

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS

YEAR ENDED 31 MARCH 2007

BRISTOL WATER plc
REGULATORY ACCOUNTING STATEMENTS
for the year ended 31 March 2007

The Company was appointed by the Secretary of State for the Environment as a Water Undertaker under the Water Act 1989 and is required to comply with Conditions set out in its Instrument of Appointment ("the Licence").

The regulatory information that follows has been prepared in accordance with Condition F of the Licence and Regulatory Accounting Guidelines issued by the Water Services Regulation Authority (Ofwat). These financial statements have been prepared for use by Ofwat. They may not be appropriate for any other purpose. As required by Ofwat, they do not correspond with the Statutory Annual Report and Accounts particularly in respect of infrastructure renewals accounting.

The accompanying Historical Cost and Current Cost Accounting Statements were approved by a Committee of the Board on 13 July 2007.

| CONTENTS | Page |
|--|-------------|
| Regulatory Accounting Statements | |
| Operating and Financial Review | 3 |
| Reconciliation between Statutory Annual Report and Accounts and Regulatory Accounts – Historical cost accounting statements | 12 |
| Historical cost accounting statements | 15 |
| Current cost accounting statements | 42 |
| Directors' Remuneration | 55 |
| Independent accountants' report | 56 |
| Regulatory certificate by the directors | 58 |
| Appendix - Statutory Annual Report & Accounts | 61 |

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS for the year ended 31 March 2007

OPERATING AND FINANCIAL REVIEW

This Operating and Financial Review is based on the Chairman's Statement and the Directors' Report and Business Review included in the Company's Annual Report and Accounts for the year ended 31 March 2007, but adapted to remove some specific disclosures and include additional commentary relevant to the Regulatory Accounts

BUSINESS STRATEGY AND OBJECTIVES

The company's vision is to be **'a local water company committed to delivering world class performance at best value, efficiently, innovatively and sustainably'**. To achieve this vision the company's key objectives are to:

- provide a safe and reliable supply of water
- deliver comprehensive high quality service
- create value by operating as efficiently as possible and outperforming regulatory targets
- act in a reasonable and sustainable manner
- make the company a great place to work

The company provides water supply and related services to a population of over one million people and businesses in an area of almost 2,400 square kilometres centred on Bristol.

The company is a regulated business and subject to economic regulation by the Water Services Regulation Authority (Ofwat) through a price cap mechanism, whereby the prices the company can charge for the majority of its services are limited to increases in inflation plus or minus a K factor (RPI+/-K). Price limits, the 'K' factors, are currently reviewed every five years. The last review was announced in December 2004 and covers the five years 2005/06 to 2009/10.

The water industry is essentially a monopoly and the Government through Ofwat is progressively seeking to open up competition within the industry for large industrial and commercial customers and greenfield domestic developments. To date, competition has had no significant impact on either the company or the rest of the industry.

The water industry is subject to a range of UK and EU legislation, with operational and service standards being tightened on a regular basis. The company's performance is monitored by three main regulators - Ofwat for levels of service to customers, the Environment Agency (EA) for environmental protection and the Drinking Water Inspectorate (DWI) for drinking water quality.

RISK AND UNCERTAINTY

The key risks and uncertainties that the company faces are:

Operational:

- contamination or interruption of water resources and/or supplies
- failure of key assets to maintain expected outputs, adversely affecting the ability to maintain supplies to customers
- climate/weather pattern change affecting resource availability and/or customer demand
- retention and recruitment of key staff

Regulatory:

- failure to meet existing regulatory requirements which could result in penalties or enforcement action by Ofwat, EA or DWI
- increased costs of meeting regulatory requirements
- impact of legislative changes including those related to environmental or drinking water quality requirements
- significant development of competition within the water sector
- impact of future periodic and/or interim determinations of price limits by Ofwat; the next periodic review will set prices for 2010/11 onward

Financial:

- loss of major customers as a result of closure
- pensions – the company has a final salary defined benefit scheme. This was closed to new employees some time ago but remains open to future benefit accrual for existing members. At March 2007 the scheme had a surplus before taxation of £11.3m on an FRS17 basis. The funding requirements of the scheme are subject to a range of factors including longevity assumptions, investment allocation and investment returns
- worsening debt collection experience particularly household debt giving rise to increasing levels of bad debts
- inflation – operating costs, the capital investment programme and the company's £98.2m of index-linked debt are subject to inflation; potential adverse impacts of high inflation are mitigated by the index-linking of the majority of revenues through the RPI +/- K price limits
- further increases in energy prices
- changes in the taxation regime applicable to the company
- failure to meet banking covenants

The company has a range of risk management strategies to mitigate the impact of these risks and uncertainties. For certain events it would be able to seek from Ofwat an increase in price limits to meet additional costs that could not have been avoided by prudent management action.

Risk management and mitigation will be an important element of the PR09 25 year strategic direction statement we are preparing for submission to Ofwat in December 2007.

DEVELOPMENT AND PERFORMANCE OF THE BUSINESS DURING THE YEAR

Key developments during the year were:

- The previous ultimate holding company, Bristol Water Group plc (BWG), was acquired by Sociedad General de Aguas de Barcelona SA (Agbar). Agbar provides water services to approximately 23 million people worldwide and their expertise and understanding of the water industry reinforces Bristol Water's commitment to providing high standards of service to its customers.
- Completion of the second year of the regulatory period covering the years 2005-10 with continuing good progress made towards delivery of the required outputs and efficiency targets assumed by Ofwat in its determination of the price limits.

OPERATIONAL PERFORMANCE

The company continues to make good progress in the delivery of the outputs required by Ofwat's determination of price limits for the 2005-2010 period. In particular we have three major capital schemes in progress:

- A £24m project to improve the security of supply for a population of almost 200,000 in the northern and eastern parts of Bristol and surrounding areas
- An £11m project to upgrade our Banwell treatment works to improve its effectiveness in dealing with a range of different raw water qualities
- A £7m project to construct a new treatment works to treat water from the River Axe

In total, we invested £45.5m in capital projects during the year. We currently anticipate a total investment programme for the 5-year regulatory period of almost £170m (in current prices, before grants and contributions). This is broadly in line with Ofwat's assumptions.

