion at a local and national level and proved to be a valuable pre-cursor to the Government's own White Paper on water management which was published in the autumn

**Strategic Initiative: Environment, Catchments, Water and Coast** – We maintain and improve the water and the environment from source to sea

During 2011/12, work started in earnest on the company's £110m programme of investment to improve the quality of Yorkshire's beaches and bathing waters

Driven by the Revised Bathing Water Directive, the first phase of construction started in Scarborough, with the second phase of work due to start in 2012 in Bridlington

The aim of the investment is to achieve the new "excellent" bathing water quality standard introduced by Europe and due to come into effect in 2015. Our work is being co-ordinated by an environmental partnership board which involves us working with a range of external organisations such as the Environment Agency, local councils and Welcome to Yorkshire, the region's tourism board

Work also started on a £79m programme of investment in the Don catchment in South Yorkshire, which will see significant improvements in the quality of the river from source to sea

On a visit to Yorkshire in October, the Environment Minister, Richard Benyon, praised Yorkshire Water for its ground-breaking and innovative approach to catchment management and urged other water companies to adopt a similar approach to managing the natural environment

## Business Review

The following month Yorkshire Water was delighted to announce that 100% of the Sites of Special Scientific Interest situated within Yorkshire Water catchments were now in 'recovering or better' status. This ensured that Yorkshire Water out-performed the target set by Government.

**Strategic Objective: Strong Financial Performance** - We deliver our services to customers at a price that is willing and able to pay, whilst ensuring investors will get the best return long-term investment.

During 2011/12, Yorkshire Water continued to make significant progress to reduce our energy consumption, emissions and our reliance on grid electricity.

Work started on a £33m project at Esholt Waste Water Treatment Works in Bradford, where the company is creating the UK's first energy-neutral urban sewage plant. This latest investment involves the construction of a BioTheyls Sludge Treatment Plant which will be used to create energy from human waste and trade effluent.

Approval was also given for a new £23m anaerobic digestion facility at Blackburn Meadows Waste Water Treatment Works in Sheffield, which will again contribute towards our plan to use renewable resources of power wherever it is appropriate.

In total, Yorkshire Water now generates 8% of our energy from renewable sources such as wind, combined heat and power, hydro and anaerobic digestion. We will continue in our pursuit to increase our levels of renewable energy generation.

**Strategic Objective: Strong Financial Performance** - We deliver our services to customers at a price that is willing and able to pay, whilst ensuring investors will get the best return long-term investment.

### Key financial performance indicators

	2012	2011
Operating profit (£m)	303.3	313.6
Net debt (£m)	3,159.1	2,956.3
Adjusted net debt to Regulatory Capital Value (RCV)	79.7%	73.7%

Explanation of measures provided in Appendix to Business Review on page 14.

Turnover increased by 3.0% to £893.6m (2011: £867.4m), compared with an average tariff increase of 3.4%. The impact of the average increase in tariffs is slightly offset by domestic customers opting to switch from unmeasured to measured tariffs. Of the £893.6m, £419.5m related to water services, £465.5m related to sewerage services and £8.6m was from non-regulated business.

Operating profit decreased by 3.3% to £303.3m (2011: £313.6m) driven by an increase in operating costs. Operating profit is shown after £9.6m of exceptional costs (2011: £5.9m). Following the severe winters experienced during 2009/10 and 2010/11, Yorkshire Water's network of water mains suffered an increase in the number of bursts and consequently experienced a higher level of leakage. During 2011/12 additional expenditure was incurred to improve leakage performance such that leakage targets could be achieved even in the event of another severe winter. The additional spend was monitored separately by management and is over and above historic levels of investment.

## **Business Review**

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Operating costs have increased by £36.4m or 6.6%. The increase above inflation is due to exceptional leakage costs of £9.6m, a further increase in the non-domestic rates charge of £4.0m as transitional relief which was available in 2010/11 has ceased, a new charge of £3.7m in relation to the government's Carbon Reduction Commitment (CRC) energy reduction scheme, and additional operating costs of £5.0m as a result of new Government legislation that on 1 October 2012 made Yorkshire Water responsible for approximately an extra 22,000kms of sewers and lateral drains. The additional rates costs were funded by Ofwat within the final determination of the review of prices which came into effect on 1 April 2010. Strong management of costs has allowed Yorkshire Water to absorb some of these additional costs.

Net interest payable before exceptional items increased from £231.2m in 2010/11 to £234.8m in 2011/12. The interest charge includes £63.8m in respect of RPI accrued on the index-linked swaps (2011: £22.8m). The increase of £41.0m compared to 2010/11 is due to a change in the discount applied to the swap bullet payment at the end of the term as a result of the re-structure of the swap portfolio discussed below. This increase to the interest charge has been largely offset by an increase in the interest receivable on the upstream loan to Kelda Holdco Ltd. The loan balance has increased during the year resulting in increased interest payable to Yorkshire Water.

Yorkshire Water holds certain index-linked swaps with a nominal value of £1,289m which had an adverse market value of £1,403.7m at 31 March 2012. At the balance sheet date it was concluded that 28% (£391.9m) of the swaps did not represent an effective hedge and an onerous contract provision has therefore been recognised within the accounts, £64.5m within borrowings and £327.4m within provisions in respect of an onerous contract provision. No significant change has been required to the provision during 2011/12.

The tax credit of £9.2m represents a reduction of £66.1m compared to the prior year (2011 credit of £75.3m). Of this tax credit, £18.9m relates to current tax offset by a £9.7m charge to deferred tax. The current tax credit includes prior year items. The deferred tax charge includes the reduction in the deferred tax provision following the change in the future rate of corporation tax from 26% to 24%.

Regulated capital investment for the year was £404.3m (2011: £300.3m). All regulatory outputs have been achieved.

### **Capital structure**

During the year, Yorkshire Water secured a total of £150m of funding from the European Investment Bank with a term of 15 years. The company refinanced its capex and working capital revolving credit facility. The new £490m facility expires October 2016. In addition a total of £335m (sterling equivalent) of funding was raised in the US Private Placement market over a range of maturities from 7 to 30 years. Furthermore, the company carried out a restructure of its portfolio of index-linked swaps to eliminate all break dates falling in 2012 and 2014.

The total net debt at 31 March 2012 was £3,159.1m (2011: £2,956.3m), which includes an upstream loan to Kelda Holdco Ltd. Adjusted net debt, excluding upstream loans and unamortised debt issue costs, is used to calculate gearing ratios to comply with the bank covenants. Adjusted net debt at 31 March 2012 was £4,209.5m (2011: £3,629.6m). The adjusted debt to Regulatory Capital Value (RCV) ratio must remain less than 85% at 31 March 2012 under the terms of the debt covenants. Actual adjusted debt to RCV at 31 March 2012 was 79.7% (2011: 73.7%).

# **Business Review**

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Dividend payments were £63.4m during the year (2011: £46.9m). No final dividend is proposed in respect of 2011/12. At 31 March 2012 Yorkshire Water had profit and loss account reserves of £842.7m (2011: £827.9m).

## **Kelda Group pension plan**

In April 2012, Yorkshire Water's parent company, Kelda Group Ltd, initiated a review of the company's pension plan with a view to making it more financially stable and sustainable in the long-term. The aims of the review are to reduce the deficit, stop it from re-emerging and ensure the company continues to offer members a high quality pension at an affordable cost.

## **Revaluation of fixed assets**

Certain classes of the company's tangible fixed assets were revalued at March 2012. Management concluded that the most reliable valuation method to determine the current value for the tangible fixed assets of a UK water company is a two step approach:

- Estimating the business value in use ('VIU'), using a discounted cash flow ('DCF') model excluding outperformance against Ofwat's targets to determine the business enterprise value. Excluding forecast outperformance against the regulatory allowance is a proxy for excluding any goodwill that a purchaser would pay for the business. The enterprise value was then cross-checked against the Regulatory Capital Value ('RCV'). This step was followed by
- Allocating the VIU of the business (less relevant working capital balances) to individual classes of tangible fixed assets.

Such valuations were incorporated into the financial statements and the resulting revaluation adjustments taken to the revaluation reserve. The revaluations during the year ended 31 March 2012 resulted in a net revaluation surplus of £1,607.9m.

## **Accounting policies**

The company accounts have been prepared in accordance with the accounting policies described in note 1 to the accounts.

## **Treasury policy**

The company's treasury operations are controlled centrally for the Kelda group (the Group) by a treasury department which operates on behalf of all companies controlled by the ultimate parent. Activities are carried out in accordance with approved board policies, guidelines and procedures. Treasury strategy is designed to manage exposure to fluctuations in interest rates, preclude speculation and to source and structure the Group's borrowing requirements.

The Group uses a combination of fixed capital, retained profits, long term loans, finance leases and bank facilities to finance its operations. Any funding required is raised by the Group treasury department in the name of the appropriate company, operating within the debt covenants. Funds raised may be lent to or from the company at commercial rates of interest. Cash surplus to operating requirements is invested in short term instruments with institutions having a long term rating of at least A- or A3 and a short term rating of at least A1 or P1 issued by Standard and Poor's and Moody's respectively.

# ***Business Review***

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## **Financial risk management**

The company has an executive team (Kelda Management Team, 'KMT'), which receives regular reports from all areas of the business to enable prompt identification of financial and other risks so that appropriate actions can be taken

The operation of the treasury function is governed by policies and procedures, which set out guidelines for the management of interest rate risk and foreign exchange risk and the use of financial instruments Treasury policy and procedures are incorporated within the financial control procedures of the company

The company's operations expose it to a variety of financial risks that include the effects of changes in debt market prices, price risk, liquidity risk, interest rate risk and exchange rate risk Derivative financial instruments, including cross currency swaps, interest rate swaps and forward currency contracts are employed to manage the interest rate and currency risk arising from the primary financial instruments used to finance the company's activities The company actively maintains a broad portfolio of debt, diversified by source and maturity and designed to ensure the company has sufficient available funds for operations

The company is exposed to commodity price risk, especially energy price risk, as a result of its operations The company aims to manage its risk by fixing contract prices where possible

## **LOOKING FORWARD**

In April 2011, the Group, of which Yorkshire Water is a member, published its own views on the future of the water industry

Responsible leadership and significant levels of investment have led to the water industry delivering considerably improved services in the 21 years since privatisation

However the industry now stands at a crossroads The growing demand for water and waste water services, increasing pressure for sustainable solutions, climate change and the constant search for even better value for money are all forces for change and it is important that the water industry is empowered to step up to address the challenges

The Group's document "Taking responsibility for the water environment for good" combines strategic and structural recommendations with more direct solutions

The underlying theme of the proposals is of the water industry playing a bigger role in addressing the sustainability of water whilst achieving even better value for money for customers The sector and its regulators will have to think differently and be more innovative to achieve these dual goals

To obtain a full copy of the Group's forward-looking plan, go to

<http://www.yorkshirewater.com/public-affairs/read-our-white-paper-online.aspx>

# ***Business Review***

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## **PRINCIPAL RISKS AND UNCERTAINTIES**

None of the risks discussed below are considered likely to have a significant impact on the short or long term value of the company in the immediate future

We classify principal risks in six categories

- Changes to the regulatory environment,
- Changes in legislation,
- Climatic changes,
- Changes in technology,
- Social influences, and
- Supplier markets

### ***Changes to the regulatory environment***

#### *Ofwat's proposed licence modifications*

Ofwat recently extended its consultation into proposals to modify the price review element of water companies' licences

Under the Water Industry Act 1991, Ofwat is able to modify the conditions of a company's licence if it agrees to the change. If a company does not agree, and in the absence of any alternative, Ofwat can refer the matter to the Competition Commission. The Competition Commission then decides whether the modification should be made and, if so, in what form.

Ofwat believes that the existing price-setting framework (where price limits are reviewed every five years) is not flexible enough and now wants to be able to specify the nature, form, length and number of price limits it sets in the future.

Ofwat agreed to extend the consultation in relation to the proposed modifications in light of opposition expressed by water companies concerned that it could undermine the confidence of investors in the sector.

We are currently discussing both these issues with Ofwat.

#### *Revised Bathing Water Directive*

From 2015 the EU's revised Bathing Water Directive comes into force, which aims to improve the quality of coastal waters. Bathing waters will be classified by the Environment Agency as either poor, sufficient, good or excellent. We are the only UK water company aiming for 'excellent'.

Our £110 million investment programme for the east coast was launched last year to improve our assets, and how we manage them, at 20 designated beaches along 100km of coastline from Staithes to Withernsea.

#### *Rising pension costs*

The cost of providing pensions has been steadily increasing as people are living longer. In addition to this, pension funds across the UK have had hundreds of millions of pounds wiped off their value as a result of the global economic downturn. Therefore in April 2012, Yorkshire Water's parent company, Kelda Group Ltd, announced a review of the company's pension plan with a view to making it more sustainable in the future.

# **Business Review**

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## ***Changes in legislation***

### *Draft Water Bill*

On 10 May 2012, it was announced in the Queen's Speech that a draft Water Bill will be included in the Government's legislative programme for the coming year

The Bill allows for greater freedom of public bodies and businesses to choose their water supplier and is designed to make water companies more responsive to the needs of customers. Reforms will mainly apply to England and Wales but will also allow for a joint water and sewerage retail market with Scotland

It is anticipated that the draft Bill will be published before the summer recess on 17 July 2012. It will then be subjected to pre-legislative scrutiny led by the House of Commons EFRA Select Committee

The Committee will call for evidence and invite stakeholders to present evidence to the Committee in person. The Committee will go through the Bill looking at its overall principles and then publish recommendations to the Government

We will respond to the consultation once the draft bill is published

### *Natural Environment White Paper*

In June 2011 the Government published a Natural Environment White Paper setting out measures to protect wildlife, promote green spaces and wildlife corridors, value natural capital and produce an analysis of the state of the UK's natural asset base (the National Ecosystems Assessment)

The House of Commons EFRA Select Committee inquiry on the White Paper ended in April, with the report expected to be published in early summer

### *Environmental legislation*

Government and European policy is increasingly focussed on the environmental agenda, which creates both opportunities and challenges for Yorkshire Water

For example, this year the European Commission will present a *Blueprint to Safeguard Europe's Water Resources*. This document will assess the implementation and achievements of EU water policy as well as identify gaps and shortcomings. On the basis of this analysis, the Blueprint will identify actions to strengthen water policy and to address ongoing vulnerability of the water environment

The European Commission is asking the public for its views on the most appropriate actions to improve water management in Europe and to safeguard water resources for all users (consumers, agriculture, industry and nature itself). The public's views will help to formulate the policy proposals to be included in a Blueprint to Safeguard Europe's Water Resources planned for the end of 2012

The consultation closes on 7 June 2012. We will monitor the outcomes of the consultation

# **Business Review**

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## ***Climatic changes***

### *Climate change – carbon reduction*

The provision of high quality water and wastewater services is carbon and energy intensive. Our energy consumption and the price of electricity are both set to rise significantly in the future. We therefore recognise that we have an important role to play in developing secure low-carbon energy for the UK and our business.

Approximately 70% of our operational carbon footprint stems from our use of electricity. Therefore we continue to invest in our programmes for energy efficiency and low-carbon renewable self-generation. Yorkshire Water is working on a group-wide sustainable energy strategy to do the right thing environmentally and economically for both customers and investors. For our own energy generation, we want to use the right commercially viable technology for the resource appropriate to the site.

### *Climate change – adaptation*

In the future our assets and services are likely to be challenged by more frequent and more severe extreme weather events which are projected to occur because the climate is changing. Our recently completed climate change risk assessment has confirmed that climate change presents opportunities and risks to our business, in both the short and long term. We are working at the forefront of climate change adaptation because we recognise that the climate and weather are fundamental to the sustainability of our water and wastewater services. To avoid significant price shocks for our customers and investors, we are developing long term plans to prepare for the changing climate. We are currently part way through a multi-phase climate change project which will inform our approach to the upcoming Price Review and longer term planning.

## ***Changes in technology***

Increasingly organisations are quickly brought to account by customers and the media. This trend has been assisted by the development of social networking sites such as Facebook, YouTube and Twitter which allow pressure groups to form quickly, share their views and form opinions.

Dealing with this new form of dialogue and engagement will be an increasing challenge for corporate communications over the next five years. Yorkshire Water will be monitoring online conversations across social media channels to understand customer sentiment and provide help and advice where possible.

Over the last five years Yorkshire Water have seen a significant year-on-year increase in website usage, with over one million customers visiting the website each year to pay bills, send meter readings and request water saving packs.

We have developed a social media policy which is being kept under frequent review as new technologies emerge.

## ***Social influences***

### *Public confidence*

With the effects of a changing climate becoming more visible, the public are increasingly likely to demand more involvement and a stronger say in the provision of water and waste

# ***Business Review***

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water services Public activism will be highly relevant as Yorkshire Water attempts to create advocacy to drive further investment and solve customers' problems

We have developed our own Customer Panel to capture the views of customers and consumers on key business issues

## *The skills agenda*

Increasingly Yorkshire Water has found it challenging to recruit new employees with appropriate skills and experience for specific parts of the business Engineering and operational skilled labour is increasingly difficult to recruit as the pool of potential recruits shrinks, particularly those with science, technology, engineering and maths qualifications In response we are now running highly-effective graduate and apprentice recruitment campaigns The number of apprentices employed during 2011/12 was 15

## *Bad debt*

In light of the current economic conditions and in particular the contraction of the public sector in Yorkshire it is predicted that higher levels of unemployment will continue This will have an impact on customers and their ability to pay their water bills We operate several schemes, including the Yorkshire Water Community Trust and Resolve, to help customers who are genuinely struggling to pay their bills

## ***Supplier markets***

### *A global economy*

The national and international economic uncertainties may put pressure on Yorkshire Water's input costs Yorkshire Water has significant and growing energy demands thus making the business model exposed to energy price fluctuations

As clean and waste water regulatory standards become more stringent, the energy requirements of conventional treatment techniques tend to increase This correlation of increasing regulatory demands and energy usage will provide a challenging environment over the next ten to twenty years, particularly as the Carbon Reduction Commitment (CRC) has been implemented and we can expect increased 'carbon tax' in future

To mitigate this, we are looking to reduce our reliance on grid electricity and use renewable energy where appropriate and economically viable

# **Business Review - Appendix**

## *KPI Glossary of Terms*

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### **FINANCIAL KEY PERFORMANCE INDICATORS**

#### **Operating profit**

Operating profit is disclosed in the Yorkshire Water profit and loss account

#### **Net debt**

Net debt represents the value of loans and finance leases owed to third parties and other companies within the group, offset by available cash

#### **Adjusted net debt to Regulatory Capital Value (RCV)**

The RCV is determined by Ofwat and is the value of the capital base on which a return is allowed for price setting purposes. The values are calculated and published annually by Ofwat. This ratio expresses adjusted net debt as a proportion of the RCV, both of which are published in Yorkshire Water's audited accounts.

### **NON FINANCIAL KEY PERFORMANCE INDICATORS**

#### **Overall customer satisfaction**

The company recognises the value of listening to customers in order to deliver improvements that not only meet but surpass expectations. Customer satisfaction is monitored on a regular basis by Ofwat based upon the Service Incentive Mechanism (SIM).

SIM measures the level of customer concern with company service and how well the company deals with them. The SIM is a financial mechanism to incentivise optimal levels of customer service, through the price control process. SIM is a combination of a qualitative and quantitative measure and both household and non-household customers are included.

The quantitative measure reflects the number of complaints and telephone contacts that the company receives. It measures the number of complaints from different stages of the complaints process and takes into account whether the company resolved the customer's problem first time. Each element within the quantitative measure is weighted to reflect the increasing impact on customers, and the cost of failing to deal effectively with a complaint first time.

The qualitative measure reflects how satisfied customers are with the quality of service they receive from their company. It is based on a survey of customers who have had direct contact with their company. The survey asks customers how satisfied they were with the way the supplier resolved their billing or operational issue.

Both of these measures are combined to give a combined customer experience measure.

#### **Leakage**

Total leakage measures the sum of distribution losses and supply pipe losses in megalitres per day (Ml/d). It includes any uncontrolled losses between the treatment works and the customer's stop tap. It does not include internal plumbing losses.

# **Business Review - Appendix**

## *KPI Glossary of Terms*

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### **Water quality**

The Drinking Water Inspectorate (DWI) regulates public water supplies in England and Wales. It is responsible for assessing the quality of drinking water, taking enforcement action if standards are not being met and appropriate action when water is unfit for human consumption.

The Government has set legal standards for drinking water in the Water Quality Regulations. Most of these standards come directly from European law and are based on World Health Organisation guidelines. The UK has additional standards to safeguard the already high quality of water in England and Wales. The standards are strict and generally include wide safety margins. They cover

- Bacteria,
- Chemicals such as nitrate and pesticides,
- Metals such as lead, and
- Appearance and taste

The measure we use is for overall drinking water quality which consists of the average compliance values for 39 different parameters.