Bristol Water has a mix of water sources with approximately 40% from impounding reservoirs, 40% to 50% from river sources and the balance from groundwater sources. This mix provides considerable flexibility. We have not had any water usage restrictions for over 15 years and do not anticipate any need for them in the foreseeable future. We are not complacent and are continually reinforcing the message to customers of the need to use water wisely. During 2006/07 we continued to meet our leakage target agreed with Ofwat.

Billing and operational service levels have remained high. Our surveys show continuing high levels of customer satisfaction.

BOARD STRUCTURE

Professor David Blockley retired on 23 May 2007 after three years service as a director of the company and nine years service with the Bristol Water Group.

In June 2006 three Agbar appointees joined the Board, two in executive positions. We now welcome Ciril Rozman, a senior financial manager with Agbar, who was appointed to the Board as a non-executive director on 23 May 2007.

At the date of this report, for the purpose of Condition P of the companies Instrument of Appointment as a Water Undertaker, the three non-executive directors regarded as independent, are Trevor Smallwood, Peter McIlwraith and Chris Curling.

FINANCIAL PERFORMANCE

The company continues to report under UK GAAP as modified by Ofwat in certain situations.

Summary performance:

| | Regulated Historical Cost Accounts Total | | Regulated Historical Cost Accounts Appointed business | | Current Cost Accounts Appointed business | |
|--|---|--------------|---|--------------|---|--------------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| | £m | £m | £m | £m | £m | £m |
| Turnover | 85.8 | 81.4 | 83.6 | 79.7 | 83.6 | 79.7 |
| Operating costs | (42.1) | (39.0) | (40.3) | (37.5) | (40.3) | (37.6) |
| Depreciation | (8.8) | (8.8) | (8.8) | (8.7) | (15.1) | (14.4) |
| Infrastructure renewals charge | (12.0) | (9.8) | (12.0) | (9.8) | (12.0) | (9.8) |
| Working capital adjustment | - | - | - | - | (0.1) | - |
| Operating profit | 22.9 | 23.8 | 22.5 | 23.7 | 16.1 | 17.9 |
| Other net income | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 |
| Net finance costs | (6.3) | (6.5) | (6.3) | (6.5) | (6.3) | (6.5) |
| Financing adjustment | - | - | - | - | 5.4 | 3.2 |
| Profit before tax | 17.0 | 17.7 | 16.6 | 17.6 | 15.6 | 15.0 |
| Taxation | (2.5) | (6.8) | (2.4) | (6.8) | (2.4) | (6.8) |
| Profit after tax | 14.5 | 10.9 | 14.2 | 10.8 | 13.2 | 8.2 |
| Capital investment before grants & contributions | 45.5 | 22.6 | 45.5 | 22.6 | 45.5 | 22.6 |
| Net debt (excluding 8.75% irredeemable cumulative preference shares) at 31 March | 176.3 | 166.2 | 176.3 | 166.2 | 176.3 | 166.2 |
| Ratio of net debt (excluding 8.75% irredeemable cumulative preference shares): Regulatory Capital Value (RCV) | 68% | 71% | | | | |

Historical cost performance

Turnover increased by £4.4m to £85.8m. This mainly reflects the impact of the average increase of 5.2% in main charge tariffs from April 2006 worth £4.0m. There has been a reduction in household unmeasured income, offset by an increase in household measured income, due to unmeasured customers opting for a meter to be fitted and therefore changing to a measured supply.

Operating costs increased by £3.1m, after allowing for RPI this is an increase of £1.4m in real terms:

| | Change £m |
|---|--------------|
| Real increase in power costs | 1.0 |
| Real increase in chemical and material costs | 0.3 |
| Real increase in bad debt charges | 0.6 |
| Additional costs related to business process review | 0.3 |
| Additional new Quality & Supply/Demand opex | 0.4 |
| Reduction in abortive capex | (0.2) |
| Efficiency and other net changes | (1.0) |
| Increase in real terms | <u>1.4</u> |
| RPI effect | <u>1.7</u> |
| Total increase | <u>3.1</u> |

An important element of our operating cost base is energy. In line with general market movements we were adversely affected by the impact of a price increase of approximately 65% effective from October 2006. We have now entered into a 3 year flexible energy purchasing contract which will allow us to reduce our exposure to market movements. We currently anticipate that energy costs for 2007/08 will remain at broadly the same level as for 2006/07 with the full year effect of the October 2006 tariff increase being offset by reduced tariffs from October 2007.

Our charge for bad debts increased to £2.3m (2006: £1.6m) and represents approximately 2.7% of turnover. We are experiencing a continuing trend of customer debt becoming harder and more expensive to collect. An important factor was the Government decision to remove in 2000 the right of water companies to disconnect supplies to domestic customers who do not pay. We have enhanced our debt collection activity and have initiatives to assist customers facing genuine difficulties in paying.

Historical cost depreciation remained loosely unchanged. This reflects additional depreciation related to completed projects of £1.5m offset by a reduction of £0.5m in the charge for accelerated depreciation related to assets to be taken out of operational service before being fully depreciated, and a reduction of £1.0m in respect of fully depreciated assets.

Infrastructure renewals charge

The Infrastructure renewals charge (IRC) is calculated over a fifteen year period.

In 2005/06 the IRC was the annual average of:

- the Infrastructure Renewals Actual Expenditure (IRE) for the period from 2000/01 to 2005/06
- the latest forecast IRE for 2006/07 to 2009/10
- the Final Determination IRE for 2010/11 to 2014/15

all expressed in 2005/06 prices less the opening prepayment at 1 April 2000, with the total being divided by fifteen.