### **Waste water treatment works compliance**

The Environment Agency issues consents to allow the discharge of treated water from waste water treatment works. The three principal consented limits are for suspended solids, biochemical oxygen demand and ammonia. A range of other substances may be limited depending on the type of discharge. This indicator shows loads for the following determinands

- suspended solids, which can blanket the river bed, thereby destroying fish habitat,
- biochemical oxygen demand (BOD), which is a measure of the amount of oxygen consumed in water - usually by organic pollution - and therefore reflects the quality of the water,
- ammonia, which is toxic to fish, and
- phosphate, which promotes excessive plant growth which upon decomposition strips oxygen from the water

All waste water treatment works are monitored for compliance with their discharge consents and the receiving waters are monitored to assess their compliance with water quality targets. The frequency of monitoring depends on the size of the treatment works, small works are monitored on a quarterly basis and large works are monitored every week.

### **Reportable and notifiable accidents**

The Health and Safety Commission is responsible for health and safety regulation in Great Britain. The Health and Safety Executive and local government are the enforcing authorities who work in support of the Commission.

The Reporting of Injuries, Diseases and Dangerous Occurrences Regulations 1995 (RIDDOR) places a legal duty on employers to notify and report some work related accidents, diseases and dangerous occurrences. These include, amongst other things, accidents where employees are absent from work for three days or more.

# **Corporate Social Responsibility**

*For the Year Ended 31 March 2012*

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In 2011/12, Yorkshire Water's parent company, Kelda Holdings Ltd, attained the gold standard in Business in the Community's annual Corporate Responsibility Index

Kelda's approach to corporate responsibility (CR) is founded on the principle that the interests of the environment, customers and society at large are best served through the efficient, effective and proper operation of our business

This is achieved through a clear strategic focus on providing excellent customer service, strong financial and environmental performance and by effectively managing the relationships we have with our people, service partners and society. Successful progress in each of these areas provides benefits for all.

Our progress in this area is driven and monitored by the Kelda CR Committee, which meets quarterly.

The committee's key tasks include

- demonstrating commitment and leadership in the area of corporate responsibility to help drive Kelda's ambitions and targets,
- shaping the company's corporate responsibility activity and setting clear objectives,
- monitoring and challenging the company's CR performance, and
- determining an agenda for key issues to be addressed through the involvement of external bodies and agencies

Membership of the committee includes

- Richard Flint, CEO of Kelda Holdings Ltd and Yorkshire Water (Chair)
- Kevin Whiteman, Chairman of Kelda Holdings Ltd
- Kath Pinnock, Non-executive director of Yorkshire Water
- Martin Havenhand, Non-executive of Yorkshire Water

Meetings are also attended by Michelle Lewis, Yorkshire Water's Director of Corporate Communications

During 2011/12, the committee considered a number of CR issues, including an assessment of the wider economic impact of the company's activities in the Yorkshire region and a review of the company's environment and sustainability reporting.

There was also detailed discussion about the company's performance in Business In the Community's annual Corporate Responsibility Index and where further improvements could be made in the future. Several changes to the way the company measures and reports its performance will be implemented in 2012/13.

There are five focus areas for our CR activity

## **Community**

We provide local communities with much more than just high quality water and sewerage services.

We have an extensive engagement programme, providing support and help-in-kind to a wide variety of different organisations across the communities we serve. These partnerships are of enormous importance to us in terms of forging stronger links and by making a tangible and positive difference to the quality of people's lives.

# **Corporate Social Responsibility**

*For the Year Ended 31 March 2012*

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We provide this support in three key areas

- Education - through educating young people and local communities on the value of what we do,
- Environment - playing a key role as one of Yorkshire's largest landowners in enhancing the natural and build environment, and
- Empowerment - providing opportunities for our colleagues to share skills with the local community through employee supported volunteering

Further information about our community programmes is available on the Yorkshire Water website at <http://www.yorkshirewater.com/about-us/giving-something-back.aspx>

## **Environment**

We recognise that the long term viability of our water and sewerage business is dependent on sustainable operations. We believe sustainable operations are those that drive efficient resource use and provide a healthy environment, which in turn facilitates social progress and economic growth. As a company we therefore strive to act as responsible stewards of the environment and commit to continual improvement.

To balance these challenging needs we are committed to efficient and effective practices. We recognise that sustainability is the collective responsibility of governments, businesses, individuals and communities and so work in partnership with our stakeholders to pursue this goal.

Further information about our environmental performance is available at <http://www.keldagroup.com/kel/csr/respecting-our-environment/>

## **Marketplace – supply chain**

A highly effective and sustainable supply chain is a critical part of the success of our business.

We want our supply chain to be a highly successful, innovative organisation that grows, develops and thrives as a direct result of working together.

We strive for excellence and our expectations of our supply chain relationships are

- Service partners are excellent employers and operate safely,
- We set absolutely clear expectations of service partners,
- Our service partners continually bring new ideas to the table,
- Our service partners have an integrated policy for inclusion, equality and diversity,
- Win, win, win means better service, lower cost and healthy profits for all, and
- We continuously listen and talk to service partners to achieve win, win, win

Further information about our supply chain is available at <http://www.keldagroup.com/kel/csr/marketplace-our-cust-n-sup-chain/supp-our-commitment/>

## **Marketplace – customers & consumers**

We take great pride in our customer service, aiming to provide an outstanding quality of service, value for money and consider customers' points of views at all times.

Managing a high quality, secure water supply and distribution network is not cheap and requires billions of pounds of long term investment. Whilst it is essential that this investment is carried out, there is also a difficult balancing act to be struck to ensure that

# **Corporate Social Responsibility**

*For the Year Ended 31 March 2012*

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all customers receive good value for money, but that those who are financially vulnerable are appropriately protected

We offer a range of schemes to help customers struggling to pay their bills

Further information about our customer service promise is available at <http://www.yorkshirewater.com/your-water-services/customer-services/our-service-promises.aspx>

## **Workplace – our employees and partners**

We strive to create a positive working environment for all our people. This means

- we ensure that our working environment protects the health, safety and wellbeing of all our people,
- our competitive reward and benefits package attracts and retain the best people,
- our people are valued for their contribution and understand how they can make a difference,
- we value and respect each individual and have an inclusive approach,
- our people maximise their potential through skills development, and
- we communicate and engage with our people and unions openly

# **Directors' Report**

*For the Year Ended 31 March 2012*

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The directors present their report and the audited financial statements of the company for the year ended 31 March 2012

## **Financial results for the year**

Profit for the financial year was £77.7m (2011: £117.7m)

## **Business review**

A review of the development and performance of the business of the company, including strategy, the financial performance during the year, key performance indicators, health and safety policy, forward-looking statements and a description of the principal risks and uncertainties facing the company are set out in the business review on pages 10 to 13.

The purpose of this annual report is to provide information to the company's stakeholders and contains certain forward looking statements with respect to the operations, performance and financial condition of the company. By their nature, these statements involve uncertainty since future events and circumstances can cause results to differ from those anticipated. Nothing in this report should be construed as a profit forecast.

## **Principal activities**

The directors' report should be read in conjunction with the business review. The principal activities of the company are the supply of clean water and the treatment and disposal of waste water in Yorkshire, for which the company is the water and sewerage undertaker. The majority of the company's operations are regulated by Ofwat.

## **Directors**

The directors who served during the year and up to the date of signing these financial statements, including any changes, are shown below:

Richard Flint	Chief Executive
Liz Barber	Finance & Regulation Director
Graham Dixon	
Alan Harrison	(resigned 4 April 2012)
Charlie Haysom	(appointed 27 April 2011)
Mark Penny	(resigned 14 October 2011)
Helen Phillips	(appointed 28 March 2012)
Pamela Rogerson	(appointed 27 April 2011)

## **Non executive Directors**

Kevin Whiteman	Chairman
Roger Hyde	
Martin Havenhand	
Kathryn Pinnock	
Rhys Evenden	(resigned 26 October 2011)
Holly Koeppel	(resigned 31 March 2012)
Scott Auty	(resigned 31 March 2012)
Mark Lorkin	(resigned 31 March 2012)
Jane Seto	(resigned 31 March 2012)
Stuart Baldwin	(appointed 23 November 2011, resigned 31 March 2012)

# **Directors' Report**

*For the Year Ended 31 March 2012*

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As permitted by the articles of association, the Directors have the benefit of an indemnity which is a qualifying third party indemnity provision as defined by section 234 of the Companies Act 2006. The indemnity was in force throughout the last financial year and is currently in force. The company has directors' and officers' liability insurance in place.

## **Dividends**

The total dividend of £63.4m (2011: £46.9m) paid to Yorkshire Water's immediate parent company, Yorkshire Water Services Holdings Ltd, in the year related to payments to Group companies to fund the payment of interest and loan repayment.

No final dividend for the year is proposed.

The company's dividend policy is to

- deliver real growth in dividends recognising the management of economic risks, the continuing need for investment of profits in the business and to pay additional dividends which reflect efficiency improvement, and particularly improvements beyond those assumed in the determination of price limits,
- to pay dividends in respect of the non-appointed business reflecting the profitability of those activities, and
- where it is foreseeable that the company will have sufficient profits available for distribution, to continue to pay annual dividends consistent with this policy, the company can also pay special dividends as part of any capital reorganisation which the board concludes to be in the best interests of the company and complies with its obligations under its licence.

The directors consider that the dividends paid in the year are in accordance with these principles.

## **Reserves**

The profit for the year of £77.7m has been transferred to the profit and loss reserve, bringing the balance held in this reserve to £842.7m (after dividends in the year of £63.4m and a £0.5m credit from the revaluation reserve).

## **Research and development**

The company undertakes a programme of research in pursuit of improvements in service and operating efficiency. In 2011/12, £8.2m was committed to research and development including £7.5m on fixed assets.

## **Fixed assets**

The directors are aware that the value of certain land and buildings in the balance sheet may not be representative of their market value. However, a substantial proportion of land and buildings comprises specialised operational properties and structures for which there is no ready market and it is not therefore practicable to provide a full valuation.

Movements in fixed assets include transfers to KeyLand Developments Ltd, which have all been made on the basis of independent external valuations obtained specifically for the purpose and approved by Ofwat. With effect from 1 April 1996, only those transfers with a value of over £500,000 have been subject to approval by Ofwat.

# **Directors' Report**

*For the Year Ended 31 March 2012*

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## **Revaluation of assets**

Certain classes of the company's tangible fixed assets were revalued at March 2012, as covered in the Business Review on page 8

In addition in March 2009, Yorkshire Water re-valued its non specialised land and buildings (i.e. non operational land and buildings, including offices and rural estates), resulting in an increase to fixed assets of £52.7m and a corresponding increase in reserves. The Manager of Land, Property and Planning, a member of the Royal Institution of Chartered Surveyors (MRICS), has reviewed the carrying value at 31 March 2012 of Yorkshire Water's non specialised land and buildings and considers that no impairment or uplift would be required to the accounts, and the current book values are not materially different to current market values.

The Directors confirm that they know of no material change to the value of Yorkshire Water's non specialised land and buildings to be disclosed within the accounts of Yorkshire Water at 31 March 2012.

These assets will continue to be revalued on a periodic basis, to coincide with valuations required for future Ofwat Periodic Reviews.

## **Capital and infrastructure renewals expenditure**

Total expenditure on regulated activities during the year amounted to £404.3m (2011 £300.3m).

## **Payment of suppliers**

The company's policy on the payment of suppliers is to ensure that all payments are made in accordance with the terms and conditions agreed with suppliers. For construction contracts, payment terms are covered by the appropriate Conditions of Contract, such as NEC Form of Contract, ICE 6th Edition and Model Form of Conditions of Contract for Process Plants (IChemEng).

The payment day ratio (the figure, expressed in days, which bears the same proportion to the number of days in the year as the amount owed to trade creditors at the year end bears to the amounts invoiced by suppliers during the year) is 19 days (23 days in 2011).

## **Instrument of Appointment**

Condition F of the company's Instrument of Appointment as a water and sewerage undertaker requires the company to publish regulatory accounting information in a prescribed format in addition to that required for the statutory accounts.

## **Employees and employment policies**

The company strives to create a positive working environment for all colleagues and places great emphasis on open two-way communications. It values involvement and engagement at all levels, recognising that everyone in the business is valued for their contribution and is a potential source of innovation and change. Internal consultation and communication processes provide the key to this involvement.

# **Directors' Report**

*For the Year Ended 31 March 2012*

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The company communications strategy is based on a 'face to face first' approach and all messages are delivered through 'two-way' channels, including regular 'Team Talks' and 'Talk Back' sessions with line managers and the Directors

Regular employee satisfaction surveys are undertaken throughout the company, using a variety of engagement tools including telephone-based and online surveys. We also supplement the surveys with a variety of employee focus groups

These surveys and focus groups highlight what is going well and provide the company with valuable information about where to place more emphasis to really make a difference to how people feel at work

To promote successful employee relations, the company demonstrates its commitment to effective and two way communication through its information and consultation framework. In addition to collective bargaining arrangements with its recognised trade unions, communication and consultative team meetings take place across the company, comprising elected (union and non-union) employees who meet regularly with directors and senior managers

The company promotes freedom of association, principally through its diversity and inclusion strategy. The company's equality and diversity, 'open to all', policy covers gender, marital status, parental status, sexual orientation, race, colour, ethnic or national origin, disability, age, religion or belief and trade union membership. Yorkshire Water has previously been recognised by winning the Personnel Today award for Diversity in the Workplace and has also featured as a case study on a website created by the London Development Agency for businesses in their region. We have an active approach to keeping employees who become disabled in employment and our commitment to equal opportunities for less able job applicants has been recognised with the 'double tick' accreditation from the UK Employment Service

Key to achieving operational excellence and delivering out-performance is ensuring that every individual understands their role and how they can make a difference whilst feeling valued for their contribution. We are committed to rewarding the right performance and we adopt a 'total reward' approach to salary and benefits which are designed to be competitive. Performance related pay gives colleagues at all levels the opportunity to share in the success of the business, through quarterly or annual bonus payments linked to the achievement of individual and business plan targets

The company continually strives to attract, select and retain the best people. Looking to the future, there is a strong commitment and focus on proactively resourcing the business by understanding future roles and skills requirements and ensuring that plans are in place to meet our needs. Our approach includes understanding people's career aspirations, meeting development needs and actively mitigating resourcing challenges to ensure that we retain our best talent. In 2012/13 a further 17 apprentices will join what is already a successful programme

The company places great emphasis on enhancing business performance by maximising individual, team and organisational potential through skills development. We are focused on developing safety, technical, behavioural and leadership capability. It is our belief that everyone can demonstrate leadership skills. This commitment is demonstrated through our focus on leadership development for managers and senior managers across the business and the company's commitment to embedding a coaching culture. This enables people to learn and grow by identifying and focusing on their own development areas. The company provides a wide range of development opportunities, including in-house and accredited

# **Directors' Report**

*For the Year Ended 31 March 2012*

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programmes to help all employees (including disabled employees) develop the necessary skills, knowledge, values and experience to realise their performance potential

## **Health and safety**

Yorkshire Water is committed to achieving high health and safety standards throughout its business. The management of health and safety issues operates in the context of the health and safety policy adopted by the board and the system of internal control.

The company operates within a framework of policy/procedural requirements and must have in place appropriate health and safety policies and procedures and provide necessary information, instruction, training and supervision. In addition, the company provides occupational health, safety and welfare advisory services for employees.

Specific health and safety goals are also set within the business. These goals include a combination of reductions of accidents, near miss reporting, hazard identification, behavioural safety conversation, training delivery, internal safety audits and health promotion and surveillance programmes.

Senior management awareness and active employee involvement in health and safety is fundamental to company success. A Think Safety First programme was launched successfully in Yorkshire Water in 2006 and is now being reviewed to further improve its currency and its impact in communicating and engagement with colleagues across the business around their health and safety risks.

Consultation with all employees via area and functional health and safety forum groups and safety committees is actively encouraged. Where possible, the intent is for local health and safety issues to be discussed and resolved with line management. In Yorkshire Water there are health and safety champions who work alongside the Trade Union safety representatives and line management. This ensures that health and safety issues are regularly discussed within each team in all business units.

Our aspiration is to achieve zero accidents and the measures taken by the company are intended to place emphasis on the proactive identification and control of our health and safety risks.

## **Directors' statement as to disclosure of information to auditors**

As at the date of this report, as far as each director is aware, there is no relevant audit information of which the company's auditors are unaware and each director has taken steps as he or she should have taken as a director in order to make him or herself aware of any relevant audit information, and to establish that the company's auditors are aware of that information.

# **Directors' Report**

*For the Year Ended 31 March 2012*

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## **Independent auditors**

The auditors, PricewaterhouseCoopers LLP, have indicated their willingness to continue in office and the board has passed a resolution confirming their reappointment



ON BEHALF OF THE BOARD

Kevin Whiteman

Chairman

27 June 2012

Registered office Western House, Halifax Road, Bradford BD6 2SZ  
Registered in England no 2366682

# **Corporate Governance Report**

*For the Year Ended 31 March 2012*

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## **Corporate Governance**

Throughout the year the board remained accountable to the company's shareholders for maintaining standards of corporate governance. The following is an explanation of the measures taken by the company.

### **The board of directors**

The board held ten scheduled meetings during the year. Additional meetings were held where it was considered appropriate or where business needs required. In addition, meetings of committees of the board were held when required. The board had a schedule of matters reserved for its decision.

The board determines the company's strategic objectives and key policies, and approves the business plans for the company, interim and final financial statements, recommendations of dividends, significant investment and major new business proposals, as well as significant organisational matters and corporate governance arrangements. There are clear levels of delegated authority, which enable management to take decisions in the normal course of business.

All new directors, where applicable, received an induction and training on joining the board, including information about the company and their responsibilities, meetings with key managers, and visits to the company's operations. There is an agreed procedure for directors to take independent professional advice at the company's expense in furtherance of their duties in relation to board or committee matters. Directors have access to the company secretary who is responsible for ensuring that board procedures are followed. The directors receive full and timely access to all relevant information, including a monthly board pack of operational and financial reports. Direct access to key executives is encouraged. The company has directors' and officers' liability insurance in place.

At the end of the year, the Yorkshire Water board comprised a non executive chairman, six executive directors and three further non executive directors.

The board has delegated certain authority to board committees as and when appropriate. The company does not have its own remuneration, nominations or audit committees but these are operated at Group level by Kelda Holdings Ltd, the company's ultimate parent company.

### **Kelda Holdings Ltd audit committee**

Roger Hyde, who is an independent non executive director, sits on the Kelda Holdings Ltd audit committee and four Group directors comprise the balance of the committee. The external auditors, the head of internal audit and the company secretary attend all meetings. The group finance and regulation director attends by invitation. The committee also meets with the external auditors without the presence of executive management when it considers it necessary or appropriate to do so. The committee chairman reports on the activities of the committee to the group board meeting immediately following each committee meeting.

# Corporate Governance Report

For the Year Ended 31 March 2012

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The audit committee's key tasks include

- reviewing and monitoring of the integrity of the annual financial statements,
- reviewing the company's system of internal control, including financial, operational, compliance and risk management,
- overseeing the company's relationship with the external auditors, agreeing the nature and scope of the audit and reviewing the independence and objectivity of the external auditors, and
- monitoring and reviewing the effectiveness of the internal audit function

In undertaking these tasks the committee receives and reviews work carried out by the internal and external auditors and their findings. Both the internal and external auditors work to an annual plan developed in consultation with the committee. In addition, the committee reviews specific business areas and processes from time to time.

The regular business of the audit committee includes consideration of reports on financial statements, audit planning, the activities of internal audit and its key findings, and the consideration of the operation of internal control processes.

The independence and objectivity of the external auditors is considered on a regular basis, with particular regard to the level of non audit fees.

The Group has adopted an auditor independence policy which establishes procedures and guidance under which the company's relationship with its external auditor is governed so that the audit committee is able to satisfy itself that there are no factors which may, or may be seen to, impinge upon the independence and objectivity of the audit process.

## Internal control

An ongoing process, in accordance with the guidance of the Turnbull Committee on internal control, has been established for identifying, evaluating and managing the significant risks faced by the company and this has been in place for the year under review and up to the date of approval of the annual report and accounts. Strategic, financial, commercial, operational, social, environmental and ethical risks fall within the scope of this process. The process is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, not absolute, assurance against material misstatement or loss.

The company has comprehensive and well defined control policies with clear structures, delegated authority levels and accountabilities.

The company's risk management process aims to be comprehensive, systematic and continuous, and based on constant monitoring of business risk. The key features of the process include the following:

- The main risks facing the company are identified and recorded in a strategic risk register together with the control mechanisms applicable to each risk. These are collated from risk registers maintained by individual businesses,
- There is clear allocation of management responsibility for risk identification, recording, analysis and control,
- The audit committee reviews the effectiveness of the systems which are in place and reports to the group holding company board,
- An established risk management forum, chaired by the group company secretary operated during the year. This was in transition to passing responsibility for risk to

# **Corporate Governance Report**

*For the Year Ended 31 March 2012*

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operational business units throughout the Group, reporting to the audit committee via the executive team,

- Business units are required to report annually on principal business risks and the operation of control mechanisms, and
- The internal audit department provides objective assurance and advice on risk management and control, and monitors the risk management process

The audit committee reviews and monitors the effectiveness of the process on behalf of the Group holding company board

In addition to this process, the business is subject to a quarterly comprehensive review by the executive team, independent internal and external audits which were reported to the executive team and the audit committee, an extensive budget and target-setting process, a quarterly reporting and forecasting process reviewing performance against agreed objectives, appropriate delegated authority levels, established financial policies and procedures, and other risk management policies and procedures such as health and safety and environmental policies

## **Kelda Group Ltd corporate responsibility committee**

During 2011/12 the Kelda group re-established its corporate responsibility committee Martin Havenhand and Kathryn Pinnock, who are independent non executive directors, sit on the Kelda Group Ltd corporate responsibility committee Kevin Whiteman, the non executive chairman, also sits on this committee which is chaired by Richard Flint The Director of communications and the company secretary attend all meetings Other directors and Group employees attend by invitation During 2011/12 this committee met on five occasions and in future is scheduled to meet on a quarterly basis

The corporate responsibility committee's key tasks include

- delivery of the Group's corporate social responsibility reports,
- the creation of a culture of environmental and corporate responsibility awareness within the Group,
- liaising with and directing activity of other relevant Group committees,
- advising on opportunities for partnerships to further the Group's corporate responsibility objective,
- benchmarking performance of the Group against leading comparators, and
- monitoring the work of and receiving reports from the Environmental Advisory Panel

## **Environment**

The environmental policy of the company recognises that a sustainable water and waste water business is dependent on environmentally sustainable operations It is therefore committed to integrating environmental best practice and continuous improvement in environmental performance through the efficient, effective and proper conduct of its business

Environmental performance is reported through the company's website which is regularly updated This can be viewed at [www.yorkshirewater.com/our-environment.aspx](http://www.yorkshirewater.com/our-environment.aspx)

# **Corporate Governance Report**

*For the Year Ended 31 March 2012*

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## **Community**

The company contributes actively to the communities which it serves. It encourages and supports colleagues in volunteering, charitable giving and community involvement. One in three employees is active in a wide range of supported community activities. These include a Speakers' Panel and support to local education ranging from governor appointments, and Right to Read in junior schools through to coaching at senior schools and mentoring university students from diverse ethnic backgrounds.

## **Going concern**

After making enquiries, the directors have a reasonable expectation, given the nature of the regulated water services business, that the company has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

# Profit and Loss Account

for the year ended 31 March 2012

	Note	2012 £m	2011 £m
<b>Turnover</b>		<b>893.6</b>	<b>867.4</b>
Operating costs before exceptional costs	2	(580.7)	(547.9)
Exceptional operating costs	2	(9.6)	(5.9)
<b>Total operating costs</b>		<b>(590.3)</b>	<b>(553.8)</b>
<b>Operating profit</b>		<b>303.3</b>	<b>313.6</b>
Net interest payable and similar charges before exceptional costs	5	(234.8)	(231.2)
Non operating exceptional costs	4	-	(40.0)
Net interest payable and similar charges - total		(234.8)	(271.2)
<b>Profit on ordinary activities before tax</b>		<b>68.5</b>	<b>42.4</b>
Tax on profit on ordinary activities	6	9.2	75.3
<b>Profit for the financial year</b>	18	<b>77.7</b>	<b>117.7</b>

All of the above results relate to continuing activities

There is no material difference between the profit before tax and the profit for the year stated above and their historical cost equivalents. There is no material difference between the historical cost depreciation charge and the actual depreciation charge for the year as a result of the revaluation of certain tangible fixed assets.

## Statement of Total Recognised Gains and Losses

for the year ended 31 March 2012

		2012 £m	2011 £m
<b>Profit for the financial year</b>		<b>77.7</b>	<b>117.7</b>
Prior year adjustment	9	1,607.9	-
<b>Total recognised gains and losses recognised since last annual report</b>		<b>1,685.6</b>	<b>117.7</b>

# Balance Sheet

as at 31 March 2012

	Note	2012 £m	2011 (restated) £m
<b>Fixed assets</b>			
Intangible assets	8	6.6	7.6
Tangible assets	9	6,143.9	5,965.7
Investments	10	0.1	0.1
		<u>6,150.6</u>	<u>5,973.4</u>
<b>Current assets</b>			
Stock	11	1.2	1.2
Debtors falling due within one year	12	186.6	160.0
Debtors falling due after more than one year	12	1,289.5	928.9
Debtors - total	12	1,476.1	1,088.9
Cash at bank and in hand	14	8.3	45.4
		<u>1,485.6</u>	<u>1,135.5</u>
<b>Creditors: amounts falling due within one year</b>			
Short term borrowings	14	(55.7)	(63.3)
Other creditors	13	(319.3)	(333.8)
		<u>(375.0)</u>	<u>(397.1)</u>
<b>Net current assets</b>		<u>1,110.6</u>	<u>738.4</u>
<b>Total assets less current liabilities</b>		<u>7,261.2</u>	<u>6,711.8</u>
<b>Creditors: amounts falling due after more than one year</b>			
Long term borrowings	14	(4,120.7)	(3,578.6)
Other creditors	13	(125.5)	(134.4)
		<u>(4,246.2)</u>	<u>(3,713.0)</u>
<b>Provisions for liabilities and charges</b>	16	(499.8)	(497.9)
<b>Net assets</b>		<u>2,515.2</u>	<u>2,500.9</u>
<b>Capital and reserves</b>			
Called up share capital	17	10.0	10.0
Profit and loss reserve	18	842.7	827.9
Share based payment reserve	18	3.5	3.5
Revaluation reserve	18	1,659.0	1,659.5
<b>Total shareholder's funds</b>	18	<u>2,515.2</u>	<u>2,500.9</u>

The financial statements on pages 29 to 53 were approved by the board of directors on 27 June 2012 and signed on their behalf by

Richard Flint  
Chief Executive Officer



Yorkshire Water Services Ltd  
Registered in England no 2366682

# Notes to the Financial Statements

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## Notes to the financial statements for the year ended 31 March 2012

### 1. ACCOUNTING POLICIES

The following paragraphs summarise the more important accounting policies applied in the preparation of the accounts

#### **Basis of preparation and accounting**

The company's financial statements are prepared on a going concern basis, under the historical cost convention as modified by the revaluation of certain tangible fixed assets, in compliance with all applicable United Kingdom accounting standards (Financial Reporting Standards 'FRS', Statement of Standard Accounting Practice 'SSAP' and Urgent Issues Task Force abstract 'UITF') and, except where otherwise stated in the notes to the accounts, with the Companies Act 2006

The accounting policies have been reviewed in accordance with the requirements of FRS 18. The directors consider that the accounting policies set out below remain most appropriate to the company's circumstances, have been consistently applied and are supported by reasonable and prudent estimates and judgements

The financial statements present information about the company as an individual company undertaking and do not contain consolidated financial information as the parent of a group. The company is exempt from preparing group financial statements under Section 400 of the Companies Act 2006 as it and its subsidiary undertakings are included by full consolidation in the consolidated financial statements of its ultimate UK parent, Kelda Eurobond Co Ltd, a company registered in England and Wales

The accounts do not include a cashflow statement because the cashflows of the company are consolidated in the cashflow statement of the Kelda Eurobond Co Ltd financial statements in accordance with FRS 1 (Revised)

The accounts reflect the benefit of a revaluation of tangible fixed assets as a prior year adjustment and comparative figures for 2011 have been restated

#### **Turnover**

Turnover comprises charges to customers for water, sewerage and other services excluding value added tax and is derived only from the United Kingdom

Turnover is not recognised until the service has been provided to the customer. Turnover relates to charges due in the year, excluding any amounts paid in advance. Turnover for measured water charges includes amounts billed plus an estimation of the amounts unbilled at the year end. The accrual is estimated using a defined methodology based upon daily average water consumption, which is calculated based upon historical billing information

No turnover is recognised for unoccupied properties and no bills are raised. If a bill has been issued, and the company subsequently become aware that the property is unoccupied, the bill and relevant turnover is cancelled. Generally a property is classed as void if it is unoccupied and unfurnished

#### **Pensions**

The company accounts for its pensions in accordance with FRS 17 "Retirement Benefits". A majority of the company's employees participate in the Kelda Group Pension Plan (KGPP), a group defined benefit pension scheme as described in note 21 of the financial statements. The KGPP is a group multi-employer scheme, such that the company's pension scheme's assets and liabilities are included with those of other companies in the KGPP. The company is unable to identify its share of the underlying assets and liabilities in

## **Notes to the Financial Statements**

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the scheme on a consistent and reasonable basis and therefore accounts for the scheme as if it was a defined contribution scheme. The KGPP closed to new members in 2006. The company also provides a defined contribution scheme, Kelda Stakeholder+, which is available to new and existing employees.

### **Share based payments**

#### **Savings related share option scheme**

In prior years, the then ultimate parent company, Kelda Group Ltd (formerly Plc), operated a savings related share option scheme under which options were granted to employees. The fair value of options granted in exchange for employee services rendered was recognised as an expense in Yorkshire Water's profit and loss account with a corresponding credit to equity.

The total amount expensed over the vesting period was determined by the fair value of the option at the date of the grant. The fair value of the option calculated was determined by use of mathematical modelling including the Black Scholes option pricing model.

The Group re-assesses its estimate of the number of options that are expected to become exercisable at each balance sheet date. Any adjustments to the original estimates are recognised in the profit and loss account (and equity). No expense is recognised for awards that did not ultimately vest, except for awards where vesting was conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition was satisfied, provided that all other performance conditions are satisfied.

During 2008/09 the scheme was closed following the acquisition of Kelda Group Plc by Saltaire Water Ltd. Certain schemes have been allowed to continue until the planned maturity, with members choosing whether to continue contributing. For any member who has taken that option, charges to the profit and loss account will continue until the maturity of the scheme. For any other member who has opted to close their scheme, charges to the profit and loss account ceased in the month that they chose to leave the scheme.

For both share options the corresponding entries to equity represent capital contributions from the parent company. When the amounts are recharged by the parent, a corresponding entry to reserves is recorded.

#### **Research and development expenditure**

Research and development expenditure is written off in the profit and loss account in the financial year in which it is incurred. Expenditure on fixed assets relating to development projects is written off over the expected useful life of those assets.

#### **Taxation**

The taxation charge is based on the result for the year as adjusted for disallowable and non-taxable items using current rates and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and for accounting purposes.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more or a right to pay less tax in the future have occurred at the balance sheet date, subject to the following:

- provision is made for gains on disposals of fixed assets that have been rolled over into replacement assets only where, at the balance sheet date, there is a commitment to dispose of the replacement assets, and

## **Notes to the Financial Statements**

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- deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted

Deferred tax is calculated at the rates at which it is estimated that tax will arise based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax is discounted.

### **Investments**

Other fixed asset investments are stated at cost and reviewed for impairment if there are any indications that the carrying value may not be recoverable.

### **Intangible assets**

Goodwill is the excess of the fair value of the consideration paid for a business or an associate over the fair value of the identifiable assets and liabilities acquired. Goodwill is recognised and amortised on a straight line basis over its economic useful life, which normally will not exceed 20 years. Impairment tests on the carrying value of goodwill are undertaken at the end of the first full financial year following the acquisition and in other periods if events or changes in circumstances indicate that the carrying value may not be recoverable. When it is determined that the carrying value of goodwill exceeds the recoverable amount, the excess is written off to the profit and loss account.

### **Tangible fixed assets and depreciation**

Tangible fixed assets comprise the following:

#### **Infrastructure assets**

Infrastructure assets comprise a network of systems being mains and sewers, impounding and pumped raw water storage reservoirs, dams and sea outfalls.

Expenditure on infrastructure assets to increase capacity or enhance the network and to maintain the operating capability of the network in accordance with defined standards of service is treated as a fixed asset addition and included at cost after deducting grants and contributions.

Following a change in accounting policy in 2012, infrastructure assets are held at valuation with external valuations being undertaken on a periodic basis. An interim valuation is booked in the intervening years if in the view of the directors there has been a material change. The depreciation charge for infrastructure assets is the estimated level of annual expenditure required to maintain the operating capability of the network based on an independently certified asset management plan.

Adopted assets, including private drains and sewers, are recognised at cost, which is generally £nil.

#### **Other tangible fixed assets**

Following a change in accounting policy in 2009, residential properties, non-specialised properties and rural estates held within land and buildings are held at valuation. Other tangible fixed assets are included at cost, which represents the purchase price, less accumulated depreciation. Finance costs incurred in respect of the construction of other tangible fixed assets are expensed as incurred.

Freehold land is not depreciated. Depreciation is charged on other tangible fixed assets (including those assets held at valuation, where appropriate) on a straight-line basis over their estimated economic lives, or the estimated useful economic lives of their individual major components, from the month following commissioning. Useful economic lives are principally as follows:

# Notes to the Financial Statements

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Buildings	25 - 60 years
Fixed plant	5 - 40 years
Vehicles, mobile plant and computers	3 - 10 years

Fixed plant, vehicles, mobile plant and computers are classified as plant and equipment within Note 9. Assets under construction are not depreciated until they are brought into use. Residential properties, non-specialised properties and rural estates are held at valuation with external valuations being undertaken on a periodic basis. An interim valuation is booked in the intervening years if in the view of the directors there has been a material change.

## **Leased assets**

Assets which are financed by leasing agreements that transfer substantially all the risks and rewards of ownership to the lessee (finance leases) are capitalised in tangible fixed assets and the corresponding capital cost is shown as an obligation to the lessor in borrowings. Depreciation is generally charged to the profit and loss account over the shorter of the estimated useful life and the term of the lease. If the operational life of an asset is longer than the lease term, and the agreement allows an extension to that term, the asset may be depreciated over its operational life. The capital element of lease payments reduces the obligation to the lessor and the interest element is charged to the profit and loss account over the term of the lease in proportion to the capital amount outstanding.

All other leases are operating leases and the rentals are charged to the profit and loss account on a straight-line basis over the term of the lease.

## **Grants and contributions**

Grants and contributions in respect of tangible assets, other than infrastructure assets as described below, are deferred and credited to the profit and loss account by installments over the expected economic useful lives of the related assets.

Grants and contributions in respect of expenditure enhancing the infrastructure network are applied in reducing that expenditure. This is not in accordance with the Companies Act 2006, which requires tangible fixed assets to be shown at cost and hence grants and contributions as deferred income. The presentation is adopted because infrastructure assets do not have determinable finite lives and therefore such grants and contributions would remain as liabilities in perpetuity. The directors consider that the company's presentation shows a true and fair view of the investment in infrastructure assets.

Grants and contributions received in respect of expenditure charged to the profit and loss account during the year are included in the profit and loss account.

## **Stock**

Stock is stated at cost less any provision necessary to recognise damage and obsolescence. Work in progress is stated at the lower of cost and net realisable value. Cost includes labour, materials, and an appropriate proportion of overheads.

## **Receipts in advance**

Receipts in advance include the monies received from customers where the related turnover has not yet been recognised and also grants and contributions received in relation to capital schemes where the work has not yet commenced. They are recognised within other creditors until the related revenue or costs are recognised.

## **Foreign currencies**

Individual transactions denominated in foreign currencies are translated into sterling at the actual exchange rates ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currency are translated at the exchange rates prevailing at the balance

## **Notes to the Financial Statements**

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sheet date Profits and losses on both individual currency transactions settled during the year and unsettled monetary assets and liabilities are dealt with in the profit and loss account

### **Provisions**

Provisions are recognised when the company has a present obligation as a result of a past event, it is probable that a transfer of economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation

Provision is made in accordance with FRS 12 "Provisions, contingencies and commitments" for self insured claims, including an estimate for claims incurred but not reported

Provisions also include index linked swaps novated from Saltaire Water Ltd to Yorkshire Water in August 2008 Under the terms of the agreement, the swaps were transferred to Yorkshire Water at fair value and are held in the balance sheet as a provision This provision is being amortised over the life of the swaps (38 years) and is not discounted This provision is reviewed at each balance sheet date against the mark to market valuation of the swaps

### **Financial instruments**

#### **Trade debtors and creditors**

Trade debtors do not carry any interest and are stated at their nominal value as reduced by appropriate allowances for estimated recoverable amounts There is no intention to trade the debtors Trade creditors are not interest bearing and are stated at their invoiced value

#### **Interest rate swaps and cross-currency interest rate swaps**

Interest rate swaps (and cross-currency interest rate swaps) are used to hedge the company's exposure to fluctuations in interest rates and foreign exchange rates on its borrowings The amounts payable or receivable in respect of interest rate swaps are accounted for on an accruals basis through adjustments to the interest expense of the corresponding liability

#### **Index linked swaps**

Index linked swaps are intended to hedge Yorkshire Water's exposure to movements in RPI against its LIBOR linked borrowings

Yorkshire Water applies hedge accounting for its swaps to the extent that there is sufficient floating rate debt within Yorkshire Water, over the entire life of the swap, from existing or expected future debt To the extent that there is insufficient floating rate debt and the mark to mark valuation of the swap is negative, any exposure relating to the portion of the swap that is not hedged is provided for in the balance sheet as an onerous contract provision

The swaps have three cashflows

- Six monthly interest receivable linked to LIBOR,
- Six monthly interest payable linked to RPI, and
- An RPI-linked final bullet payment that is payable on maturity of the instruments or at certain predetermined points in time over the life of the swaps

Interest payments and receipts are accrued in the profit and loss account The RPI bullet is calculated based on the RPI at the measurement date, accrued in the profit and loss account and recognised within long term borrowings

These swaps were novated to Yorkshire Water from Saltaire Water Ltd in August 2008 at which time the swaps were out of the money by £308.9m This value was reflected in Yorkshire Water's balance sheet as an intercompany debtor, with a provision for the same

## Notes to the Financial Statements

amount The onerous contract provision above takes into account the unamortised novation provision

The calculation of the onerous contract provision takes account of both the RPI swaps and the interest rate (finance lease) swaps

The company is not required to prepare its financial statements in accordance with FRS 26 and apart from the provisions noted above its index linked swaps are not recognised in the financial statements in accordance with UK GAAP (note 15)

### 2. OPERATING PROFIT

Operating profit (before exceptional costs) is stated after (crediting)/charging

	<b>2012</b>	<b>2011</b>
	<b>£m</b>	<b>£m</b>
Own work capitalised	<b>(35.8)</b>	(31.6)
Raw materials and consumables	<b>26.6</b>	22.7
Other external charges	<b>255.2</b>	234.3
Wages and salaries	<b>76.7</b>	71.3
Social security costs	<b>7.2</b>	6.3
Pension costs (note 21)	<b>27.5</b>	25.9
Depreciation of fixed tangible assets (note 9)		
On owned assets		
- infrastructure	<b>59.8</b>	59.6
- other assets	<b>155.8</b>	151.7
On assets held under finance leases		
- infrastructure	<b>1.6</b>	2.3
- other assets	<b>8.5</b>	9.1
Operating lease charges		
- plant and equipment	<b>1.9</b>	1.9
- other	<b>0.6</b>	0.7
Amortisation of grants and contributions	<b>(3.3)</b>	(3.1)
Amortisation of goodwill on subsidiary undertakings (note 8)	<b>1.0</b>	0.9
Restructuring costs	<b>0.6</b>	0.2
Research and development	<b>0.7</b>	0.8
Other operating income	<b>(3.9)</b>	(5.1)
	<b><u>580.7</u></b>	<b><u>547.9</u></b>

#### Exceptional operating costs

Following the severe winters experienced during 2009/10 and 2010/11, Yorkshire Water's network of water mains suffered an increase in the number of bursts and consequently experienced a higher level of leakage. During 2011/12 additional expenditure was incurred to improve leakage performance such that leakage targets could be achieved even in the event of another severe winter. The additional spend was monitored separately by management and is over and above historic levels of investment. The additional spend of £9.6m is material and therefore is disclosed separately within the financial statements in line with FRS 3.

Exceptional operating costs in the year ended 31 March 2011 of £5.9m relate to costs incurred during the severe winter weather in December 2010.