Following discussion with Ofwat we have based the infrastructure renewals charge for 2006/07 on:

- One fifteenth of the total actual and forecast expenditure between 2005 and 2020
- An adjustment is made to the charge to ensure that there is no pre-payment or accrual at the end of 2020, taking into account:
 - The opening accrual in 2005 and the charge for 2005/06
 - That the charge during 2010-2015 will be based on expenditure between 2010 and 2025
 - That the charge between 2015-2020 will be based on expenditure between 2015 and 2030.
 - Forecast expenditure is based on the Company capital programme up to 2010 and then upon the PR04 Determination figures between 2010 and 2020. Expenditure beyond 2020 is assumed to be the same as in the period 2015-2020.

This approach has been used for the purposes of Regulatory Accounting only. In our UK GAAP statutory accounts we are continuing to calculate IRC based on IRE for the current five year regulatory period.

The approach we have taken for the Regulatory Accounts:

- Takes a medium term view
- Avoids creation of a non-reversing accrual or prepayment
- Uses the PR04 Determination IRE values for 2010 onwards to provide reasonable certainty

The **current and deferred tax charges** are included in line with the statutory accounts. The regulatory accounts adjustments do not have an effect on the current tax charges and for deferred tax have been treated as permanent timing differences within the tax reconciliation.

The tax charge of £2.5m represents an effective tax rate of 14% (2006: 37%). The principal reasons for the low rate compared to 2006 are prior year adjustments together with a significant variation in the discount rates used to calculate the deferred tax liability.

Current Cost Performance

The **current cost depreciation charge** increased by £0.7m to £15.1m reflecting:

| | £m | £m |
|------------------------------------|------------|-------------|
| 2005/06 charge | | 14.4 |
| Inflation | 0.7 | |
| Assets fully depreciated | (0.8) | |
| 2005/06 additions full year effect | 0.5 | |
| 2006/07 additions | 0.4 | |
| Accelerated depreciation | (0.2) | |
| Other | 0.1 | |
| Net increase | <u>0.7</u> | |
| 2006/07 charge | | <u>15.1</u> |

The **financing adjustment** has increased by £2.2m to £5.4m. £2.7m of this year's adjustment is due to the higher RPI, 4.8% in 2006/07 compared to 2.4% in 2005/06.

Changes occurring for reasons other than the increased RPI are:

- The financing adjustment relating to creditors due after one year increased by £1.3m to £5.2m as the opening balance included new long term debt raised during 2005/06 of £50.1m plus premiums
- A further intra-group loan of £21.5m made during 2005/06 out of the proceeds of the new loans reduced the financing adjustment by £0.5m
- Increased cash balances reduced the financing adjustment by £0.7m
- Changes to the basis of the calculation of the financing adjustment from 2005/06 for which no restatement has been made to previous years:
 - The infrastructure maintenance provision is included in the calculation of the financing adjustment in 2006/07 in accordance with the revised guidelines in RAG 1.04. Previously it was included in the working capital adjustment.
 - The deferred tax provision has been excluded from the calculation of the financing adjustment in 2006/07 in line with the revised guidelines in RAG 1.04.
 - The FRS17 pension surplus has also been excluded

TREASURY

Net cash inflow from operating activities was £42.2m (2006: £33.4m) and the outflow from financing activities £2.5m (2006: £52.7m inflow). Net cash used in investing activities was £37.7m (2006: £39.6m including £21.5m advanced to BWG), and net cash used in investment returns and servicing finance was £4.4m (2006: £6.1m).

Net interest charges in the year totalled £6.3m (2006: £6.5m) and were covered 3.6 times (2006: 3.7 times) by operating profit.

At 31 March 2007 gross debt excluding the 8.75% irredeemable cumulative preference shares was £207.1m (2006: £206.7m). Approximately 47% of this debt is index-linked and 38% fixed rate; the index-linked element is hedged against the company's index-linked revenue base.

The company's policy is to maintain a balanced debt portfolio with mainly long dated maturities reflecting the long-term nature of the company's asset base.

The company maintains cash balances and committed credit facilities to meet foreseeable requirements for the remainder of the regulatory period to 2009/10.

Net debt including the 8.75% irredeemable cumulative preference shares increased to £188.8m from £178.7m at 31 March 2006. The increase reflects the continuing capital investment programme.

At the year-end net debt excluding the 8.75% irredeemable cumulative preference shares was £176.3m, representing approximately 68% of Regulatory Capital Value (RCV). We anticipate that this ratio will be maintained in the range of 70% to 80% over the remainder of the five-year regulatory period to 2009/10. This ratio is key and is effectively replicated within the banking covenants. The range that the company expects to operate within provides a headroom margin to meet adverse impacts from risks and uncertainties.

PENSIONS

Pension arrangements for the majority of employees are provided through membership of the Water Companies' Pension Scheme (WCPS) which provides defined benefits based on final pensionable pay. The company has a separate section within WCPS for the regulated water business. This section was closed to new employees a number of years ago. All new employees are offered stakeholder pension arrangements.

At 31 March 2007 the gross surplus before tax under FRS17 of the company's section of WCPS was £11.3m. This represents a £6.9m improvement from the £4.4m surplus at 31 March 2006 and reflects additional contributions made during the year and favourable actuarial movements. The company has agreed to make additional contributions of £1.0m in each of the four years beginning April 2006 and £0.9m in 2010/11.

DIVIDENDS

The company's ordinary dividends policy is to pay an annual level of dividends comprising:

- A base level of dividend reflecting the cost of capital allowed by Ofwat in the determination of price limits, adjusted to reflect actual gearing levels and where appropriate actual performance relative to Ofwat's assumptions and
- An amount equal to the post-tax interest receivable from Bristol Water Group Ltd in respect of intercompany loans.

Interim dividends totalling £2.8m have been declared in respect of the year, and the Board proposes a final dividend of £6.0m.

NON-FINANCIAL PERFORMANCE

The company uses a comprehensive system of Key Performance Indicators (KPIs) to monitor non-financial performance throughout the year. Key measures of performance include:

| Years to 31 March | 2006 | 2005 |
|--|------------------------|------------------|
| Ofwat performance measures | | |
| Ofwat overall performance assessment (OPA): | | |
| OPA score (out of 288) | 281 | 281 |
| Ranking (out of 22 companies) | 9th | 10 th |
| Ofwat relative efficiency rankings (out of 22 companies) | | |
| Operating costs | 17th | 13 th |
| Capital maintenance | 11th | 14 th |

The 2007 rankings will be published by Ofwat later this year.

The English and Welsh water companies operate to very high quality and service levels and relatively small differences in performance can have a significant impact on the Ofwat performance measures.

| | Units | Notes | 2007 | 2006 |
|--|---------------|-------|---------------|--------|
| Environment | | | | |
| Excavated materials diverted from landfill | Tonnes | | 16,910 | 16,358 |
| Average energy used to supply 1ML of water | KwH | 1 | 802 | 820 |
| Emission of greenhouse gases in total to supply 1 ML of water | Tonnes of CO2 | 1 | 0.36 | 0.36 |
| Compliance with EA abstraction licences | | | 100% | 100% |
| Status of SSSIs – percentage favourable | | | 100% | 100% |
| Social | | | | |
| Security of supply index | | | 100% | 100% |
| Water quality compliance | | 2, 3 | 99.95% | 99.97% |
| Employees | | | | |
| Turnover rate | | | 6.3% | 4.2% |
| Accidents reportable to HSE | No. | 2 | 7 | 6 |
| Assets | | | | |
| Percentage of properties with interruptions to supply greater than six hours | | | 0.76% | 0.21% |
| Loss of water from supply network | MLD | 4 | 54 | 53 |

- Notes:
- 1 ML = megalitres (1 million litres)
 - 2 Based on 12 months to 31 December ending in the relevant accounting period
 - 3 Water quality is based on mean zonal compliance data
 - 4 MLD = megalitres per day

CORPORATE SOCIAL RESPONSIBILITY

The company is committed to acting in a responsible and sustainable manner.

Environment

The water industry has a high environmental impact. By reference to a range of sustainability measures developed by Water UK (the trade body for water companies in England and Wales), the company performs well compared to its peer group.

We:

- fulfil and in many areas exceed all the requirements of conservation and environmental duties set out in the Water Industry Act 1991 and codes of practice on conservation, access and recreation
- have a well established environmental policy with a strong commitment to the sustainable management of water resources and our assets
- carefully assess the risks associated with the potential environmental impact of our work to ensure that risks are mitigated and managed effectively

Social and community

We:

- deliver high quality reliable supplies of water to over one million people
- provide the best possible access to our major reservoirs whilst seeking to maintain a balance between wildlife and recreational demands. Chew Valley Lake, our largest reservoir, has an international reputation for the quality of its fishing
- undertake a programme of educational support including open days, access to visitor centres and school visits
- make charitable donations, sponsorships and grants to local organisations and individuals to promote good causes. During the year ended 31 March 2007 these were made by BWG on the company's behalf, but in future years will be made by Bristol Water plc directly. There were no donations to charitable trusts and other funds assisting customers with payment difficulties in 2006/07 (2005/06 - £1k).

Employees

Our employees are vital to the success of the company.

We:

- are committed to employee involvement, communication, training and sound relationships with trade unions
- are an equal opportunity employer providing employment and appropriate facilities for disabled people and for those who have become disabled while employed by the company
- have high standards for health and safety
- operate bonus schemes for all employees
- make continued efforts to improve the work environment

Key performance indicators:

The company uses a series of KPIs to monitor environmental performance; some key measures are included in the non-financial performance section earlier in this report.

Further details of the company's environmental, conservation and recreation policies are available on our website www.bristolwater.co.uk.

OUTLOOK

The main drivers of future profitability for the period to 2009/10 will be:

- increases in charges to customers in line with the RPI+/-K price limits. The K factors for the next 3 years are:

| | K % |
|---------|-------|
| 2007/08 | +1.5% |
| 2008/09 | +0.7% |
| 2009/10 | -2.3% |

- changes in operating costs - further efficiencies obtained by the company offset by the cost of new obligations and inflation
- inflation – operating costs, the capital investment programme and the company's £98.2m of index-linked debt are subject to inflation; potential adverse impacts of high inflation are mitigated by the index-linking of the majority of revenues through the RPI +/- K price limits
- the company is a major energy user; in line with general market movements costs were adversely affected by a price increase of approximately 65% effective from October 2006. We have now entered into a 3 year flexible energy purchasing contract which will allow us to reduce our exposure to market movements. We currently anticipate that energy costs for 2007/08 will remain at approximately the same level as for 2006/07 with the full year effect of the October 2006 tariff increase being offset by reduced tariffs from October 2007
- delivery of the capital investment programme required to meet the obligations set out in Ofwat's determination of price limits. We currently anticipate delivering the capital investment programme in real terms broadly in line with Ofwat's assumptions
- changes in pension funding/deficits
- the impact of changes in corporation tax arrangements as announced in the Chancellor's recent budget and explained in note 4 to the accounts.

Ofwat price review for 5 years from 2010 (PR09)

The PR09 price review, which will result in the setting of price limits for the 5-year period 2010/11 to 2014/15, is now underway. The first major milestone will be the submission to Ofwat in December 2007 of our strategic direction statement setting out our vision and outline plans for the next 25 years.

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

Following guidance issued by the Department of Trade and Industry (DTI), as the company does not prepare consolidated accounts, it is not mandatory for the company to adopt IFRS.

The company has decided at this stage not to adopt IFRS. The company will therefore continue to prepare its financial statements using UK GAAP accounting standards for the foreseeable future.

AUDITORS AND DISCLOSURE OF INFORMATION TO AUDITORS

Following the acquisition of BWG by Agbar, Deloitte & Touche LLP were appointed auditors on 11 September 2006 in place of PricewaterhouseCoopers LLP.

Each of the persons who is a director at the date of approval of this report confirms that:

- (1) so far as the director is aware, there is no relevant audit information of which the company's auditors are unaware; and
- (2) the director has taken all the steps that he ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of s235 ZA of the Companies Act 1985.

DIRECTORS' RESPONSIBILITIES FOR THE PREPARATION OF FINANCIAL STATEMENTS

The directors are responsible for preparing the Annual Report including the financial statements. The directors have chosen to prepare the financial statements for the company in accordance with United Kingdom Generally Accepted Accounting Practice (UK GAAP).