# Notes to the Financial Statements

## Services provided by the company's auditors

During the year the company obtained the following services from its auditors at costs as detailed below

	2012 £'000	2011 £'000
Fees payable for the audit	151	132
Fees payable for taxation services	8	16
Fees payable for other services	14	50
	<u>173</u>	<u>198</u>

## Average number of employees

The average number of persons employed by the company during the year was

	2012 Number	2011 Number
Operational	1,882	1,723
Capital investment	102	100
Admin	505	506
Total average number of employees	<u>2,489</u>	<u>2,329</u>

## 3. DIRECTORS' EMOLUMENTS

(excluding those listed below)

	2012 £'000	2011 £'000
Aggregate emoluments	<u>1,678</u>	<u>1,367</u>
The amounts in respect of the highest paid director are as follows		
Emoluments	<u>362</u>	<u>361</u>

Stuart Baldwin, Jane Seto, Mark Lorkin, Scott Auty, Rhys Evenden and Holly Koepfel are non-executive directors of Kelda Holdings Ltd and do not receive any emoluments for their service

All executives have service agreements which are terminable by the company on 12 months' notice

During 2011/12, all except two executive directors were contributory members of the Kelda Group Pension Plan, a defined benefit scheme. Two directors were contributory members of the Kelda Stakeholder Plus scheme (a money purchase scheme). The accrued pension benefit of the highest paid director in 2011/12 was £73,472 (2011 £61,178). The company contributed £56,303 to defined contribution schemes on behalf of directors (2011 £nil). No directors have exercised share options during the year (2011 nil).

## 4. NON OPERATING EXCEPTIONAL COSTS

Yorkshire Water holds certain index linked swaps with a nominal value of £1,289m which had an adverse market value at 31 March 2012 of £1,403.7m. At the balance sheet date it was concluded that 28% (2011 43%) of the swaps (£391.9m of the £1,403.7m) did not represent an effective hedge. The unhedged portion is recognised within the balance sheet, £64.5m (2011 £40.0m) classified as borrowings in relation to the RPI uplift to date and £327.4m (2011 £335.5m) classified as an onerous contract provision within the accounts. The only movement in the onerous contract provision during the year relates to the annual amortisation of the provision over the life of the swaps recognised within interest receivable and similar income. During the prior year the provision was increased by £40.0m and recognised as a non-operating exceptional cost.

# Notes to the Financial Statements

## 5. INTEREST PAYABLE AND SIMILAR CHARGES BEFORE EXCEPTIONAL COSTS

	2012 £m	2011 £m
<b>Interest receivable and similar income:</b>		
Inter-company loans	(58.2)	(42.3)
Index linked swaps	(14.7)	(12.4)
Amortisation of fair value of index linked swaps (note 15)	(8.1)	(8.1)
Other	(0.3)	(0.7)
	<u>(81.3)</u>	<u>(63.5)</u>
<b>Interest payable and similar charges:</b>		
Bank loans and overdrafts	15.3	16.7
Finance leases	7.6	7.2
Inter-company loans	179.1	182.6
RPI uplift on index linked swaps	63.8	22.8
Interest rate swap interest	4.7	9.4
Index linked swaps coupon payable	36.7	39.3
Other	8.9	16.7
	<u>316.1</u>	<u>294.7</u>
<b>Net interest payable</b>	<u>234.8</u>	<u>231.2</u>

Net interest payable includes one off, non-recurring fees of £3.2m (2011 £1.8m)

Interest of £9.3m on a finance lease due April 2012 was paid in March 2012. This payment was included within prepayments (note 12) and is not included within the interest shown above.

Of £58.2m interest receivable on inter company loans during the year, £55.3m was received from Kelda Holdco Ltd.

## 6. TAX CREDIT ON PROFIT ON ORDINARY ACTIVITIES

	2012 £m	2011 £m
<b>Current tax:</b>		
Corporation tax at 26% (2011 28%)	0.7	14.7
Adjustments in respect of prior years	(19.6)	(30.8)
Total current tax	<u>(18.9)</u>	<u>(16.1)</u>
<b>Deferred tax:</b>		
Charge for timing differences arising and reversing in the year	(21.2)	(18.2)
Adjustments in respect of prior years	1.1	1.3
	<u>(20.1)</u>	<u>(16.9)</u>
Increase/(decrease) in discount	65.8	(4.8)
Effect of change in tax rate	(36.0)	(37.5)
Total deferred tax (note 16)	<u>9.7</u>	<u>(59.2)</u>
<b>Total tax credit:</b>	<u>(9.2)</u>	<u>(75.3)</u>

Note 16 shows further detail on the discounting of the deferred tax provision.

## Notes to the Financial Statements

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The difference between the total current tax charge shown and the amount calculated by applying the standard rate of UK corporation tax to the profit before tax is as follows

	<b>2012</b>	<b>2011</b>
	<b>£m</b>	<b>£m</b>
<b>Profit on ordinary activities before tax</b>	<b>68.6</b>	<b>42.4</b>
Tax on profit on ordinary activities at standard UK corporation tax rate of 26% (2011 28%)	<b>17.8</b>	11.9
Effects of		
Income not chargeable for tax purposes	<b>(1.1)</b>	(0.9)
Expenses not deductible for tax purposes	<b>7.4</b>	5.0
Capital allowances less than depreciation and other timing differences	<b>16.0</b>	19.5
Movement in short term timing differences	<b>0.1</b>	(1.1)
Utilisation of tax losses in other group companies	<b>(39.5)</b>	(19.7)
Adjustments in respect of prior years	<b>(19.6)</b>	(30.8)
Current tax credit for the year	<b>(18.9)</b>	(16.1)

The tax charge in future periods may be affected by the following factors

- capital investment is expected to remain at similar levels. The company expects to be able to claim capital allowances in excess of depreciation in future years
- changes in the medium and long-term interest rates used to discount deferred tax assets and liabilities will affect the amount of deferred tax charged in the profit and loss account

In 2012 the adjustments in respect of prior years of £19.6m relates to the release of the over provision of tax provisions in previous periods. Upon agreement of the tax treatment of items with HM Revenue and Customs, these provisions have now been released.

In addition, industrial buildings allowances were phased out at the end of March 2011. The net impact of this change is not expected to be material.

In addition to the changes in rates of Corporation tax disclosed above a number of further changes to the UK Corporation tax system were announced in the March 2011 UK Budget Statement.

Legislation to reduce the main rate of corporation tax from 24% to 23% from 1 April 2013 is expected to be included in the Finance Act 2012. Further reductions to the main rate are proposed to reduce the rate to 22% from 1 April 2014. These further changes had not been substantively enacted at the balance sheet date and, therefore, are not included in these financial statements.

The effect of the changes expected to be enacted in the Finance Act 2012 would be to reduce the deferred tax liability provided at the balance sheet date by £7.1m. This £7.1m decrease in the deferred tax liability would increase profit by £7.1m.

The proposed reduction of the main rate of corporation tax to 22% from 1 April 2014 is expected to be enacted separately. The overall effect of this further change, if it applied to the deferred tax balance at the balance sheet date, would be to further reduce the deferred tax liability by an additional £7.1m.

# Notes to the Financial Statements

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## 7. DIVIDENDS

No final dividend for the year has been proposed. The dividend in the year of £63.4m (2011 £46.9m) was paid in order to fund interest and a loan repayment on a loan from Yorkshire Water to Kelda Holdco Ltd.

## 8. INTANGIBLE ASSETS

	<i>Goodwill</i>
<b>Cost</b>	<b>£m</b>
Balance at 1 April 2011 and 31 March 2012	<u>17.9</u>
<b>Amortisation</b>	
Balance at 1 April 2011	(10.3)
Charge for the year	<u>(1.0)</u>
Balance at 31 March 2012	<u>(11.3)</u>
<b>Net book amount as at 31 March 2012</b>	<b><u>6.6</u></b>
Net book amount as at 31 March 2011	<u>7.6</u>

Goodwill arose on the transfer of the trade and net assets of The York WaterWorks Ltd on 1 April 2000 and is being amortised over 19 years. The directors do not believe this should be impaired as it relates to assets which are still in continuing use within the business.

## Notes to the Financial Statements

### 9. TANGIBLE ASSETS

	Land and buildings	Infrastructure assets	Plant and equipment	Under construction	Total
	£m	£m	£m	£m	£m
<b>Cost or valuation</b>					
At 1 April 2011 as previously stated	1,765.0	2,731.5	2,470.0	288.9	7,255.4
Prior year adjustment	-	1,607.9	-	-	1,607.9
At 1 April 2011 as restated	1,765.0	4,339.4	2,470.0	288.9	8,863.3
Additions	8.2	60.7	42.4	304.4	415.7
Transfers on commissioning	9.9	13.8	53.7	(77.4)	-
Disposals - external	(6.4)	-	(5.8)	(0.2)	(12.4)
Grants and contributions	-	-	-	(11.4)	(11.4)
<b>At 31 March 2012</b>	<b>1,776.7</b>	<b>4,413.9</b>	<b>2,560.3</b>	<b>504.3</b>	<b>9,255.2</b>

#### Depreciation

At 1 April 2011	556.3	1,075.3	1,266.0	-	2,897.6
Disposals	(6.1)	-	(5.7)	(0.2)	(12.0)
Depreciation for the year	34.6	61.3	129.6	0.2	225.7
<b>At 31 March 2012</b>	<b>584.8</b>	<b>1,136.6</b>	<b>1,389.9</b>	<b>-</b>	<b>3,111.3</b>
<b>Closing net book amount</b>	<b>1,191.9</b>	<b>3,277.3</b>	<b>1,170.4</b>	<b>504.3</b>	<b>6,143.9</b>
Opening net book amount	1,208.7	3,264.1	1,204.0	288.9	5,965.7

At 31 March 2012 assets above held under finance leases amounted to

Cost	109.5	71.7	192.6	-	373.8
Depreciation	(32.1)	(23.3)	(129.4)	-	(184.8)
<b>Closing net book amount</b>	<b>77.4</b>	<b>48.8</b>	<b>63.2</b>	<b>-</b>	<b>189.0</b>
Opening net book amount	92.5	78.3	72.2	-	243.0

	Cost at 31 March 2012	Depreciation at 31 March 2012	Net book value at 31 March 2012	Net book value at 31 March 2011
	£m	£m	£m	£m
<b>The net book amount of land and buildings comprised:</b>				
Freehold properties	1,771.1	(583.8)	1,187.3	1,203.7
Properties held on long lease	0.5	-	0.5	0.5
Properties held on short lease	5.1	(1.0)	4.1	4.5
	<b>1,776.7</b>	<b>(584.8)</b>	<b>1,191.9</b>	<b>1,208.7</b>

Grants and contributions received relating to infrastructure assets have been deducted from the cost of fixed assets. The company's accounting policy in respect of grants and contributions is a departure from the Companies Act 2006 requirements and is adopted, as explained in the accounting policy note on page 34, in order to show a true and fair view of the investment in infrastructure assets.

## Notes to the Financial Statements

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Certain classes of the company's tangible fixed assets were revalued at March 2012. These valuations were performed in accordance with FRS 15 which requires that assets subject to a policy of revaluation should be carried at their current value.

Current value is defined in FRS 15 as the lower of replacement cost and recoverable amount. The recoverable amount is further defined as the higher of Net Realisable Value ("NRV") and Value in Use ("VIU"). Having considered the above definitions of value, Management, based upon KPMG's advice, concluded that the most reliable valuation method to determine the current value for the tangible fixed assets of a UK water company is a two step approach:

- Estimating the business VIU, using a discounted cash flow ("DCF") model excluding outperformance against Ofwat's targets to determine the business enterprise value. Excluding forecast outperformance against the regulatory allowance is a proxy for excluding any goodwill that a purchaser would pay for the business. The enterprise value was then cross-checked against the Regulatory Capital Value ("RCV"). This step was followed by
- Allocating the VIU of the business (less relevant working capital balances and other adjustments) to individual classes of tangible fixed assets.

Such valuations were incorporated into the financial statements and the resulting revaluation adjustments taken to the revaluation reserve.

If the revalued assets were stated on a historical cost basis, the historic cost before depreciation would be £4,536.0m (2011: £4,357.8m).

Certain other categories of the company's land and buildings are also held at valuation, on the basis of existing use, valued by independent qualified valuers in March 2009. The valuations were undertaken in accordance with the Appraisal and Valuation Manual of the Royal Institution of Chartered Surveyors in the UK. These external valuations will be re-performed on a periodic basis. An interim valuation is booked in intervening years based on directors' valuations. No changes in values have been booked during the year.

No deferred tax is provided on timing differences arising from the revaluation of fixed assets unless, by the balance sheet date, a binding commitment to sell the asset has been entered into and it is unlikely that any gain will be rolled over.

Categories of assets revalued are as follows:

	Valuation	Historical cost basis
	£m	£m
Infrastructure assets	3,277.3	1,669.4
Non-specialist properties	7.5	2.4
Rural estates	43.9	0.8
Residential properties	4.7	0.1
	<u>3,333.4</u>	<u>1,672.7</u>

## Notes to the Financial Statements

Analysis of the net book value of revalued non specialised land and buildings is as follows

	Valuation	Historical cost basis
	£m	£m
31 March 2010	55.5	3.3
Disposal of revalued assets	(0.3)	-
Transfer to the profit and loss account in respect of additional depreciation incurred on revaluation	<u>(0.3)</u>	<u>-</u>
31 March 2011	54.9	3.3
Disposal of revalued assets	(0.2)	-
Transfer to the profit and loss account in respect of additional depreciation incurred on revaluation	<u>(0.3)</u>	<u>-</u>
<b>31 March 2012</b>	<b><u>54.4</u></b>	<b><u>3.3</u></b>

Analysis of the net book value of revalued infrastructure assets is as follows

	Valuation	Historical cost basis
	£m	£m
At cost	4,413.9	2,806.0
Aggregate depreciation	<u>(1,136.6)</u>	<u>(1,136.6)</u>
<b>31 March 2012</b>	<b><u>3,277.3</u></b>	<b><u>1,669.4</u></b>

If the revalued assets noted above were sold at the values shown, a tax charge of £431.3m would arise. However the infrastructure assets form an integral part of the business and as such Yorkshire Water have no plans to dispose of the assets.

### 10. INVESTMENTS

Investments of £0.1m at 31 March 2012 and 31 March 2011 includes £27,119 of 8% Unsecured Loan Stock in Water Research Centre (1989) Plc, which conducts research on behalf of the water industry.

The company has taken advantage of the exemption from preparing group accounts under section 400 of the Companies Act 2006. Consolidated accounts have been prepared by Kelda Eurobond Co Ltd, the largest UK group to consolidate these accounts. Copies can be obtained from the Company Secretary, Kelda Eurobond Co Ltd, Western House, Halifax Road, Bradford, BD6 2SZ.

### 11. STOCK

	2012	2011
	£m	£m
Raw materials and consumables	<u>1.2</u>	<u>1.2</u>

# Notes to the Financial Statements

## 12. DEBTORS

	2012 £m	2011 £m
<b>Receivable within one year</b>		
Trade debtors	79.5	77.9
Amounts owed by group undertakings	10.8	10.6
Amounts owed by subsidiary undertakings	2.3	1.4
Prepayments and accrued income	59.0	59.8
Taxation receivable	16.7	-
Other debtors	18.3	10.3
	<u>186.6</u>	<u>160.0</u>
<b>Receivable after more than one year</b>		
Amounts owed by Group undertakings	1,289.4	928.8
Other debtors	0.1	0.1
	<u>1,289.5</u>	<u>928.9</u>

Amounts owed by Group undertakings within one year and after more than one year includes £280.4m (2011 £288.6m) in respect of the fair value of index linked swaps at the date of novation from Saltaire Water Ltd to Yorkshire Water in August 2008 and £1,009.0m upstream loans to Kelda Holdco Ltd (2011 £640.2m)

## 13. OTHER CREDITORS

	2012 £m	2011 £m
<b>Amounts falling due within one year:</b>		
Trade creditors	53.3	46.9
Capital creditors	103.0	104.4
Deferred grants and contributions on depreciating fixed assets	2.9	2.9
Amounts owed to Group undertakings	14.2	17.0
Amounts owed to subsidiary undertakings	75.4	74.1
Social security and other taxes	2.0	1.9
Taxation payable	-	5.7
Receipts in advance	48.6	50.3
Other creditors	19.9	30.6
	<u>319.3</u>	<u>333.8</u>
<b>Amounts falling due after more than one year:</b>		
Deferred grants and contributions on depreciating fixed assets	68.0	71.0
Other creditors	57.5	63.4
	<u>125.5</u>	<u>134.4</u>

Amounts owed to subsidiary companies are in relation to accrued interest on debt raised by subsidiaries and lent to Yorkshire Water to finance its operations

# Notes to the Financial Statements

## 14. AGGREGATE BORROWINGS AND CASH

	2012			Total
	Bank loans and overdrafts	Other loans	Finance leases	
	£m	£m	£m	£m
<b>Short term borrowings:</b>				
In one year or less or on demand	48.8	-	6.9	55.7
<b>Long term borrowings:</b>				
In more than one year, but not more than two years	34.0	-	24.6	58.6
In more than two years, but not more than five years	94.6	-	100.3	194.9
In more than five years	165.1	64.5	163.3	392.9
	293.7	64.5	288.2	646.4
Amounts owed to group companies				3,474.3
				<u>4,120.7</u>
Cash at bank and in hand				(8.3)
Amounts owed from group companies				(1,009.0)
<b>Net debt at 31 March 2012</b>				<u><u>3,159.1</u></u>

	2011			Total
	Bank loans and overdrafts	Other loans	Finance leases	
	£m	£m	£m	£m
<b>Short term borrowings:</b>				
In one year or less or on demand	45.9	-	17.4	63.3
<b>Long term borrowings:</b>				
In more than one year, but not more than two years	41.0	-	20.1	61.1
In more than two years, but not more than five years	91.7	-	90.3	182.0
In more than five years	127.1	40.0	237.3	404.4
	259.8	40.0	347.7	647.5
Net amounts owed to group companies				2,931.1
				<u>3,578.6</u>
Cash at bank and in hand				(45.4)
Amounts owed from group companies				(640.2)
<b>Net debt at 31 March 2011</b>				<u><u>2,956.3</u></u>

Net amounts owed to Group companies includes £1,009.0m receivable (2011 £640.2m) in relation to loans to parent companies. This is disclosed within debtors receivable after more than one year.

## **Notes to the Financial Statements**

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Amounts owed to Group companies includes loans from other members of the Yorkshire Water Financing Group relating to bonds originally held by Yorkshire Water Services Finance Limited, subsequently exchanged for bonds held by Yorkshire Water Services Odsal Finance Ltd (see note 3 to the regulatory accounts)

Yorkshire Water raises debt as part of the Yorkshire Water financing group. This group of companies includes Yorkshire Water and its subsidiary companies. Debt covenants covering the financing group include the consolidated external debt of this group of companies. When calculating the consolidated debt position it should be noted that the book value recorded in these accounts on the internal loan relating to the exchanged bonds is higher than the book value recorded in Yorkshire Water Services Odsal Finance Ltd accounts by £36.0m, which account for the exchanged bonds in line with International Accounting Standard 39.

Net debt includes unamortised issue costs of £1.4m (2011 £0.1m)

Borrowings repayable in instalments after more than five years include £163.3m (2011 £237.3m) in respect of finance leases which have expiry dates ranging from 2018 to 2043 and carry interest rates based on 12 month LIBOR (London Interbank Offered Rate) and 6 month LIBOR. The finance lease creditors are secured on the underlying assets.

As at 31 March 2012 Yorkshire Water had access to undrawn committed bank facilities totalling £324.0m (2011 £510m), £249m of which expires in October 2016 and £75.0m which must be drawn by way of loan by 30 June 2013.

### **15. FINANCIAL DERIVATIVES**

#### **Interest rate swaps**

Yorkshire Water holds £45.0m nominal value (2011 £125.0m) of floating to fixed rate interest swaps. These swaps had an out of the money mark to market value of £19.4m at 31 March 2012 (2011 £15.2m).

#### **Cross currency Interest rate swaps**

Yorkshire Water hedges the fair value of the US Dollar bonds using a series of combined interest rate and foreign currency swaps that in combination form cross currency interest rate swaps, swapping dollar principal repayments into sterling and fixed rate dollar interest payments into floating rate sterling interest payments. These swaps had an out of the money mark to market value of £3.4m at 31 March 2012.

#### **Index linked swaps**

In February 2008, Saltaire Water Ltd, at that time an intermediate parent company, entered into certain index linked ('IL') swaps, with a nominal value of £1,289m. These swaps were novated to Yorkshire Water in August 2008 at which time the swaps had an adverse market value of £308.9m. This value was reflected in Yorkshire Water's balance sheet as an intercompany debtor, receivable from Saltaire Water Ltd, with a provision for the same amount. The provision is amortised through the Yorkshire Water profit and loss account over a 38 year period (being the remaining weighted average life of the swaps) and for 2011/12 the amortisation charge was £8.1m.

A proportion of these swaps have mandatory break dates prior to the ultimate maturity date and during the period the portfolio was reprofiled such that break dates in 2012 and 2014 were removed. This was achieved by, amongst other things, moving a proportion of the swap portfolio (£463m) to a Pay-As-You-Go ("PAYG") structure whereby Yorkshire Water paid down the RPI accretion to date at the time of the restructure and agreed to pay future RPI accretions at five yearly intervals. Swaps not subject to a PAYG structure pay RPI accretion in one single payment on maturity.

## Notes to the Financial Statements

Post the restructure, the total nominal amount of the swaps remained unchanged at £1,289m with maturity dates ranging from 2026 to 2063, £837m of the restructured swap portfolio have no mandatory break dates. The remaining swaps totalling £452m have break dates in 2018, 2020, 2023 and 2025.

There are three cashflows associated with the swaps

- Six monthly interest receivable linked to LIBOR,
- Six monthly interest payable linked to RPI, and
- An RPI-linked final bullet that is payable on maturity of the instruments or at certain predetermined dates over the duration of the swaps

Interest payments and receipts are accrued in the profit and loss account. The RPI bullet accumulated at the balance sheet date is discounted using an average of the 25 and 30 year gilt rate at the relevant date, accrued in the profit and loss account and recognised within long term borrowings.

With six month LIBOR and applicable discount rates at historically low levels in the short term, these swaps gave rise to an out of the money mark to market value of £1,403.7m (2011 £867.2m) at the year end date. Of this £64.5m (2011 £40.0m) has been recognised within long term borrowings, this represents the discounted value of the RPI bullet accrued to 31 March 2012, the RPI bullet accrued to 31 March 2012 was £143.2m which reduced by £78.7m when discounted to present values.

A further £327.4m is included within provisions for liabilities and charges (2011 £335.5m) (note 16) which represents an onerous contract provision in relation to the unhedged portion of the interest rate and index linked swaps.

When calculating the size of the provision required at 31 March 2012, the directors have considered that

- At the year end, the swaps are effectively hedging 72% of the floating rate debt held by Yorkshire Water and the further floating rate debt to be taken out by Yorkshire Water, and
- The swaps are held for the long term benefit of the business and provide a hedge against existing and future floating rate debt as Yorkshire Water gears up in the foreseeable future under the securitised structure.

All of the swaps outlined above were valued using information provided by external consultants, using a discounted cash flow model and quoted market information. This information is reviewed by the group treasury department and discussed with relevant directors to ensure it is appropriate for use.

### 16. PROVISIONS FOR LIABILITIES AND CHARGES

	Index linked swaps onerous contract provision £m	Deferred tax £m	Self insurance £m	Total £m
At 1 April 2010	295.5	221.3	0.3	517.1
(Credited)/charged to the profit and loss account or utilised in the year	40.0	(59.3)	0.1	(19.2)
At 31 March 2011	335.5	162.0	0.4	497.9
Charged/(credited) to the profit and loss account and utilised in the year	(8.1)	9.7	0.3	1.9
<b>At 31 March 2012</b>	<b>327.4</b>	<b>171.7</b>	<b>0.7</b>	<b>499.8</b>

## Notes to the Financial Statements

### Deferred tax

	2012	2011
	£m	£m
At 1 April	162.0	221.2
Deferred tax charged/(credited) to the profit and loss account	8.6	(60.5)
Adjustments in respect of prior years	1.1	1.3
<b>At 31 March</b>	<b>171.7</b>	<b>162.0</b>

Deferred tax is provided as follows

	At 31 March 2012	At 31 March 2011
	£m	£m
Accelerated capital allowances	440.5	492.5
Short term timing differences	(1.0)	3.1
Undiscounted provision for deferred tax	439.5	495.6
Discount	(267.8)	(333.6)
<b>Discounted provision for deferred tax</b>	<b>171.7</b>	<b>162.0</b>

The corporation tax rate of 24% (2011 26%) has been used to calculate the amount of deferred tax. In accordance with FRS 19 in order to reflect the time value of money, the company discounts its deferred tax liability. The period of discounting runs until the underlying timing differences completely reverse. In carrying out this calculation, all future movements in the accelerated capital allowances and depreciation charges are scheduled out on a yearly basis, taking account of future depreciation rates. No account is taken of timing differences that might arise on fixed assets expected to be purchased in the future. The discount rate used is the post-tax yield on Government gilts with equivalent maturity dates and currency to those of the deferred tax balance, at the balance sheet date.

### 17. CALLED UP SHARE CAPITAL

	<i>Authorised</i> £	<i>Allotted and fully paid</i> £
10,000,000 ordinary shares of £1 each at 31 March 2011 and 31 March 2012	10,000,000	10,000,000

## Notes to the Financial Statements

### 18. MOVEMENT IN TOTAL SHAREHOLDER'S FUNDS

	Profit and loss reserve	Share- based payment reserve	Share capital	Revaluation reserve	Total shareholder's funds
	£m	£m	£m	£m	£m
At 1 April 2010 as previously reported	756.5	3.4	10.0	52.2	822.1
Prior year adjustment	-	-	-	1,607.9	1,607.9
At 1 April 2010 restated	756.5	3.4	10.0	1,660.1	2,430.0
Profit for the year	117.7	-	-	-	117.7
Dividends	(46.9)	-	-	-	(46.9)
Revaluation reserve released during the year	0.6	-	-	(0.6)	-
Share-based payments amount due to parent	-	0.1	-	-	0.1
At 31 March 2011 restated	<b>827.9</b>	<b>3.5</b>	<b>10.0</b>	<b>1,659.5</b>	<b>2,500.9</b>
Profit for the year	77.7	-	-	-	77.7
Dividends	(63.4)	-	-	-	(63.4)
Revaluation reserve released during the year	0.5	-	-	(0.5)	-
At 31 March 2012	<b>842.7</b>	<b>3.5</b>	<b>10.0</b>	<b>1,659.0</b>	<b>2,515.2</b>

### 19. CAPITAL AND OTHER FINANCIAL COMMITMENTS

	2012 £m	2011 £m
Capital and infrastructure renewals expenditure commitments for contracts placed at 31 March were	<b>267.6</b>	<b>343.8</b>

The long term investment programme for the company, which identified substantial future capital expenditure commitments in the period 2010 to 2015, was agreed as part of the Periodic Review process which was finalised in December 2009

At the year end the company was committed to making the following annual payments during the next financial year under non-cancellable operating leases expiring as set out below

	Land and buildings 2012 £m	Other 2012 £m	Land and buildings 2011 £m	Other 2011 £m
<b>Leases which expire:</b>				
Within one year	-	1.0	-	0.7
Between two and five years	-	1.1	0.3	1.5
After five years	1.0	-	-	-
	<b>1.0</b>	<b>2.1</b>	<b>0.3</b>	<b>2.2</b>

# Notes to the Financial Statements

## 20. CONTINGENT LIABILITIES

The banking arrangements of the company operate on a pooled basis with other group companies and the bank balances of each subsidiary can be offset against each other. The company had guaranteed the following bonds with Yorkshire Water Services Finance Ltd, Yorkshire Water Services Bradford Finance Ltd and Yorkshire Water Services Odsal Finance Ltd at 31 March 2012

	Nominal £m	Coupon %	Maturity	Liability at 31 March 2012 £m
<b>Fixed rate</b>				
Yorkshire Water Services Finance Ltd	6.8	5.375%	2023	3.9
Yorkshire Water Services Finance Ltd	7.4	5.500%	2027	6.2
Yorkshire Water Services Finance Ltd	0.2	6.625%	2031	0.6
Yorkshire Water Services Finance Ltd	200.0	5.500%	2037	194.9
Yorkshire Water Services Odsal Finance Ltd	29.9	6.588%	2023	29.9
Yorkshire Water Services Odsal Finance Ltd	180.8	6.588%	2023	180.8
Yorkshire Water Services Odsal Finance Ltd	135.5	6.454%	2027	135.5
Yorkshire Water Services Odsal Finance Ltd	255.0	6.601%	2031	255.0
Yorkshire Water Services Bradford Finance Ltd	275.0	6.000%	2019	273.0
Yorkshire Water Services Bradford Finance Ltd	200.0	6.375%	2039	198.0
Yorkshire Water Services Bradford Finance Ltd	100.0	6.375%	2039	108.2
Yorkshire Water Services Bradford Finance Ltd	450.0	6.000%	2025	446.7
Yorkshire Water Services Bradford Finance Ltd	18.9	3.180%	2018	18.8
Yorkshire Water Services Bradford Finance Ltd	9.4	3.180%	2019	9.3
Yorkshire Water Services Bradford Finance Ltd	72.3	3.770%	2021	71.9
Yorkshire Water Services Bradford Finance Ltd	25.1	3.770%	2022	25.0
Yorkshire Water Services Bradford Finance Ltd	94.3	3.870%	2023	93.8
Yorkshire Water Services Bradford Finance Ltd	18.8	3.870%	2024	18.7
Yorkshire Water Services Bradford Finance Ltd	47.2	5.070%	2022	46.9
<b>Total fixed</b>				<b>2,117.1</b>
<b>Index linked</b>				
Yorkshire Water Services Finance Ltd	0.1	3.048%	2033	(1.1)
Yorkshire Water Services Odsal Finance Ltd	127.8	3.307%	2033	138.9
Yorkshire Water Services Finance Ltd	65.0	1.823%	2050	75.2
Yorkshire Water Services Finance Ltd	125.0	1.462%	2051	148.9
Yorkshire Water Services Finance Ltd	85.0	1.758%	2054	98.4
Yorkshire Water Services Finance Ltd	125.0	1.460%	2056	148.8
Yorkshire Water Services Finance Ltd	100.0	1.709%	2058	115.7
Yorkshire Water Services Bradford Finance Ltd	175.0	2.718%	2039	196.9
Yorkshire Water Services Bradford Finance Ltd	85.0	2.718%	2039	108.7
Yorkshire Water Services Bradford Finance Ltd	50.0	2.160%	2041	49.8
<b>Total index linked</b>				<b>1,080.2</b>

# Notes to the Financial Statements

## 21. PENSION COMMITMENTS

The company sponsors a UK pension scheme, the Kelda Group Pension Plan (KGPP). The KGPP has a number of benefit categories providing benefits on a defined benefit basis and one category providing benefits on a defined contribution basis.

Contributions during the year ended 31 March 2012 were paid by members at 3%, 4%, 4.5%, 5% or 6% of pensionable pay (depending on benefit category). The company contributed at 23.6% (2011: 22.2%) of members' pensionable pay during the accounting year in respect of the majority of members.

The most recent finalised actuarial valuation of the KGPP was carried out as at 31 March 2010 when the market value of assets was £838.2m. The company participates in the Group multi-employer scheme, such that the company's pension scheme's assets and liabilities are included with those of other subsidiary companies of Kelda Holdings Ltd. The company is unable to identify its share of the underlying assets and liabilities of the KGPP as the scheme's members are not unitised by company. The company therefore accounts for pension costs on a contribution basis.

The company's total pension charge for the year was £27.5m (2011: £25.9m). At 31 March 2012, the company had outstanding contributions of £1.2m (2011: £1.4m). An accrual for these unfunded benefits have been included in the company's accounts.

A summary of scheme position as disclosed in the Kelda Holdco Ltd accounts as at 31 March 2012 is as follows:

	2012		2011	
	Market value	Expected long term rate of return	Market value	Expected long term rate of return
	£m	%	£m	%
Fair value of scheme assets				
Equities	539.2	6.2	541.7	7.2
Bonds	279.6	4.2	251.0	4.9
Property	78.8	6.2	76.9	7.2
Other	6.4	3.5	5.3	4.4
Total value of assets	<u>904.0</u>		<u>874.9</u>	
Present value of scheme liabilities	<u>(1,003.7)</u>		<u>(914.9)</u>	
Net pension liability	<u>(99.7)</u>		<u>(40.0)</u>	

Pension contributions are determined with the advice of independent qualified actuaries, Mercer Human Resource Consulting, on the basis of annual valuations using the projected unit credit method and use the following assumptions:

	2012	2011
Inflation	3.2%	3.4%
Rate of increase in salaries	4.2%	4.4%
Rate of increase to pensions in payment and deferred pensions	3.2%	3.4%
Discount rate for scheme liabilities	5.1%	5.5%
Life expectancy of male pensioner aged 60 (in years)	26.6	26.4
Projected life expectancy at age 60 for male aged 40 (in years)	28.7	28.4

# Notes to the Financial Statements

## 22. ULTIMATE PARENT UNDERTAKING

The company's immediate parent company is Yorkshire Water Services Holdings Ltd. The company's ultimate parent company and controlling party is Kelda Holdings Ltd, a company registered in Jersey.

Kelda Holdco Ltd, a company registered in England and Wales, is the parent undertaking of the smallest group to consolidate these accounts. Kelda Eurobond Co Ltd, a company registered in England and Wales, is the largest UK group to consolidate these accounts.

Copies of the Group accounts may be obtained from the Company Secretary, Kelda Eurobond Co Ltd, Western House, Halifax Road, Bradford BD6 2SZ.

## 23. RELATED PARTY TRANSACTIONS

The company is exempt under the terms of FRS 8 "Related party transactions" from disclosing related party transactions with entities that are part of the Kelda Holdings Ltd group.

During the year there were no transactions or outstanding balances with other related parties.

## 24. SEGMENTAL INFORMATION

For statutory purposes, the directors consider there to be only one business segment, being the provision of water and sewerage services.

## 25. SHARE-BASED PAYMENTS

### Share options

In prior years the ultimate parent company, Kelda Group Ltd (formerly plc), operated a savings related share option scheme under which options were granted to employees and provided for at an exercise price equal to the daily average market price on the date of grant less 20%. The options vested if the employee remained in service for the full duration of the options scheme (either 3 or 5 years).

In 2008, the scheme was closed following the acquisition of Kelda Group plc by Saltaire Water Ltd. Certain schemes have been allowed to continue until the planned maturity of three or five years from grant date with members choosing whether to continue to contribute.

	<b>Options</b>	<b>2012 Weighted average exercise price £</b>	<b>Options</b>	<b>2011 Weighted average exercise price £</b>
Outstanding at the beginning of the year	99,161	6.99	259,192	6.20
Lapsed during the year	(1,087)	6.64	(11,057)	6.62
Exercised during the year	(92,030)	6.95	(148,974)	5.72
Outstanding at the end of the year	<b>6,044</b>	<b>7.41</b>	99,161	6.99
Of which exercisable at the end of the year	<b>6,044</b>	<b>7.41</b>	28,347	5.88

The weighted average share price at the date of exercise for share options exercised during the year was £10.90 (2011: £10.90).

## Notes to the Financial Statements

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The options outstanding at 31 March 2012 had a weighted average exercise price of £7.41 and a weighted average remaining contractual life of less than one year

The fair value of the share options granted is estimated as at the date of grant using the Black Scholes statistical model. No shares were granted since 2007. The inputs to the Black Scholes model for 2007 were as follows:

	<b>2007</b>
Share price at date of grant	926p
Exercise price	741p
Expected volatility	25%
Expected life	3 and 5 years
Risk free rate	5.08%
Expected dividends	31p

Expected volatility was determined by calculating the historical volatility of the Group's share price over the last 6 years of its trade.

# **Directors' Responsibilities**

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## **Statement of directors' responsibilities**

The directors are responsible for preparing the Directors' Report and the financial statements in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and accounting estimates that are reasonable and prudent,
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

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

# ***Independent Auditors' Report***

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## **INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF YORKSHIRE WATER SERVICES LTD**

We have audited the financial statements of Yorkshire Water Services Ltd for the year ended 31 March 2012 which comprise the Profit and Loss Account, Statement of Total Recognised Gains and Losses, the Balance Sheet and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

### **Respective responsibilities of directors and auditors**

As explained more fully in the Directors' Responsibilities Statement set out on page 54 the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, 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.

### **Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### **Opinion on financial statements**

In our opinion the financial statements

- give a true and fair view of the state of the company's affairs as at 31 March 2012 and of its profit for the year then ended,
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, and
- have been prepared in accordance with the requirements of the Companies Act 2006.

### **Opinion on other matter prescribed by the Companies Act 2006**

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

# ***Independent Auditors' Report***

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## **Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us, or
- the financial statements are not in agreement with the accounting records and returns, or
- certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit



Richard Bunter (Senior Statutory Auditor)  
For and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Leeds  
27 June 2012

# Regulatory Accounting Information 2012

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### *Explanatory note*

Pages 57 to 85 include the regulatory accounting information which the company is required to publish under the company's Instrument of Appointment as a water and sewerage undertaker. The information has been prepared in accordance with the requirements of Regulatory Accounting Guidelines issued by the Water Services Regulation Authority (Ofwat).

# Historical Cost Profit & Loss Account

for the year ended 31 March 2012

	2012			2011		
	Appointed £m	Non- appointed £m	Total £m	Appointed £m	Non- appointed £m	Total £m
<b>Turnover</b>	885.0	8.6	893.6	859.7	7.7	867.4
Operating costs	(425.9)	(7.2)	(433.1)	(394.7)	(6.5)	(401.2)
Historical cost depreciation	(161.1)	-	(161.1)	(157.6)	-	(157.6)
Operating income	1.5	-	1.5	2.6	-	2.6
<b>Operating profit</b>	299.5	1.4	300.9	310.0	1.2	311.2
Other income	2.4	-	2.4	2.4	-	2.4
Net interest	(234.8)	-	(234.8)	(271.2)	-	(271.2)
<b>Profit on ordinary activities before taxation</b>	67.1	1.4	68.5	41.2	1.2	42.4
Taxation - current	19.3	(0.4)	18.9	16.4	(0.4)	16.0
Taxation - deferred	(9.7)	-	(9.7)	59.2	-	59.2
<b>Profit on ordinary activities after taxation</b>	76.7	1.0	77.7	116.8	0.8	117.6
Dividends	(63.4)	-	(63.4)	(46.9)	-	(46.9)
<b>Retained profit for the year</b>	13.3	1.0	14.3	69.9	0.8	70.7

The accounting policies set out on page 31 of the statutory financial statements of Yorkshire Water Services Ltd (Yorkshire Water) apply to the historical cost regulatory accounting information, with the exception of the accounting for infrastructure assets and the investment in The York Waterworks Ltd (Note 1 on page 64)

There is no material difference between the profit before tax and the profit for the year stated above and their historical cost equivalents. There is no material difference between the historical cost depreciation charge and the actual depreciation charge for the year as a result of the re-valuation of certain tangible fixed assets

# Historical Cost Balance Sheet

As at 31 March 2012

	2012			2011		
	Appointed £m	Non- appointed £m	Total £m	Appointed £m	Non- appointed £m	Total £m
<b>Fixed assets</b>						
Tangible assets	6,134.1	3.7	6,137.8	4,372.0	4.0	4,376.0
Investment - loan to a group company	1,289.4	-	1,289.4	928.8	-	928.8
Investment - other	6.7	-	6.7	7.6	-	7.6
	<b>7,430.2</b>	<b>3.7</b>	<b>7,433.9</b>	<b>5,308.4</b>	<b>4.0</b>	<b>5,312.4</b>
<b>Current assets</b>						
Stocks	1.2	-	1.2	1.2	-	1.2
Debtors	168.0	2.0	170.0	159.0	1.1	160.1
Corporation tax receivable	17.1	-	17.1	-	-	-
Cash	3.0	5.3	8.3	40.4	-	40.4
Short term deposits	-	-	-	5.0	-	5.0
	<b>189.3</b>	<b>7.3</b>	<b>196.6</b>	<b>205.6</b>	<b>1.1</b>	<b>206.7</b>
<b>Creditors: amounts falling due within one year</b>						
Infrastructure renewals accrual	6.1	-	6.1	(18.2)	-	(18.2)
Creditors	(316.1)	(0.3)	(316.4)	(324.9)	(0.2)	(325.1)
Borrowings	(55.7)	-	(55.7)	(68.2)	4.9	(63.3)
Corporation tax payable	-	(0.4)	(0.4)	(5.4)	(0.4)	(5.8)
	<b>(365.7)</b>	<b>(0.7)</b>	<b>(366.4)</b>	<b>(416.7)</b>	<b>4.3</b>	<b>(412.4)</b>
<b>Net current assets/(liabilities)</b>	<b>(176.4)</b>	<b>6.6</b>	<b>(169.8)</b>	<b>(211.1)</b>	<b>5.4</b>	<b>(205.7)</b>
<b>Total assets less current liabilities</b>	<b>7,253.8</b>	<b>10.3</b>	<b>7,264.1</b>	<b>5,097.3</b>	<b>9.4</b>	<b>5,106.7</b>
<b>Creditors' amounts falling due after more than 1 year</b>						
Borrowings	(4,120.7)	-	(4,120.7)	(3,578.6)	-	(3,578.6)
Other creditors	(57.5)	-	(57.5)	(63.3)	-	(63.3)
	<b>(4,178.2)</b>	<b>-</b>	<b>(4,178.2)</b>	<b>(3,641.9)</b>	<b>-</b>	<b>(3,641.9)</b>
<b>Provisions for liabilities and charges</b>						
Deferred tax provision	(171.7)	-	(171.7)	(162.0)	-	(162.0)
Deferred income - grants and contributions	(67.6)	(3.3)	(70.9)	(70.5)	(3.5)	(74.0)
Other provisions	(328.1)	-	(328.1)	(335.8)	-	(335.8)
	<b>2,508.2</b>	<b>7.0</b>	<b>2,515.2</b>	<b>887.1</b>	<b>5.9</b>	<b>893.0</b>
<b>Capital and reserves</b>						
Called up share capital	10.0	-	10.0	10.0	-	10.0
Profit and loss reserve	835.7	7.0	842.7	822.0	5.9	827.9
Other reserves - share based payments	3.5	-	3.5	3.5	-	3.5
Other reserves - revaluation surplus	1,659.0	-	1,659.0	51.6	-	51.6
	<b>2,508.2</b>	<b>7.0</b>	<b>2,515.2</b>	<b>887.1</b>	<b>5.9</b>	<b>893.0</b>