Company law requires the directors to prepare such financial statements for each financial year which give a true and fair view, in accordance with UK GAAP, of the state of affairs of the company and of the profit or loss of the company for that period and comply with UK GAAP and the Companies Act 1985. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business;
- ensure so far as they are aware, there is no relevant audit information of which the company's auditors are unaware; and
- take all steps they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of the information.

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

After making enquiries, the directors are of the opinion that the company has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt a going concern basis in preparing these financial statements.

In addition, the directors have responsibility for ensuring that the company keeps proper accounting records sufficient to enable the historical cost and current cost information required by Condition F of the licence to be prepared, having regard to all Regulatory Accounting Guidelines.

The directors are also required to confirm in the financial statements that, in their opinion, the company was in compliance with paragraph 3.1 of Condition K of the licence relating to the availability of the rights and assets, at the end of the financial year.

By order of the Board
S C Robson
Secretary
13 July 2007

BRISTOL WATER plc
REGULATORY ACCOUNTING STATEMENTS
for the year ended 31 March 2007

RECONCILIATION BETWEEN STATUTORY ANNUAL REPORT AND ACCOUNTS AND REGULATORY ACCOUNTS

PROFIT AND LOSS ACCOUNT

| | Statutory Annual Report and Accounts 2007 | Net rental income | Basis for Infrastructure renewals charge | Section 41 revenue deficit contributions | Regulatory Historical cost accounts 2007 | Non-appointed activities | Regulatory Appointed Historical cost accounts 2007 |
|--------------------------------|--|-------------------|--|--|---|--------------------------|---|
| | £m | £m | £m | £m | £m | £m | £m |
| Turnover | 86.3 | (0.5) | - | - | 85.8 | (2.2) | 83.6 |
| Operating costs | (42.2) | 0.1 | - | - | (42.1) | 1.8 | (40.3) |
| Depreciation | (9.1) | - | - | 0.3 | (8.8) | - | (8.8) |
| Infrastructure renewals charge | (9.8) | - | (2.2) | - | (12.0) | - | (12.0) |
| Operating profit | 25.2 | (0.4) | (2.2) | 0.3 | 22.9 | (0.4) | 22.5 |
| Other net income | - | 0.4 | - | - | 0.4 | - | 0.4 |
| Net finance costs | (6.3) | - | - | - | (6.3) | - | (6.3) |
| Profit before tax | 18.9 | - | (2.2) | 0.3 | 17.0 | (0.4) | 16.6 |
| Taxation | (2.5) | - | - | - | (2.5) | 0.1 | (2.4) |
| Profit after tax | 16.4 | - | (2.2) | 0.3 | 14.5 | (0.3) | 14.2 |

Ofwat accounting guidelines state that net rental income should be classified as “other income”, below operating profit.

In the Statutory Annual Report and Accounts the infrastructure renewals charge (IRC) calculation is based on the infrastructure renewals expenditure for the current five year regulatory period. The calculation of the charge in the regulatory accounts is based on a fifteen year forward looking period, creating a higher charge than in the Statutory Annual Return and Accounts.

In 2005/06 there was a change in the accounting treatment of Section 41 revenue deficit contributions in the statutory accounts, which was not adopted for the regulatory accounts. This change has now been reversed following consultation with our new auditors. The change credited the revenue deficit contributions to deferred income, and amortised them over three years, instead of crediting them against fixed assets. It created a difference between the depreciation in the regulatory accounts and the statutory accounts, equivalent to the amount amortised during the year.

RECONCILIATION BETWEEN STATUTORY ANNUAL REPORT AND ACCOUNTS AND REGULATORY ACCOUNTS

BALANCE SHEET

| | Statutory Annual Report and Accounts | Infrastructure renewals charge | Infrastructure renewals provision | Regulatory Historical cost accounts | Non- appointed activities | Regulatory Appointed Historical cost accounts |
|--|---|--------------------------------------|---|--|---------------------------------|--|
| | 2007 £m | £m | £m | 2007 £m | £m | 2007 £m |
| Tangible fixed assets (net book value) | 218.7 | (2.6) | 1.4 | 217.5 | (1.3) | 216.2 |
| Investments-loans to ultimate UK holding company | 68.5 | - | - | 68.5 | - | 68.5 |
| Net current assets | 25.8 | - | - | 25.8 | 1.3 | 27.1 |
| Creditors-amounts falling due after more than one year | (204.6) | - | - | (204.6) | - | (204.6) |
| 8.75% Irredeemable preference shares | (12.5) | - | - | (12.5) | - | (12.5) |
| Deferred Income | (9.4) | - | - | (9.4) | - | (9.4) |
| Provisions for liabilities and charges | (19.7) | - | (1.4) | (21.1) | - | (21.1) |
| Retirement benefit obligations | 8.3 | - | - | 8.3 | - | 8.3 |
| Net assets | <u>75.1</u> | <u>(2.6)</u> | <u>-</u> | <u>72.5</u> | <u>-</u> | <u>72.5</u> |
| Capital and reserves | | | | | | |
| Called up share capital | 6.0 | - | - | 6.0 | - | 6.0 |
| Share premium account | 4.4 | - | - | 4.4 | - | 4.4 |
| Other reserves | 5.8 | - | - | 5.8 | - | 5.8 |
| Profit and loss account | <u>58.9</u> | <u>(2.6)</u> | <u>-</u> | <u>56.3</u> | <u>-</u> | <u>56.3</u> |
| Total shareholders' funds | <u>75.1</u> | <u>(2.6)</u> | <u>-</u> | <u>72.5</u> | <u>-</u> | <u>72.5</u> |

RECONCILIATION BETWEEN STATUTORY ANNUAL REPORT AND ACCOUNTS AND REGULATORY ACCOUNTS

In the preparation of its statutory accounts, the company has followed common industry practice and adopted the infrastructure renewals accounting basis as set out in FRS15: Tangible Fixed Assets. Infrastructure renewals expenditure is included in additions to fixed assets, and the infrastructure charge (IRC) is included in depreciation. However for the purposes of the regulatory accounts, Ofwat requires that FRS15 is not applied for infrastructure renewals accounting, thereby providing a basis consistent with prior years and the inclusion of an infrastructure renewals provision. The £2.6m represents the cumulative difference between the IRC in the Statutory Annual Report and Accounts and the regulatory accounts. Below is a reconciliation of the fixed assets in the Statutory Annual Report and Accounts, to those in the regulatory appointed historical cost accounts:

FIXED ASSETS

| | Statutory Annual Report and Accounts | Adjustment to opening balance in respect of infrastructure renewals accounting | Additions | Infrastructure renewals expenditure capitalised in year | Reallocated statutory accounts IRC for year | Regulatory Appointed Historical cost accounts | Non-appointed activities | Regulatory Appointed Historical cost accounts |
|--|--------------------------------------|--|---------------|---|---|---|--------------------------|---|
| | 2007 £m | £m | £m | £m | £m | 2007 £m | £m | 2007 £m |
| Cost | | | | | | | | |
| Freehold land and operational structures | 164.9 | - | - | - | - | 164.9 | (1.6) | 163.3 |
| Plant & equipment | 30.0 | - | - | - | - | 30.0 | (0.2) | 29.8 |
| Infrastructure assets | 187.1 | (88.3) | - | (12.6) | - | 86.2 | - | 86.2 |
| Assets under construction | 27.5 | - | (12.6) | 12.6 | - | 27.5 | - | 27.5 |
| Total | 409.5 | (88.3) | (12.6) | - | - | 308.6 | (1.8) | 306.8 |
| Depreciation | | | | | | | | |
| Freehold land and operational structures | 70.2 | - | - | - | - | 70.2 | (0.3) | 69.9 |
| Plant & equipment | 20.9 | - | - | - | - | 20.9 | (0.2) | 20.7 |
| Infrastructure assets | 99.7 | (89.9) | - | - | (9.8) | - | - | - |
| Total | 190.8 | (89.9) | - | - | (9.8) | 91.1 | (0.5) | 90.6 |
| Net Book Value | | | | | | | | |
| Freehold land and operational structures | 94.7 | - | - | - | - | 94.7 | (1.3) | 93.4 |
| Plant & equipment | 9.1 | - | - | - | - | 9.1 | - | 9.1 |
| Infrastructure assets | 87.4 | 1.6 | - | (12.6) | 9.8 | 86.2 | - | 86.2 |
| Assets under construction | 27.5 | - | (12.6) | 12.6 | - | 27.5 | - | 27.5 |
| Total | 218.7 | 1.6 | (12.6) | - | 9.8 | 217.5 | (1.3) | 216.2 |

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS

**HISTORICAL COST ACCOUNTING STATEMENTS
for the year ended 31 March 2007**

BRISTOL WATER plc

HISTORICAL COST ACCOUNTING POLICIES

The regulatory accounts are separate from the statutory financial statements of the Company. There are differences between United Kingdom Generally Accepted Accounting Principles (UK GAAP) and the basis of preparation of information provided in the regulatory accounts because the Regulatory Accounting Guidelines (RAGs) specify alternative treatment or disclosure in certain respects. Where the RAGs do not specifically address an accounting issue, then they require UK GAAP to be followed. Financial information, other than that prepared wholly on the basis of UK GAAP, does not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in financial statements prepared in accordance with the Companies Act 1985.

The significant accounting policies adopted in the preparation of the accounts, which have been applied consistently, are set out below.

a. Accounting convention

The accounts of the company are prepared under the historical cost convention and in accordance with applicable accounting standards in the United Kingdom (UK GAAP) and with the provisions of the Companies Act 1985, except for the treatment of certain capital contributions as explained in Note d below, the disclosure of operating costs as explained in note 2 and the application of infrastructure renewals accounting as explained in the reconciliation of the statutory Annual return and accounts to the regulatory accounts.

The company has not adopted IFRS for its financial statements for the year ended 31 March 2007, and has no current plans to do so until UK GAAP and IFRS are fully harmonised.

b. Turnover

Turnover comprises charges to, and accrued income from, customers for water and other services, exclusive of VAT.

Income from metered supplies is based upon volumes of water invoiced plus estimated volumes of uninvoiced water delivered to customers during the year.

c. Tangible fixed assets and depreciation

Tangible fixed assets comprise infrastructure assets and other assets.

Infrastructure assets

Infrastructure assets comprise the integrated network of impounding and pumped raw water storage reservoirs and water mains and associated underground pipework. Expenditure on such assets relating to increases in capacity, enhancements or planned maintenance of the network is treated as an addition to fixed assets and is included at cost. The cost of infrastructure assets is their purchase cost together with incidental expenses of acquisition and directly attributable labour costs which are incremental to the company.

Other assets

Other assets include land and buildings, operational structures, fixed and mobile plant, equipment and motor vehicles. All are included at cost. The cost of other assets is their purchase cost together with incidental expenses of acquisition and directly attributable labour costs which are incremental to the company.

Depreciation

Depreciation is charged, where appropriate, on a straight-line basis on the original cost of assets over their expected economic lives. Freehold land is not depreciated. Depreciation of long-life assets commences when the assets are brought into use.

Depreciation of infrastructure assets takes account of planned expenditure levels to maintain the operating capability of the company's infrastructure assets in perpetuity, and is shown separately as the infrastructure renewals charge.

Other assets including assets under construction are depreciated after commissioning over the following estimated economic lives -

| | |
|---|-----------------|
| Operational properties and structures | 15 to 100 years |
| Treatment, pumping and general plant | 20 to 24 years |
| Computer hardware, software, communications, meters and telemetry equipment | 3 to 15 years |
| Vehicles and mobile plant | 5 to 7 years |

Assets under construction are not depreciated.