The regulatory financial statements on pages 58 to 83 were approved by the board of directors on 27 June 2012 and signed on their behalf by

Richard Flint  
Chief Executive Officer



# **Current Cost Profit and Loss Account for the Appointed Business**

for the year ended 31 March 2012

	Note	2012 £m	2011 £m
<b>Turnover</b>	5	<b>885 0</b>	859 7
Current cost operating costs	6	<b>(641 0)</b>	(602 1)
Operating expense	5	<b>(7.0)</b>	(7 7)
Working capital adjustment	5	<b>2.4</b>	(4 9)
<b>Current cost operating profit</b>		<b>239.4</b>	245 0
Other income		<b>2 4</b>	2 4
Net interest		<b>(234 8)</b>	(271 2)
Financing adjustment		<b>24 8</b>	175 2
<b>Current cost profit on ordinary activities before taxation</b>		<b>31.8</b>	151 4
Taxation - current tax		<b>19.3</b>	16 4
- deferred tax		<b>(9.7)</b>	59 2
<b>Current cost profit on ordinary activities after taxation</b>		<b>41 4</b>	227 0
Dividends		<b>(63.4)</b>	(46 9)
<b>Current cost (loss)/profit</b>		<b>(22.0)</b>	180 1

# Current Cost Balance Sheet

for the year ended 31 March 2012

	Note	2012 £m	2011 £m
<b>Fixed assets</b>			
Tangible assets	8	47,850.9	36,300.6
Third party contributions since 1989/90		(10,620.0)	(454.9)
<b>Other operating assets and liabilities</b>			
Working capital	9	(73.2)	(68.9)
Cash		3.0	40.4
Short term deposits		-	5.0
Infrastructure renewals accrual		6.1	(18.2)
<b>Net operating assets</b>		<u>37,166.8</u>	<u>35,804.0</u>
<b>Non operating assets and liabilities</b>			
Borrowings		(55.7)	(68.2)
Non-trade debtors		34.2	19.5
Non-trade creditors due within one year		(107.8)	(115.3)
Investment - loan to Group company		1,289.4	928.8
Investment - other		6.7	7.6
Corporation tax payable		17.1	(5.4)
<b>Total non operating assets and liabilities</b>		<u>1,183.9</u>	<u>767.0</u>
<b>Creditors: amounts falling due after more than one year</b>			
Borrowings		(4,120.7)	(3,578.6)
Other creditors		(57.5)	(63.3)
<b>Total creditors falling due after more than one year</b>		<u>(4,178.2)</u>	<u>(3,641.9)</u>
<b>Provisions for liabilities and charges</b>			
Deferred tax provision		(171.7)	(162.0)
Other provisions		(328.1)	(335.8)
		<u>(499.8)</u>	<u>(497.8)</u>
<b>Net assets</b>		<u>33,672.7</u>	<u>32,431.3</u>
<b>Capital and reserves</b>			
Called up share capital		10.0	10.0
Profit and loss reserve		403.5	425.2
Other reserves		3.5	3.5
Current cost reserve	10	33,255.7	31,992.6
		<u>33,672.7</u>	<u>32,431.3</u>

# Current Cost Cash Flow Statement

for the year ended 31 March 2012

	Note	2012			2011		
		Appointed	Non- appointed	Total	Appointed	Non- appointed	Total
		£m	£m	£m	£m	£m	£m
<b>Net cash flow from operating activities</b>	11	527.1	0.6	527.7	628.5	0.8	629.3
<b>Returns on investments and servicing of finance</b>							
Interest received		69.2	-	69.2	51.6	-	51.6
Interest paid		(203.5)	-	(203.5)	(182.2)	-	(182.2)
Interest in finance lease rentals		(17.6)	-	(17.6)	(20.4)	-	(20.4)
<b>Net cash flow from returns on investments and servicing of finance</b>		(151.9)	-	(151.9)	(151.0)	-	(151.0)
<b>Taxation</b>							
Tax paid		(2.9)	(0.3)	(3.2)	(11.1)	(0.6)	(11.7)
<b>Capital expenditure and financing of investment</b>							
Investment in subsidiary		-	-	-	-	-	-
Gross cost of purchase of fixed assets		(330.4)	0.1	(330.3)	(174.9)	(0.2)	(175.1)
Receipt of grants and contributions		11.7	-	11.7	7.6	-	7.6
Infrastructure renewals		(87.8)	-	(87.8)	(66.1)	-	(66.1)
Disposal of fixed assets		1.9	-	1.9	1.3	-	1.3
<b>Net cash outflow from investing activities</b>		(404.6)	0.1	(404.5)	(232.1)	(0.2)	(232.3)
<b>Equity dividends paid</b>		(63.4)	-	(63.4)	(46.9)	-	(46.9)
<b>Net cash inflow/(outflow) before financing</b>		(95.7)	0.4	(95.3)	187.4	-	187.4
<b>Financing</b>							
Capital element in finance lease rentals		(70.1)	-	(70.1)	(15.7)	-	(15.7)
New bank loans		577.4	4.9	582.3	721.4	-	721.4
Repayment of bank loans		(454.0)	-	(454.0)	(908.7)	-	(908.7)
<b>Net cash (outflow)/inflow from financing</b>		53.3	4.9	58.2	(203.0)	-	(203.0)
<b>(Decrease)/increase in cash</b>		(42.4)	5.3	(37.1)	(15.6)	-	(15.6)

# Notes to the Regulatory Accounting Information

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## 1. ACCOUNTING POLICIES - CURRENT COST INFORMATION

The current cost information has been prepared for the Appointed Business of Yorkshire Water Services Ltd (Yorkshire Water) in accordance with guidance issued by Ofwat for modified real terms financial statements suitable for regulation in the water industry. Profitability is measured on the basis of real financial capital maintenance in the context of assets which are valued at their modern equivalent asset value to the business.

The accounting policies used are the same as those adopted in the statutory accounts, except as set out below.

### Infrastructure assets

As noted on page 58, FRS 12 has not been implemented in the regulatory accounts and the difference between planned and actual expenditure on infrastructure renewals is shown separately in the current cost balance sheet.

### Tangible fixed assets

Assets in operational use are valued at the replacement cost of their operating capability. To the extent that the regulatory regime does not allow such assets to earn a return high enough to justify that value, this represents a modification of the value to the business principle. Also, no provision is made for the possible funding of future replacements of assets by contributions from third parties and, to the extent that some of those assets would on replacement be so funded, replacement cost again differs from value to the business. Redundant assets are valued at their recoverable amount.

The ownership of, and responsibility for, certain private sewers in Yorkshire Water's region were transferred to the company on 1 October 2011. To meet the requirements of RAG1 04 these assets have been included in fixed asset additions at their modern equivalent asset value (MEA) with a corresponding credit to third party contributions. The value included is based on data from a report completed by UK Water Industry Research (UKWIR) in 2007 which estimated the length of private sewers, and the number of chambers and other associated assets, to be adopted in each region in England and Wales as part of the private sewers transfer. UKWIR used average lengths of each type of drain or sewer, with different lengths applied depending on the age and type of property. To calculate the MEA cost at October 2011, the transferred sewers were valued at current construction unit costs for similar replacement activities on public sewers.

The modern equivalent asset values (MEA) arising from the last Periodic Review (PR09) are incorporated in the 2011/12 Regulatory Accounting Information.

The revaluation of historical cost fixed assets does not affect the current cost accounting information.

### - Land and buildings

Non-specialised operational properties are valued on the basis of open market value for existing use and have been expressed in real terms by indexing using the Retail Price Index (RPI).

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

# Notes to the Regulatory Accounting Information

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- **Infrastructure assets**

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

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

- **Other fixed assets**

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

- **Surplus land**

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

### **Grants and other third party contributions**

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

### **Real financial capital maintenance adjustments**

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

- **Working capital adjustment**

This is calculated by applying the change in the RPI over the year to the opening total of trade debtors and stock less trade creditors and the provision for liabilities and charges.

- **Financing adjustment**

This is calculated by applying the change in the RPI over the year to the opening balance of net finance, which comprises all monetary assets and liabilities in the balance sheet apart from those included in working capital.

### **Investment in York WaterWorks**

The intangible assets accounting policy on page 33 and note 8 of the statutory financial statements of Yorkshire Water outline the treatment of the transfer of the trade and net assets of The York WaterWorks Ltd (YWW) to Yorkshire Water in 2000.

### **Revenue recognition**

There is no difference between the turnover recognised in the statutory and regulatory accounts or in the policy for revenue recognition.

No turnover is recognised for unoccupied properties and no bills are raised. If a bill has been issued, and the company subsequently become aware that the property is unoccupied, the bill and relevant turnover is cancelled. Generally a property is classed as void if it is unoccupied and unfurnished.

# **Notes to the Regulatory Accounting Information**

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Turnover is only recognised when the occupier's name is known. This policy applies to both existing and new properties. All billing is then subsequently classed as turnover.

## **2. APPOINTED AND NON-APPOINTED BUSINESS**

The historical cost accounting information shows separate figures for Appointed and Non-Appointed Business.

The Appointed Business is defined to be the regulated activities of the Appointee, i.e. those necessary to fulfil the functions and duties of a water and sewerage undertaker. The Non-Appointed Business encompasses those activities for which Yorkshire Water is not a monopoly supplier or the activity involves the optional use of an asset owned by the Appointed Business.

## **3. DISCLOSURE OF TRANSACTIONS WITH ASSOCIATES**

### **Allocation of costs**

All direct costs are allocated immediately to the activity to which they relate. Indirect costs and overheads are apportioned on an appropriate basis to reflect the incidence of such costs. Indirect costs include administrative expenses and the provision of common services.

Direct costs attributable to the provision of services other than the Appointed Business are separately allocated and identified as 'Non-Appointed'. Indirect costs, relating to non-appointed activities, are recovered as a fixed percentage of direct costs based upon the analysis of operating costs.

### **Borrowings or sums lent**

#### ***Kelda Holdco Ltd***

A long term loan was advanced by Yorkshire Water to Kelda Holdco Ltd during 2008/09 to reflect the market value of certain index linked swaps novated from Kelda Holdco Ltd to Yorkshire Water at that point in time. Balances at 1 April 2011 and 31 March 2012 were £288.6m and £280.4m respectively. Interest is payable at current market rates.

In addition Yorkshire Water have made further loan advances to Kelda Holdco Ltd to enable the refinancing of debt in Kelda Holdco Ltd. The balance of these loans at 31 March 2012 was £1,009.0m (2011 £640.2m). Interest is payable on these loans at current market rates.

#### ***Yorkshire Water Services Finance Ltd***

On 17 April 2000, £150m was lent at a fixed rate of 6.625% repayable in 2031, and on 16 November 2001 a further £90m was lent at 6.625% repayable in 2031. On 3 July 2008 Yorkshire Water Services Finance Ltd (YWSF), a subsidiary of the company, became principal debtor under the bonds which are unconditionally and irrevocably guaranteed by Yorkshire Water. As a result, the loans from Kelda Group Ltd were transferred to YWSF.

On 24 July 2009, Yorkshire Water implemented a whole business securitisation (WBS). Post the implementation of the WBS, Yorkshire Water Services Finance Ltd will remain the issuer in respect of the existing bonds on-lent to Yorkshire Water, but will not issue further bonds in the future.

## Notes to the Regulatory Accounting Information

The table below sets out the amounts outstanding on loans from YWSF

Issue Date	Nominal £m	Coupon	Maturity	Liability @ 31/03/2012 £m
<b>Fixed Rate</b>				
07/04/2000	240.0	6.625%	2031	240.5
21/02/2003	200.0	5.375%	2023	197.1
29/05/2007	200.0	5.500%	2037	194.9
29/05/2007	150.0	5.500%	2027	148.8
<b>Index Linked</b>				
21/02/2003	100.0	3.048%	2033	132.3
27/11/2006	125.0	1.462%	2051	148.9
27/11/2006	125.0	1.460%	2056	148.8
01/06/2007	85.0	1.75756%	2054	98.5
11/06/2007	100.0	1.7085%	2058	115.7
11/06/2007	65.0	1.8225%	2050	75.2
<b>Total loan with YWSFL</b>	<b>1,390.0</b>			<b>1,500.7</b>

### Yorkshire Water Services Odsal Finance Ltd (YWSOFL)

As stated above, during the year ended 31 March 2010 Yorkshire Water implemented a WBS. Part of this process involved certain bonds initially issued by YWSFL being exchanged for new bonds issued by a fellow subsidiary YWSOFL. These exchange bonds were issued on different terms to the existing bonds.

In order to fund the change in coupon payable and differences in par values post the bond exchange, Yorkshire Water entered into a series of loans with YWSOFL:

- Deep discounting loans structured such that their redemption value will be discharged by the difference between the par value paid by YWSFL in respect of the old bonds and the par value paid by the YWSOFL in respect of the new bonds, and
- Amortising loans structured such that the regular payments of principal and interest equate to the difference between the interest received from YWSFL on the old bonds and the amount payable by the YWSOFL on the new bonds.

The balances outstanding as at 31 March 2012, regarding these deep discounting and amortising loans, are shown in the table below:

	£m
2010 to 2023 Exchange Bonds	30.2
2023 to 2023 Exchange Bonds	5.5
2027 to 2027 Exchange Bonds	5.3
2031 to 2031 Exchange Bonds	15.4
2033 to 2033 Exchange Bonds	10.5
<b>Total</b>	<b>66.9</b>

In addition to this balance there is a short term loan from YWSOFL of £241.0m which is due to be repaid in 2012/13.

### Yorkshire Water Services Bradford Finance Ltd (YWSBFL)

During April 2010 YWSBFL raised £635m of new debt, including £450m of class B debt, this was a combination of fixed rate and indexed linked debt as shown by the table below. The proceeds (net of costs and expenses where applicable) were on-

## Notes to the Regulatory Accounting Information

lent by YWSBFL to Yorkshire Water. In addition, during December 2011 and January 2012 YWSBFL raised a further £335m through the US bond market. The amounts outstanding as at 31 March 2012 are shown in the table below.

Issue Date	Nominal £m	Nominal \$m	Coupon	Maturity	Liability @ 31/03/2012 £m
<b>Fixed Rate</b>					
24/07/2009	275.0		6.000%	2019	273.0
24/07/2009	200.0		6.375%	2039	198.0
23/04/2010	100.0		6.375%	2039	108.2
23/04/2010	450.0		6.000%	2017	446.7
13/12/2011	18.9	30	3.180%	2018	18.8
05/01/2012	9.4	15	3.180%	2019	9.3
13/12/2011	72.3	115	3.770%	2021	71.9
05/01/2012	25.1	40	3.770%	2022	25.0
13/12/2011	94.3	150	3.870%	2023	93.8
05/01/2012	18.8	30	3.870%	2024	18.7
05/01/2012	47.2	75	5.070%	2022	46.9
<b>Index Linked</b>					
24/07/2009	175.0		2.718%	2039	196.9
23/04/2010	85.0		2.718%	2039	108.7
13/12/2011	50.0		2.160%	2041	49.8
<b>Total Loan with YWSBFL</b>					<b>1,665.7</b>

No other material sums were lent to or borrowed from other associated companies.

### Dividends paid to associated undertakings

Amounts paid to the parent company and the underlying dividend policy, are disclosed in the Directors' Report on page 20 of the statutory financial statements of Yorkshire Water.

### Guarantees/securities

Until August 2008, the bankers for the Kelda Group Ltd and subsidiaries current accounts provided pooling arrangements for all accounts whereby debit and credit balances were pooled with interest charged on the net group balance. Arrangements changed on 11 August 2008 and now Yorkshire Water has pooling arrangements only with YWSF and Kelda Group Ltd. Debit and credit balances are pooled with interest charged on the net group balance.

This facility is subject to provision of cross guarantees by each company within each pooling arrangement, guaranteeing each of the other companies' current account liabilities with the bank. This is provided that the aggregate of the cleared debit balances, less the aggregate of the cleared credit balances, i.e. the net amount must not exceed £10m. In addition, the aggregate of the cleared debit balances on the group accounts must not exceed £15m.

### Transfer of assets and liabilities

During the course of the year land and buildings were sold to group companies at market value. Total sale proceeds were £1.4m (2011: £1.3m).

# Notes to the Regulatory Accounting Information

## Supply of service

Details of services supplied to the Appointee by associates during the year are disclosed below where these exceed a materiality level of £1m (in line with RAG 5 04 requirements) No services of a material value were provided by the Appointee to associates

Service	Associate Company	Turnover of Associate £m	Terms of Supply	Value £m
Corporate charges	Kelda Group Ltd	6.1	Cost allocation	3.0
Customer Services	Loop Customer Management	24.1	Cost allocation	22.6

The Directors declare that, to the best of their knowledge, all appropriate transactions with associated companies have been disclosed

## 4. LINK BETWEEN DIRECTORS' PAY AND STANDARDS OF PERFORMANCE

The remuneration policy of the company, which is set within the context of the Group's remuneration policy, is to enable directors to receive remuneration which is competitive in the market and which encourages and enables upper quartile performance, taking into account individual performance, responsibilities and experience. Accordingly, the remuneration of the directors of the company is structured into three elements: base salary, annual incentive and long term incentive plan (LTIP).

### Salary

The base salary is a fixed figure and does not vary in relation to business or individual performance.

### Annual incentive plan

Under the annual incentive plan, each director has the opportunity to earn an annual incentive award based on a percentage of their salary. Awards are entirely performance related as described below.

Early in the 2008/09 financial year, the company implemented a new annual incentive plan based on company performance and personal contribution. Under this plan the annual incentive award is calculated as a percentage of basic salary as at 31 March as follows:

- 50% of the total maximum annual bonus payable was dependent upon delivery of agreed personal / individual objectives set at the start of the financial year.
- 50% of the total maximum annual bonus payable was dependent upon delivery of agreed corporate objectives which supported the company's strategic objectives. The same corporate objectives were shared by all directors. These are set out in the table below with the percentage payable.