Impairment

The values of fixed assets are reviewed regularly to ensure that their carrying amounts do not exceed their fair values in use. Where such an excess is believed to exist it will be treated as an impairment loss and charged in the Profit and Loss account.

d. Grants and contributions

Contributions received in respect of tangible assets, other than those received in respect of infrastructure assets, are treated as deferred income and amortised to the profit and loss account over the expected useful lives of the related assets. Contributions received in respect of enhancing the infrastructure network are not shown as deferred income but are deducted from the cost of the related fixed assets. This treatment is permitted by Statement of Standard Accounting Practice Number 4 but is a departure from the Companies Act 1985 which requires such contributions to be shown as deferred income.

It is the directors' opinion that this treatment is necessary to show a true and fair view as the related assets do not have determinable finite lives and therefore no basis exists for the amortisation of the contributions. The effect on tangible fixed assets is shown in Note 6(d) to the accounts.

Grants and contributions in respect of expenditure charged to the profit and loss account are netted against such expenditure as received.

e. Leased assets

Assets financed by leasing agreements that transfer substantially all the risks and rewards of ownership of an asset to the lessee are capitalised and depreciated over the shorter of their estimated useful lives and the lease term. The capital portion of the lease commitment is included in current or non-current creditors as appropriate. The capital element of the lease rental is deducted from the obligation to the lessor as paid. The interest element of lease rentals and the depreciation of the relevant assets are charged to the profit and loss account.

Operating lease rental payments are charged to the profit and loss account as incurred over the term of the lease.

f. Pension costs

The company operates both defined benefit and defined contribution pension arrangements.

Defined benefit scheme liabilities are measured by an independent actuary using the projected unit method and discounted at the current rate of return on high quality corporate bonds of equivalent term and currency to the liability. The increase in the present value of the liabilities of the company's defined benefit pension schemes expected to arise from employee service in the period is charged to operating profit. The expected return on the scheme's assets and the increase during the period in the present value of the scheme's liabilities, arising from the passage of time, is included in other finance income or cost.

Actuarial gains and losses arising from experience adjustments, changes in actuarial assumptions and amendments to pension plans are charged or credited direct to the statement of recognised gains and losses.

Costs of defined contribution pension schemes are charged to the Profit and Loss account in the period in which they fall due. Administration costs of defined contribution schemes are borne by the company.

g. Research and development

Research and development expenditure is charged to the profit and loss account as incurred.

h. Taxation

In accordance with Ofwat guidelines, the overall tax charge is based on the charge in the statutory accounts and deferred tax has not been recalculated to take account of differences between the statutory and regulatory accounts.

Advance Corporation Tax (ACT) in respect of dividends in previous years was written off to the profit and loss account unless it could be recovered against mainstream corporation tax in the current year or with reasonable assurance in the future. Credit is taken for ACT previously written off when it is recovered against mainstream corporation tax liabilities.

Deferred tax is recognised as a liability or asset if transactions have occurred at the balance sheet date that give rise to an obligation to pay more taxation in future, or a right to pay less taxation in future. An asset is not recognised to the extent that the transfer of economic benefits in future years is not probable. Deferred tax assets and liabilities recognised have been discounted at rates equivalent to the post-tax yields to maturity that could be obtained at the balance sheet date on government bonds with maturity dates similar to those of the deferred tax assets and liabilities.

i. Distributions to shareholders

Dividends and other distributions to shareholders are reflected in financial statements when approved by shareholders in a general meeting, except for interim dividends which are included in financial statements when paid by the company. Accordingly, proposed dividends are not included as a liability in the financial statements.

j. Stocks

Stocks are valued at the lower of cost and net realisable value. Following established practice in the water industry no value is included in the accounts in respect of water held in store.

k. Financial instruments

The company had an interest rate swap which was measured at fair value.

The net costs of issue of loans (being expenses incurred less premiums received) are amortised over the lives of the respective loans and disclosed within net borrowings. Index-linked loans are considered to be effective economic hedges and are valued at cost plus accrued indexation.

l. Share Option schemes

The company formerly operated a number of equity settled, share-based compensation plans for employees. The fair value of the employee services received in exchange for the grant was recognised as an expense over the vesting period of the grant.

The fair value of employee services is determined by reference to the fair value of the awards granted calculated using an appropriate pricing model, excluding the impact of any non-market vesting conditions.

All these plans were closed during the year.

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS

**HISTORICAL COST PROFIT AND LOSS ACCOUNT
for the year ended 31 March 2007**

| | Notes | Appointed business 2007 £m | Non- appointed 2007 £m | Total 2007 £m | Appointed business 2006 £m | Non- appointed 2006 £m | Total 2006 £m |
|---|-------|-------------------------------------|---------------------------------|------------------------------|-------------------------------------|---------------------------------|---------------------|
| Turnover | 1 | 83.6 | 2.2 | 85.8 | 79.7 | 1.7 | 81.4 |
| Operating costs | 2 | (61.1) | (1.8) | (62.9) | (56.0) | (1.6) | (57.6) |
| Operating profit | | 22.5 | 0.4 | 22.9 | 23.7 | 0.1 | 23.8 |
| Other net income, being rents | | 0.4 | - | 0.4 | 0.4 | - | 0.4 |
| Other net interest payable and similar charges | 3 | (6.7) | - | (6.7) | (6.3) | - | (6.3) |
| Dividends on 8.75% irredeemable cumulative preference shares | 3 | (1.1) | - | (1.1) | (1.1) | - | (1.1) |
| Net finance income in respect of retirement benefit obligations | 3 | 1.5 | - | 1.5 | 0.9 | - | 0.9 |
| Profit on ordinary activities before taxation | | 16.6 | 0.4 | 17.0 | 17.6 | 0.1 | 17.7 |
| Taxation on profit on ordinary activities | 4 | (2.4) | (0.1) | (2.5) | (6.8) | - | (6.8) |
| Profit on ordinary activities after taxation | | 14.2 | 0.3 | 14.5 | 10.8 | 0.1 | 10.9 |
| Dividends on ordinary shares | 5 | (6.0) | (0.3) | (6.3) | (10.1) | (0.1) | (10.2) |
| Profit retained for the year | | 8.2 | - | 8.2 | 0.7 | - | 0.7 |

All of the turnover and operating costs above relate to continuing operations.