## Notes to the Regulatory Accounting Information

Strategic Theme	Measure	% of corporate bonus
Most efficient, lowest cost	1 EBITDA 2 Capital Programme Allowance 3 Capital efficiency	15 (20% max)
Best customer experience	1 SIM qualitative 2 SIM quantitative 3 Reservoir stocks	6 (7.5% max)
100% compliance	1 DWI incidents 2 Leakage rolling average 3 Mean zonal compliance 4 Category 1 & 2 pollution incidents 5 No of WWTW's failing numeric consent	2.5 (7.5% max)
World class asset management	1 Critical Raw Water Pumping asset availability 2 Engineering Reliability asset availability 3 Capital programme index 4 Serviceability (4 asset groups)	2.5 (5% max)
Best People and Technology	1 People tracker - leadership 2 People tracker – alignment with vision 3 Union relationship score 4 IT – calls resolved within service level	4 (5% max)
Zero accidents (Kelda)	1 Lost time injury incident rate (LTIIR) 2 RIDDOR incident rate (RIR) 3 Near miss reports incident rate	2.5 (5% max)

Using these principles the awards for 2011/12 were determined by the Group remuneration committee (the Committee) and taking account of performance against these measures and personal/individual objectives, total awards were made by the Committee in accordance with the table below

	<b>Max. Bonus %</b>	<b>Bonus for 2011/12 %</b>	<b>Bonus for 2011/12 £</b>
Graham Dixon	70	50	83,254
Alan Harrison	70	52	107,120
Charlie Haysom	70	56	58,430
Pamela Rogerson	70	55	56,650

These payments were approved by the Committee on 28 March 2012 and were paid in June 2012

Richard Flint and Liz Barber were executive directors of Kelda Holdco Ltd during 2011/12 and their emoluments are shown in the accounts of that company. Helen Phillips joined the company on 1 March 2012 and no bonus was paid to her for 2011/12

### Long term incentive plan (LTIP)

The first conditional award under a revised Kelda Group LTIP, which included a link to the company's performance against Ofwat comparative efficiency measures, was made on 27 September 2007. Vesting of shares awarded under this Plan was

## Notes to the Regulatory Accounting Information

triggered by the acquisition of Kelda Group plc (now Ltd) by Saltaire Water Ltd in February 2008 and the Plan was then closed. Details of the vesting of these shares were given in the regulatory accounts for 2007/08.

Following the acquisition, the Committee conducted a review of the Group's executive incentive arrangements for executive directors. A revised cash LTIP was developed and established during the year under which the first conditional awards were granted in November 2008.

The Plan provides for a cash award based on a percentage of salary. The awards as originally granted in November 2008 were subject to two performance conditions which were to be measured over a three year period.

70% of the award is subject to the valuation of the investment made by the investors in Kelda at the end of the relevant three year performance period as determined by an independent valuer.

The remaining 30% of the award was based on the company's Operating Efficiency and Capital Maintenance Efficiency performance relative to the other nine water and sewerage companies based on Ofwat published data. Ofwat's report on 'Water and Sewerage Service Unit Costs and Relative Efficiency' (the Ofwat Report) was to be used to produce an average ranking for the company for the financial year for the four operating and capital efficiency measures.

The Ofwat Report used to contain Ofwat's assessment of each water company's operating and capital maintenance efficiency for water and, in respect of the water and sewerage companies, the same efficiency measures in respect of sewerage. These assessments are based primarily on Ofwat's econometric models and unit cost comparisons.

Based on these assessments, the Ofwat Report used to contain a ranking amongst the companies based on their relative performance for each of the four measures (Operating Efficiency - Water, Capital Maintenance Efficiency - Water, Operating Efficiency - Sewerage, Capital Maintenance Efficiency - Sewerage). For the purposes of this performance condition, the water only companies are excluded from the analysis as they do not feature in the sewerage measures, leaving the ten water and sewerage companies as the comparator group.

This process of producing an average ranking would be repeated for the next two years in the performance period to establish an average for the three years. On the basis of this overall average, a ranking is established (with the company having the lowest overall average being ranked 1<sup>st</sup> and so on).

Vesting of 30% of the award was to be in accordance with the table below,

<b>OFWAT Ranking:</b>	<b>Percentage of Award Vesting (for 30% of the Award):</b>
1	100%
2	100%
3 - 5	Pro rata between 0% and 100%
6 and below	0%

# Notes to the Regulatory Accounting Information

However, since the awards were granted Ofwat have ceased to report on Capital Maintenance Efficiency - Water and Capital Maintenance Efficiency - Sewerage, and therefore these measures have since become obsolete

As a result the Committee met in May 2009 and varied the performance condition for the 2008 awards to replace the Capital Maintenance measures with a performance condition that measures performance against the phased capital efficiency target for the relevant award year and calculates a cumulative efficiency performance over a three year period (the "Capital Efficiency Measure")

Subsequently Ofwat also ceased to report on Operating Efficiency – Water and Operating Efficiency – Sewerage although reports are available for the first two years of the term for the 2008 awards. As a result the Committee met on 2 March 2011 and varied the performance condition for the 2008 awards for the third year of the term to replace the Operating Efficiency measures with a performance condition that measures financial performance against the company's EBITDA target for that third year

As a result of these changes vesting of 30% of the 2008 award was to be in accordance with the tables below,

<b>OFWAT Ranking:</b>	<b>Percentage of Award Vesting (for 10% of the Award):</b>
1	100%
2	100%
3 - 5	Pro rata between 0% and 100%
6 and below	0%

<b>Capital Efficiency Measure</b>	<b>Percentage of Award Vesting (for 15% of the Award):</b>
100%	100%
At least 75% but below 100%	Pro rata between 0% and 100%
Below 75%	0%

<b>EBITDA Measure</b>	<b>Percentage of Award Vesting (for 5% of the Award):</b>
100%	100%
At least 90% but below 100%	Pro rata between 0% and 100%
Below 90%	0%

No awards will vest under the Plan unless, in the opinion of the Committee, the underlying financial performance of the company has been satisfactory over the performance period, taking into account all relevant circumstances. The Committee has the power to scale back vesting to any extent considered appropriate in light of the company's financial performance

## Notes to the Regulatory Accounting Information

At its meeting in May 2009 the Committee granted a second set of conditional awards. At its meeting on 2 March 2011 the Committee granted a third set of conditional awards based on the above amended performance conditions and amended the 2009 awards to reflect the changes to the Ofwat Report.

Accordingly vesting of 30% of the 2009 award was to be in accordance with the tables below,

<b>OFWAT Ranking:</b>	<b>Percentage of Award Vesting (for 5% of the Award):</b>
1	100%
2	100%
3 - 5	Pro rata between 0% and 100%
6 and below	0%

<b>Capital Efficiency Measure</b>	<b>Percentage of Award Vesting (for 15% of the Award):</b>
100%	100%
At least 75% but below 100%	Pro rata between 0% and 100%
Below 75%	0%

<b>EBITDA Measure</b>	<b>Percentage of Award Vesting (for 10% of the Award):</b>
100%	100%
At least 90% but below 100%	Pro rata between 0% and 100%
Below 90%	0%

Vesting of 30% of the 2010 award (granted on 2 March 2011) is to be in accordance with the tables below,

<b>Capital Efficiency Measure</b>	<b>Percentage of Award Vesting (for 15% of the Award):</b>
100%	100%
At least 75% but below 100%	Pro rata between 0% and 100%
Below 75%	0%

## Notes to the Regulatory Accounting Information

<b>EBITDA Measure</b>	<b>Percentage of Award Vesting (for 15% of the Award):</b>
100%	100%
At least 90% but below 100%	Pro rata between 0% and 100%
Below 90%	0%

The Committee conducted a further review of the Group's LTIP arrangements and a revised set of performance conditions were developed during 2011/12. At its meeting on 25 May 2011 the Committee adopted a revised set of conditions and at its meetings on 25 May 2011 and 26 April 2012 the Committee granted sets of conditional awards based on the new performance conditions which are summarised below,

### *Step 1 - OFWAT Performance Condition*

The Ofwat Performance Condition is met only if the Ofwat Ranking of the company is in the top half of the Ofwat Comparator Group (i.e. performance relative to the other nine water and sewerage companies based on Ofwat published data) for the Ofwat Service Incentive Mechanism (SIM) Measure as ranked in the Ofwat Report (or in the event of such ranking not being published by OFWAT as ranked by such other comparative assessment as adopted by the Committee for performance in the financial year 2013/14 for the 2011 award and 2014/15 for the 2012 award) and the award shall vest in accordance with the steps 2 – 4 below

If the Ofwat Ranking of the company is in the bottom half of the Ofwat Comparator Group for the Ofwat SIM Measure as ranked in the Ofwat Report (or in the event of such ranking not being published by Ofwat as ranked by such other comparative assessment as adopted by the Committee for performance in the financial year 2013/14 for the 2011 award and 2014/15 for the 2012 award) then the Ofwat Performance Condition shall not be met and the award shall not vest

### *Step 2 - Cashflow Performance Condition*

Following the end of the three year performance period, the committee is to determine the Cashflow Measure. The Cashflow Performance Condition is that, subject to the Serviceability Performance Condition set out in step 3 below, a percentage for vesting of the award shall be determined in accordance with the following table

<b>Cashflow Measure</b>	<b>Percentage Determined</b>
Targeted Cashflow is at least 120%	100%
Targeted Cashflow is at least 100% but below 120%	Pro rata between 70% and 100%
Targeted Cashflow is at least 90% but below 100%	Pro rata between 1% and 70%
Targeted Cashflow is less than 90%	0%

### *Step 3 - Serviceability Performance Condition*

The Serviceability Performance Condition is that, subject to the SIM Bonus set out in step 4 below, 25% of the percentage determined under Step 2 shall vest in respect of the awards for each Ofwat serviceability measure as assessed in the Ofwat Report

## Notes to the Regulatory Accounting Information

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(or where replaced by such regulatory self reporting procedures that are compliant with Ofwat guidance as assessed by those regulatory self reporting procedures for performance in the financial year 2013/14 for the 2011 award and 2014/15 for the 2012 award) as "stable" or "improving"

### Step 4 – SIM Bonus

In the event that the Ofwat ranking of the company is 1<sup>st</sup> or 2<sup>nd</sup> amongst the Ofwat Comparator Group for the Ofwat SIM Measure as ranked in the Ofwat Report (or in the event of such ranking not being published by Ofwat as ranked by such other comparative assessment as adopted by the Committee for performance in the financial year 2013/14 for the 2011 award and 2014/15 for the 2012 award) then a further 10% will be added to the amount to vest in respect of the award, i.e. the amount to vest would be 110% of the value derived after step 3

In the event that the Ofwat ranking of the company is 3<sup>rd</sup> or lower amongst the Ofwat Comparator Group for the Ofwat SIM Measure as ranked in the Ofwat Report (or in the event of such ranking not being published by Ofwat as ranked by such other comparative assessment as adopted by the Committee for performance in the financial year 2013/14 for the 2011 award and 2014/15 for the 2012 award) then no SIM bonus will be paid and the amount to vest would be as derived after step 3

Details of the vesting of the 2008 awards were given in the regulatory accounts for 2010/11

At a meeting on 26 April 2012 the Committee determined an overall level of vesting of the 2009 awards at 40%. This resulted in payments to the directors in accordance with the table below and were paid in June 2012 (Note Neither Alan Harrison nor Pamela Rogerson were participants in the 2009 LTIP scheme),

	<b>Vesting %</b>	<b>Vesting £</b>
Graham Dixon	40	90,000
Charlie Haysom	40	21,618
Mark Penny	40	51,666

The emoluments for Kevin Whiteman, Richard Flint and Liz Barber are disclosed in the Kelda Holdco Ltd accounts

# Notes to the Regulatory Accounting Information

## 5. ANALYSIS OF TURNOVER & OPERATING INCOME FOR THE APPOINTED BUSINESS for the year ended 31 March 2012

	2012			2011		
	Water services £m	Sewerage services £m	Total appointed business £m	Water services £m	Sewerage services £m	Total appointed business £m
<b>Turnover</b>						
Unmeasured	207.5	242.8	450.3	199.4	238.9	438.3
Measured	179.8	185.5	365.3	172.1	179.4	351.5
Trade effluent	-	8.3	8.3	0.0	7.6	7.6
Large user and special agreement	23.4	27.7	51.1	24.5	29.2	53.7
Rechargeable works	7.7	-	7.7	6.2	-	6.2
Bulk supplies/inter company	0.1	-	0.1	0.1	-	0.1
Other sources	1.0	1.2	2.2	0.4	1.9	2.3
<b>Total turnover</b>	<b>419.5</b>	<b>465.5</b>	<b>885.0</b>	<b>402.7</b>	<b>457.0</b>	<b>859.7</b>
<b>Operating (loss)/income</b>						
Current cost profit on fixed assets net of expenses	(7.0)	-	(7.0)	0.4	(8.1)	(7.7)
<b>Total operating (loss)/income</b>	<b>(7.0)</b>	<b>-</b>	<b>(7.0)</b>	<b>0.4</b>	<b>(8.1)</b>	<b>(7.7)</b>
<b>Working capital adjustment</b>	<b>(2.5)</b>	<b>4.9</b>	<b>2.4</b>	<b>(2.4)</b>	<b>(2.5)</b>	<b>(4.9)</b>

## 6. ANALYSIS OF OPERATING COSTS AND ASSETS

All direct costs are allocated immediately to the activity to which they relate. Indirect costs and overheads are apportioned on an appropriate basis to reflect the incidence of such costs. Indirect costs include administrative expenses and the provision of common services.

# Notes to the Regulatory Accounting Information

## 6. ANALYSIS OF OPERATING COSTS AND ASSETS (continued)

for the year ended 31 March 2012

	Resources & treatment	Distribution	Water supply sub total	Sewerage	Sewage Treatment	Sludge Treatment & Disposal	Sewerage services sub total
	£m	£m	£m	£m	£m	£m	£m
<b>DIRECT COSTS</b>							
Employment costs	10.2	16.7	26.9	8.4	11.9	8.7	29.0
Power	11.2	13.1	24.3	2.0	16.3	4.8	23.1
Hired and contracted services	5.0	24.9	29.9	11.3	7.9	11.3	30.5
Associated companies	-	-	-	-	-	-	-
Materials and consumables	11.2	1.2	12.4	1.1	4.5	6.7	12.3
Service charges	5.8	-	5.8	1.2	3.4	0.2	4.8
Bulk supply imports	3.8	-	3.8	-	-	-	-
Other direct costs	2.4	5.2	7.6	1.3	1.2	0.4	2.9
<b>Total direct costs</b>	<b>49.6</b>	<b>61.1</b>	<b>110.7</b>	<b>25.3</b>	<b>45.2</b>	<b>32.1</b>	<b>102.6</b>
General and support expenditure	4.1	7.4	11.5	3.8	6.7	4.8	15.3
<b>Functional expenditure</b>	<b>53.7</b>	<b>68.5</b>	<b>122.2</b>	<b>29.1</b>	<b>51.9</b>	<b>36.9</b>	<b>117.9</b>
<b>BUSINESS ACTIVITIES</b>							
Customer services			13.2				15.0
Scientific services			4.5				2.5
Other business activities			1.9				2.1
<b>Business activities sub-total</b>			<b>19.6</b>				<b>19.6</b>
Local authority rates			32.5				17.0
Doubtful debts			7.2				8.1
Exceptional items			9.6				-
<b>Total opex less third party services</b>			<b>191.1</b>				<b>162.6</b>
Third party services - opex			9.9				0.1
<b>Total operating expenditure</b>			<b>201.0</b>				<b>162.7</b>
<b>CAPITAL MAINTENANCE</b>							
Infrastructure renewals charge	8.8	37.5	46.3	15.0	-	-	15.0
Current cost depreciation							
- service activities	30.3	45.7	76.0	23.7	87.9	28.8	140.4
- business activities			0.6				1.2
Amortisation of grants			(1.5)				(1.6)
Amortisation of intangible assets			0.9				-
<b>Total capital maintenance</b>			<b>122.3</b>				<b>155.0</b>
<b>TOTAL OPERATING COSTS</b>			<b>323.3</b>				<b>317.7</b>
							<b>641.0</b>
<b>CCA NET MEA VALUES</b>							
Service activities	4,248.1	14,865.4	19,113.5	27,224.2	1,232.1	252.7	28,709.0
Business activities	4.0	5.4	9.4	3.1	12.0	3.8	19.0
<b>TOTAL</b>			<b>19,122.9</b>				<b>28,728.0</b>

# Notes to the Regulatory Accounting Information

## 7. ANALYSIS OF OPERATING COSTS AND ASSETS

for the year ended 31 March 2011

	Resources & treatment	Distribution	Water supply sub total	Sewerage	Sewage Treatment	Sludge Treatment & Disposal	Sewerage services sub total
	£m	£m	£m	£m	£m	£m	£m
<b>DIRECT COSTS</b>							
Employment costs	10.1	11.2	21.3	5.2	14.6	8.4	28.2
Power	10.1	10.5	20.6	2.6	16.1	4.4	23.1
Hired and contracted services	2.8	21.4	24.2	-	-	-	-
Associated companies	-	-	-	7.9	5.2	9.4	22.5
Materials and consumables	9.7	0.5	10.2	-	-	-	-
Service charges	5.6	-	5.6	0.5	2.9	4.8	8.2
Bulk supply imports	3.8	-	3.8	1.1	3.5	0.2	4.8
Other direct costs	1.5	2.4	3.9	0.9	1.2	0.7	2.8
<b>Total direct costs</b>	<b>43.6</b>	<b>46.0</b>	<b>89.6</b>	<b>18.2</b>	<b>43.5</b>	<b>27.9</b>	<b>89.6</b>
General and support expenditure	7.1	10.0	17.1	3.4	10.1	6.1	19.6
<b>Functional expenditure</b>	<b>50.7</b>	<b>56.0</b>	<b>106.7</b>	<b>21.6</b>	<b>53.6</b>	<b>34.0</b>	<b>109.2</b>
<b>BUSINESS ACTIVITIES</b>							
Customer services			13.1				15.0
Scientific services			5.3				1.7
Other business activities			1.8				2.1
<b>Business activities sub-total</b>			<b>20.2</b>				<b>18.8</b>
Local authority rates			25.7				17.5
Doubtful debts			7.8				8.5
Exceptional items			4.6				1.3
<b>Total opex less third party services</b>			<b>165.0</b>				<b>155.3</b>
Third party services - opex			11.0				0.5
<b>Total operating expenditure</b>			<b>176.0</b>				<b>155.8</b>
<b>CAPITAL MAINTENANCE</b>							
Infrastructure renewals charge	13.7	29.9	43.6	18.3	-	-	18.3
Current cost depreciation							
- service activities	34.8	32.9	67.7	21.0	91.1	28.7	140.8
- business activities			0.9				0.9
Amortisation of grants			(1.4)				(1.4)
Amortisation of intangible assets			0.9				-
<b>Total capital maintenance</b>			<b>111.7</b>				<b>158.6</b>
<b>TOTAL OPERATING COSTS</b>			<b>287.7</b>				<b>314.4</b>
							602.1
<b>CCA NET MEA VALUES</b>							
Service activities	4,078.3	14,283.2	18,361.5	16,383.3	1,198.9	237.9	17,820.1
Business activities			10.6				6.4
<b>TOTAL</b>			<b>18,372.1</b>				<b>17,826.5</b>

# Notes to the Regulatory Accounting Information

## 8. CURRENT COST ANALYSIS OF FIXED ASSETS BY ASSET TYPE

as at 31 March 2012

	Specialised operational assets £m	Non- specialised operational properties £m	Infrastructure assets £m	Other tangible assets £m	Total £m
<b>WATER SERVICES</b>					
<b>Gross replacement cost</b>					
At 1 April 2011	2,647.7	101.1	17,130.1	197.3	20,076.2
RPI adjustment	95.2	3.7	616.7	7.1	722.7
Disposals	(40.6)	(0.6)	-	(1.9)	(43.1)
Additions	74.1	0.4	19.2	26.0	119.7
<b>At 31 March 2012</b>	<b>2,776.4</b>	<b>104.6</b>	<b>17,766.0</b>	<b>228.5</b>	<b>20,875.5</b>
<b>Depreciation</b>					
At 1 April 2011	1,549.0	5.2	-	99.5	1,653.7
RPI adjustment	55.7	0.2	-	3.6	59.5
Disposals	(34.0)	-	-	(0.6)	(34.6)
Charge for year	51.5	0.5	-	22.0	74.0
<b>At 31 March 2011</b>	<b>1,622.2</b>	<b>5.9</b>	<b>-</b>	<b>124.5</b>	<b>1,752.6</b>
<b>Net book amount at 31 March 2012</b>	<b>1,154.2</b>	<b>98.7</b>	<b>17,766.0</b>	<b>104.0</b>	<b>19,122.9</b>
Net book amount at 1 April 2011	1,098.6	95.9	17,130.1	97.8	18,422.4
<b>SEWERAGE SERVICES</b>					
<b>Gross replacement cost</b>					
At 1 April 2011	4,790.5	106.9	15,891.4	158.8	20,947.6
RPI adjustment	172.5	3.8	572.1	5.7	754.1
Disposals	(19.2)	(0.4)	-	(0.8)	(20.4)
Additions	139.8	0.4	10,186.6	24.0	10,350.8
<b>At 31 March 2012</b>	<b>5,083.6</b>	<b>110.7</b>	<b>26,650.1</b>	<b>187.7</b>	<b>32,032.1</b>
<b>Depreciation</b>					
At 1 April 2011	3,004.3	25.4	-	39.8	3,069.5
RPI adjustment	108.2	0.9	-	1.4	110.5
Disposals	(19.3)	-	-	(0.8)	(20.1)
Charge for year	116.9	0.6	-	26.7	144.2
<b>At 31 March 2012</b>	<b>3,210.1</b>	<b>26.9</b>	<b>-</b>	<b>67.1</b>	<b>3,304.1</b>
<b>Net book amount at 31 March 2012</b>	<b>1,873.5</b>	<b>83.8</b>	<b>26,650.1</b>	<b>120.6</b>	<b>28,728.0</b>
Net book amount at 1 April 2011	1,786.2	81.5	15,891.4	119.0	17,878.2

## Notes to the Regulatory Accounting Information

### 8. CURRENT COST ANALYSIS OF FIXED ASSETS BY ASSET TYPE (continued) as at 31 March 2012

	Specialised operational assets £m	Non- specialised operational properties £m	Infrastructure assets £m	Other tangible assets £m	Total £m
<b>TOTAL</b>					
<b>Gross replacement cost</b>					
At 1 April 2011	7,438.2	208.0	33,021.5	356.1	41,023.8
RPI adjustment	267.7	7.5	1,188.8	12.8	1,476.8
Disposals	(59.8)	(1.0)	-	(2.7)	(63.5)
Additions	213.9	0.8	10,205.8	50.0	10,470.5
<b>At 31 March 2012</b>	<b>7,860.0</b>	<b>215.3</b>	<b>44,416.1</b>	<b>416.2</b>	<b>52,907.6</b>
<b>Depreciation</b>					
At 1 April 2011	4,553.3	30.6	-	139.3	4,723.2
RPI adjustment	163.9	1.1	-	5.0	170.0
Disposals	(53.3)	-	-	(1.4)	(54.7)
Charge for year	168.4	1.1	-	48.7	218.2
<b>At 31 March 2012</b>	<b>4,832.3</b>	<b>32.8</b>	<b>-</b>	<b>191.6</b>	<b>5,056.7</b>
<b>Net book amount at 31 March 2012</b>	<b>3,027.7</b>	<b>182.5</b>	<b>44,416.1</b>	<b>224.6</b>	<b>47,850.9</b>
Net book amount at 1 April 2011	2,884.9	177.4	33,021.5	216.8	36,300.6

# Notes to the Regulatory Accounting Information

## 9. WORKING CAPITAL

	2012	2011
	£m	£m
Stocks	1.2	1.2
Trade debtors - measured household	26.9	25.6
- unmeasured household	32.8	31.6
- measured non-household	14.1	9.6
- unmeasured non-household	0.3	0.2
Other trade debtors	4.8	13.3
Measured income accrual	48.3	46.8
Prepayments and other debtors	6.5	12.5
Trade creditors	(53.4)	(47.3)
Deferred income - customer advance receipts	(48.6)	(50.4)
Short term capital creditors	(103.0)	(104.4)
Accruals and other creditors	(3.1)	(7.6)
<b>Total working capital</b>	<b><u>(73.2)</u></b>	<b><u>(68.9)</u></b>

## 10. MOVEMENT ON CURRENT COST RESERVE

	2012	2011
	£m	£m
<b>Balance at 1 April</b>	<b>31,992.6</b>	<b>30,343.4</b>
RPI adjustments		
Fixed assets	1,306.9	1,842.5
Working capital	(2.4)	4.9
Financing	(24.8)	(175.2)
Grants and third party contributions	(16.6)	(23.0)
<b>Balance at 31 March</b>	<b><u>33,255.7</u></b>	<b><u>31,992.6</u></b>

# Notes to the Regulatory Accounting Information

## 11. RECONCILIATION OF APPOINTED BUSINESS OPERATING PROFIT TO NET CASH FLOW FROM OPERATING ACTIVITIES

	2012	2011
	£m	£m
<b>Current cost operating profit</b>	<b>239.4</b>	<b>245.0</b>
Working capital adjustment	(2.4)	4.9
Movement in working capital	5.5	90.4
Receipts from other income	2.4	2.4
Current cost depreciation	216.1	208.4
Current cost profit on sale of fixed assets	7.0	7.7
Infrastructure renewals charge	61.4	61.9
Other movements	(2.3)	7.8
<b>Net cash flow from operating activities</b>	<b>527.1</b>	<b>628.5</b>

"Other" includes movements in debtors and creditors that are not classified as working capital in line with RAG 3.06 e.g. VAT debtor movements or creation of provisions. The movement in working capital as used in bank covenant calculations is adjusted from that disclosed above as follows:

	£m
Working capital and other movements as per regulatory accounts	3.2
Include non-regulated movements in working capital	(0.9)
Exclude movements in VAT debtor	7.9
Exclude movement on internal creditor not classified as working capital	(8.1)
Adjusted movements in working capital	<u>2.1</u>

## 12. NET DEBT ANALYSIS

	Fixed rate £m	Floating rate £m	Index linked £m	Total £m
<b>Maturity profile</b>				
Between one and two years	19.1	7.8	-	26.9
Between two and five years	-	-	-	-
Between five and twenty years	474.6	75.0	13.8	563.4
In more than twenty years	-	61.2	50.6	111.8
	<u>493.7</u>	<u>144.0</u>	<u>64.4</u>	<u>702.1</u>
Cash				(8.3)
<b>Adjusted net debt at 31 March 2012</b>				<u>693.8</u>
Net amounts owed to subsidiary company				2,465.3
<b>Total net debt at 31 March 2012</b>				<u>3,159.1</u>

## Notes to the Regulatory Accounting Information

### 13. RECONCILIATION BETWEEN STATUTORY AND REGULATORY ACCOUNTS

for the year end 31 March 2012

Regulatory accounts item	Statutory UKGAAP £m	Regulatory £m	
<b>Profit and loss account</b>			
Operating profit	303.4	301.0	Rental income of £2.4m classified as 'other income' in regulatory accounts
Profit before tax	68.6	68.6	Profit before tax unaffected by items shown above
<b>Balance sheet</b>			
Tangible assets	6,143.9	16,280.5	FRS15 adopted in statutory accounts does not permit infrastructure renewals accounting, as required in regulatory accounts. A £6.1m accrual is netted off assets. In addition the Regulatory accounts include the adoption of Private Sewers on 1 October 2011 excluded from statutory accounts due to their negligible economic value.
Infrastructure renewals accrual	-	6.1	
Deferred income - grants and contributions	-	(10,213.6)	Within the statutory accounts deferred income is included within creditors due within one year (£2.9m) and creditors due after more than one year (£68.0m). Deferred income in the regulatory accounts also includes £10,142.7m in respect of private sewers adopted at nil cost on 1 October 2011.
Investment - loan to a group company	-	1,289.4	An internal loan to a Group company is included within debtors in statutory accounts.
Short term deposits	-	8.3	Within the statutory accounts short term deposits are disclosed within 'cash and short term deposits'.
Borrowings (due within one year)	(55.7)	(55.7)	At 31 March 2012 there are no internal loans due within 1 year. Therefore borrowings due within one year are aligned within the statutory and regulatory accounts.
Corporation tax receivable/payable	-	16.7	Included within debtors in statutory accounts, but itemised separately in regulatory accounts.
Debtors	1,476.1	170.0	Internal loans to group company included within investment and short term deposits in regulatory accounts.
Creditors (due within one year)	(319.3)	(316.4)	As above, internal loans and corporation tax treatment differs between the statutory and regulatory accounts.
Creditors (due after more than one year)	(125.5)	(57.5)	As above, deferred income treatment differs between the statutory and regulatory accounts.

# Notes to the Regulatory Accounting Information

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## 14. REGULATORY CAPITAL VALUES AT 2011/12 PRICES

		2012 £m
Opening regulatory capital value for the year	*	4,924
Indexation		176
Capital expenditure (excluding IRE)	*	406
Infrastructure renewals expenditure		83
Infrastructure renewals charge		(60)
Grants and contributions		(16)
Depreciation		(196)
Outperformance of regulatory assumptions (5 years in arrears)		(39)
<b>Closing regulatory capital value</b>	<b>*</b>	<b>5,279</b>
<b>Average regulatory capital value</b>		<b>5,115</b>

Numbers may not add due to rounding

\* The table shows the regulatory capital value as published by Ofwat in April 2012, at March 2012 prices, with the exception of the average RCV, which is shown at average prices. The differences from the actual capital expenditure, depreciation etc will not affect price limits in the current period. Capital efficiencies will be taken into account in the calculation for the next periodic review.

# **Regulatory Operating and Financial Review**

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## **INTRODUCTION**

The requirements of the Regulatory Operating and Financial Review are set out in this section and, where noted by cross reference below, in the Business Review and Directors' Report that accompany the statutory financial statements of Yorkshire Water

The Business Review on page 2 of the statutory financial statements of Yorkshire Water contains a description of the business, its strategy and review of financial and operational performance in the year, together with key performance indicators, based on the statutory accounts. It also sets out forward-looking statements and the principal risks and uncertainties facing the business.

This review contains additional information and disclosures on regulatory financial information.

The Directors' Report on page 19 of the statutory financial statements of Yorkshire Water sets out the principal activities of the company, subsequent events and company's policy in respect of employees, employment practices, environment and community matters.

The Regulatory Operating and Financial Review in the Regulatory Accounts is required by Ofwat. The contents, including the cross-referencing to the statutory financial statements where appropriate, have been prepared following the Accounting Standards Board's Reporting Statement, as supplemented by additional Ofwat requirements.

## **FINANCIAL PERFORMANCE**

Profit before tax has increased by £26.2m to £68.6m and operating profit has reduced by £10.2m to £301.0m since 2010/11. Increased turnover of £26.2m has largely offset increased regulatory operating costs of £31.2m.

Total regulated turnover for 2011/12 amounted to £885.0m (£875.1m mains charges), an increase of £25.3m (2.9%) over the 2010/11 total of £859.7m (£851.2m mains charges). This turnover is £3.7m lower than the income anticipated within the Final Determination (FD) when restated for actual RPI (£888.7m). The main charges income increase reflects:

- A higher level of domestic meter optants than assumed in the FD,
- A lower level of new connections than assumed in the FD,
- Domestic revenue declines greater than assumed in the FD,
- Offset by additional income from commercial customers and billing process improvements.

Regulated operating costs increased by £31.2m (7.9%) from 2010/11. The year on year movement has arisen as follows:

- Increase of £18.9m in relation to a year on year movement in RPI,
- £9.6m additional expenditure on leakage management,
- £4.0m increase in the non domestic rates bill subsequent to the five yearly revaluation as transitional relief is removed,
- £5.0m in relation to new responsibilities for private sewers transferred to Yorkshire Water on 1 October 2011,
- £3.7m increase as a result of the new carbon reduction commitment charge, offset by
- £10.0m other savings identified.

The infrastructure renewals charge of £61.3m is in line with the 2010/11 charge. The increase in RPI has been offset by lower infrastructure renewals expenditure over AMP5 than anticipated previously due to the reduction in COPI, which drives the capital programme.

# Regulatory Operating and Financial Review

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The interest charge of £234.8m was £36.4m lower than 2010/11. £40.0m of the reduction was due to a £40.0m exceptional interest cost in 2010/11 in relation to the movement in an onerous contract provision in relation to index linked swaps which are out of the money and do not fully hedge floating rate debt. A review of the onerous contract provision at 31 March 2012 does not require any further adjustments in 2011/12.

The tax charge for the year includes a current corporation tax credit of £18.9m, based on the utilisation of tax losses from other group companies and adjustments in respect of prior years, and a deferred tax charge of £9.7m, reflecting the impact on deferred tax provisions of the reduction to the future corporation tax rate from 26% to 24%.

## Exceptional items

The severe winter weather event in 2010/11 and 2011/12 led to the following exceptional costs during 2011/12:

Employee Costs	£0.015m	Proactive leakage detection carried out by YW employees
Hired and contracted services	£4.843m	R&M costs associated with additional leakage repairs (non visible)
Hired and contracted services	£3.578m	Proactive leakage detection by Contract partners (RPS)
Hired and contracted services	£1.133m	R&M costs associated with additional leakage repairs on customer supply pipes
<b>Total</b>	<b>£9.569m</b>	

## Atypical costs

With the exception of the additional leakage expenditure classified as exceptional within the statutory accounts, there are no other significant items of operating cost which are considered atypical.

## Donations to charitable trusts

No notable donations (2011: £0.1m) were made by the company during the year to various charitable organisations. £0.7m was donated by Kelda Group Ltd, a company owned by the ultimate parent to the Yorkshire Water Community Trust.

## Dividends

Dividend payments of £63.4m were made during the year (2011: £46.9m). No final dividend is proposed in respect of 2011/12.

## Cautionary statement

The purpose of this annual report is to provide information to members of the company and contains certain forward-looking statements with respect to the operations, performance and financial condition of the Group. By their nature, these statements involve uncertainty since future events and circumstances can cause results to differ from those anticipated. Nothing in this report should be construed as a profit forecast.

# ***Directors' Responsibilities***

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## **STATEMENT OF DIRECTORS' RESPONSIBILITIES**

The Directors are responsible under Condition F of the Instrument of Appointment by the Secretary of State for the Environment of the company as a water and sewerage undertaker under the Water Act 1991 for

- a) ensuring that proper accounting records are kept by the Appointee as required by paragraph 3 of Condition F of the Instrument and having regard to the terms of any guidelines notified from time to time by Ofwat,
- b) preparing on a consistent basis in respect of each financial year accounting statements in agreement with the Appointee's accounting records and in accordance with the requirements of Condition F and any guidelines notified from time to time by Ofwat to the Appointee. So far as reasonably practicable these should have the same content as the annual accounts of the Appointee prepared under the Companies Act 2006 and be prepared in accordance with the formats and the accounting policies and principles which apply to those accounts,
- c) preparing accounting statements on a current cost basis in respect of the same accounting period in accordance with guidelines issued to the Appointee from time to time

## **DISCLOSURE OF INFORMATION TO THE AUDITORS**

As far as each director is aware there is no relevant audit information of which the company's auditors are unaware and each director has taken such steps as he or she should have taken as a director in order to make him or herself aware of any relevant audit information and to establish that the company's auditors are aware of the information

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

Legislation in the United Kingdom governing the preparation and dissemination of financial statements and Regulatory Accounts may differ from legislation in other jurisdiction

## **Other Regulatory Declarations**

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### **RING FENCING**

In the opinion of the Directors, the company was in compliance with paragraph 3.1 of Condition K of the Instrument of Appointment at the end of the financial year. This relates to the availability of rights and assets in the event of a special administration order.

### **DIRECTORS' CERTIFICATE - CONDITION F**

The Directors declare that, in their opinion:

- i) the company will have available to it sufficient financial resources and facilities to enable it to carry out, for at least the next 12 months, its regulated activities (including the investment programme necessary to fulfil its obligations under its appointments), and
- ii) the company will, for at least the next 12 months, have available to it
  - a) management resources, and
  - b) systems of planning and internal control

which are sufficient to enable it to carry out those functions.

In making this declaration, the Directors have taken into account -

- a) the net worth of the company and the strength of key performance indicators as shown in the audited accounts for the year ended 31 March 2012 and the company's business plan for 2012/13,
- b) borrowing facilities which include significant committed undrawn bank facilities,
- c) parental support provided by the holding company which will provide financial support to the company to enable it to meet its liabilities as they fall due,
- d) the company's formal risk management process which reviews, monitors and reports on the company's risks and mitigating controls and considers potential impact in terms of service, compliance, value, people, society and partners, and
- e) the company's employment policies and strategy as described in detail in the Directors' Report on pages 21 and 22 of the statutory financial statements of Yorkshire Water.

The Directors also declare that in their opinion all contracts entered into with any Associated Company, include all necessary provisions and requirements concerning the standard of service to be supplied to the company to ensure that it is able to meet all its obligations as a water and sewerage undertaker, as required in Section 6A.2A(3) of Condition F of the Instrument of Appointment. This opinion has been formed following examination of the documents in question.

# ***Independent Auditors' Report on the Regulatory Accounting Information***

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**Independent Auditors' report to the Water Services Regulation Authority (the Authority, referred to as the "WSRA") and the Directors of Yorkshire Water Services Ltd**

We have audited the regulatory accounts of Yorkshire Water Services Limited ("the Company") for the year ended 31 March 2012 on pages 58 to 83 (the "Regulatory Accounts") which comprise

- the regulatory historical cost accounting statements comprising the regulatory historical cost profit and loss account, the regulatory historical cost balance sheet, the regulatory historical cost statement of total recognised gains and losses and the historical cost reconciliation between the statutory financial statements and the Regulatory Accounts, and
- the regulatory current cost accounting statements, for the appointed business comprising the current cost profit and loss account, the current cost balance sheet, the current cost cash flow statement and the related notes including the Statement of Accounting Policies

These Regulatory Accounts have been prepared in accordance with the basis of preparation and accounting policies set out in the Statement of Accounting Policies

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

## **Respective responsibilities of the WSRA, the Directors and Auditors**

As explained more fully in the Statement of Directors' Responsibilities set out on page 86, the directors are responsible for the preparation of the Regulatory Accounts and for their fair presentation in accordance with the basis of preparation and accounting policies Our responsibility is to audit and express an opinion on the Regulatory Accounts in accordance with International Standards on Auditing (UK and Ireland), except as stated in the 'Scope of the audit of the Regulatory Accounts' below, and having regard to the guidance contained in Audit 05/03 'Reporting to Regulators of Regulated Entities' issued by the Institute of Chartered Accountants in England and Wales Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors

## **Scope of the audit of the Regulatory Accounts**

An audit involves obtaining evidence about the amounts and disclosures in the Regulatory Accounts sufficient to give reasonable assurance that the Regulatory Accounts are free from material misstatement, whether caused by fraud or error This includes an assessment of whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the Regulatory Accounts In addition, we read all the financial and non-financial information in the Regulatory Accounts to

# **Independent Auditors' Report on the Regulatory Accounting Information**

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identify material inconsistencies with the audited Regulatory Accounts. If we become aware of any apparent misstatements or inconsistencies we consider the implications for our report.

We have not assessed whether the accounting policies are appropriate to the circumstances of the Company where these are laid down by Condition F. Where Condition F does not give specific guidance on the accounting policies to be followed, our audit includes an assessment of whether the accounting policies adopted in respect of the transactions and balances required to be included in the Regulatory Accounts are consistent with those used in the preparation of the statutory financial statements of the company. Furthermore, as the nature, form and content of Regulatory Accounts are determined by the WSRA, we did not evaluate the overall adequacy of the presentation of the information, which would have been required if we were to express an audit opinion under International Standards on Auditing (UK & Ireland).

## **Opinion on Regulatory Accounts**

In our opinion the Regulatory Accounts

- fairly present in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA and the accounting policies set out on page 63, the state of the Company's affairs at 31 March 2012 on an historical cost and current cost basis, and its historical cost and current cost profit and its current cost cash flow for the year then ended, and
- have been properly prepared in accordance with Condition F, the Regulatory Accounting Guidelines and the accounting policies.

## **Basis of preparation**

Without modifying our opinion, we draw attention to the fact that the Regulatory Accounts have been prepared in accordance with Condition F, the Regulatory Accounting Guidelines, the accounting policies set out in the statement of accounting policies and, in the case of the regulatory historical cost accounting statements, under the historical cost convention.

The Regulatory Accounts are separate from the statutory financial statements of the Company and have not been prepared under the basis of United Kingdom Generally Accepted Accounting Practice ("UK GAAP"). Financial information other than that prepared on the basis of UK GAAP does not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in statutory financial statements prepared in accordance with the Companies Act 2006. Furthermore, the regulatory historical cost accounting statements on pages 58 and 59 have been drawn up in accordance with Regulatory Accounting Guideline 3.06 in that infrastructure renewals accounting as applied in previous years should continue to be applied and accordingly, that the relevant sections of Financial Reporting Standards 12 and 15 be disapplied. The effect of this departure from Generally Accepted Accounting Practice and a reconciliation of the balance sheet drawn up on this basis to the balance sheet drawn up under the Companies Act 2006 is given on page 82.

## **Opinion on other matters prescribed by Condition F**

Under the terms of our contract we have assumed responsibility to provide those additional opinions required by Condition F in relation to the accounting records. In our opinion

- proper accounting records have been kept by the appointee as required by paragraph 3 of Condition F, and

# **Independent Auditors' Report on the Regulatory Accounting Information**

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- the Regulatory Accounts are in agreement with the accounting records and returns retained for the purpose of preparing the Regulatory Accounts

## **Other matters**

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

Our opinion on the Regulatory Accounts is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2012 on which we reported on 27 June 2012, which are prepared for a different purpose. Our audit report in relation to the statutory financial statements of the Company (our "Statutory audit") was made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our Statutory audit work was undertaken so that we might state to the Company's members those matters we are required to state to them in a statutory audit report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume responsibility for any other purpose or to any other person to whom our Statutory audit report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.



PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Leeds  
27 June 2012