There is no difference between the profit on ordinary activities before taxation and the retained profit for the year stated above and their historical cost equivalents.

The accompanying notes to the accounts form an integral part of this statement.

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS

**STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
for the year ended 31 March 2007**

| | | Appointed Business | Non- Appointed Business | Total | Appointed Business | Non- appointed Business | Total |
|---|-------|-----------------------|-------------------------------|--------------|-----------------------|-------------------------------|-------------|
| | Notes | 2007 £m | 2007 £m | 2007 £m | 2006 £m | 2006 £m | 2006 £m |
| Profit attributable to Bristol Water plc shareholders | | 14.2 | 0.3 | 14.5 | 10.8 | 0.1 | 10.9 |
| Actuarial gains recognised in respect of retirement benefit obligations | 20 | 4.8 | - | 4.8 | 7.8 | - | 7.8 |
| Attributable deferred taxation | 16 | (1.3) | - | (1.3) | (2.1) | - | (2.1) |
| Charged against operating profit for equity-settled share- based payment | 22 | - | - | - | 0.2 | - | 0.2 |
| Attributable deferred taxation | 16 | - | - | - | 0.6 | - | 0.6 |
| Deferred tax asset reversal upon closure of equity-settled share based payment scheme | 16 | (0.6) | - | (0.6) | - | - | - |
| Total recognised gains for the year | | 17.1 | 0.3 | 17.4 | 17.3 | 0.1 | 17.4 |

The accompanying notes to the accounts form an integral part of this statement.

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS

**HISTORICAL COST BALANCE SHEET
at 31 March 2007**

| | Notes | Appointed business 2007 £m | Non- appointed 2007 £m | Total 2007 £m | Appointed business 2006 £m | Non- appointed 2006 £m | Total 2006 £m |
|--|-------|-------------------------------------|---------------------------------|-----------------------|-------------------------------------|---------------------------------|---------------------|
| Fixed assets | | | | | | | |
| Tangible fixed assets | 6 | 216.2 | 1.3 | 217.5 | 196.3 | 1.3 | 197.6 |
| Investment – loans to ultimate UK holding company | 7 | 68.5 | - | 68.5 | 68.5 | - | 68.5 |
| Current assets | | | | | | | |
| Stocks | 8 | 0.7 | 0.1 | 0.8 | 0.6 | 0.1 | 0.7 |
| Debtors | 9 | 20.7 | 0.1 | 20.8 | 19.0 | 0.1 | 19.1 |
| Cash at bank and on deposit | 12,21 | 30.8 | - | 30.8 | 40.5 | - | 40.5 |
| | | <u>52.2</u> | <u>0.2</u> | <u>52.4</u> | <u>60.1</u> | <u>0.2</u> | <u>60.3</u> |
| Creditors: amounts falling Due within one year | | | | | | | |
| Short-term borrowings | 10 | (2.5) | - | (2.5) | (2.5) | - | (2.5) |
| Other creditors | 11 | (22.6) | (1.5) | (24.1) | (17.7) | (1.5) | (19.2) |
| | | <u>(25.1)</u> | <u>(1.5)</u> | <u>(26.6)</u> | <u>(20.2)</u> | <u>(1.5)</u> | <u>(21.7)</u> |
| Net current assets/(liabilities) | | 27.1 | (1.3) | 25.8 | 39.9 | (1.3) | 38.6 |
| Total assets less current liabilities | | 311.8 | - | 311.8 | 304.7 | - | 304.7 |
| Creditors: amounts falling due after more than one year | | | | | | | |
| Long-term borrowings | 12 | (203.0) | - | (203.0) | (202.6) | - | (202.6) |
| Irredeemable debenture stocks | 12 | (1.6) | - | (1.6) | (1.6) | - | (1.6) |
| | | <u>(204.6)</u> | <u>-</u> | <u>(204.6)</u> | <u>(204.2)</u> | <u>-</u> | <u>(204.2)</u> |
| 8.75% irredeemable cumulative preference shares | 12 | (12.5) | - | (12.5) | (12.5) | - | (12.5) |
| Deferred income | 13 | (9.4) | - | (9.4) | (8.9) | - | (8.9) |
| Provisions for liabilities and charges | 16 | (21.1) | - | (21.1) | (20.8) | - | (20.8) |
| Retirement benefit obligations | 20 | 8.3 | - | 8.3 | 3.1 | - | 3.1 |
| Net assets | | <u>72.5</u> | <u>-</u> | <u>72.5</u> | <u>61.4</u> | <u>-</u> | <u>61.4</u> |
| Capital and reserves | | | | | | | |
| Called up share capital | 17 | 6.0 | - | 6.0 | 6.0 | - | 6.0 |
| Share premium account | 18 | 4.4 | - | 4.4 | 4.4 | - | 4.4 |
| Share option reserve | 18 | - | - | - | 0.8 | - | 0.8 |
| Other non-distributable reserves | 18 | 5.8 | - | 5.8 | 5.8 | - | 5.8 |
| Profit and loss account | 18 | 56.3 | - | 56.3 | 44.4 | - | 44.4 |
| Equity shareholders' funds | 18 | <u>72.5</u> | <u>-</u> | <u>72.5</u> | <u>61.4</u> | <u>-</u> | <u>61.4</u> |

The accounts were approved by a Committee of the Board on 13 July 2007 and signed on its behalf by -

A Parsons, Managing Director

A Nield, Finance Director

The accompanying notes to the accounts form an integral part of this statement.

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS

**HISTORICAL COST CASH FLOW STATEMENT
for the year ended 31 March 2007**

| | | Appointed business | Non- appointed | Total | Appointed business | Non- appointed | Total |
|---|-------|-----------------------|-------------------|----------------------|-----------------------|-------------------|---------------|
| | Notes | 2007 £m | 2007 £m | 2007 £m | 2006 £m | 2006 £m | 2006 £m |
| Net cash inflow from operating Activities | 21a | <u>41.8</u> | <u>0.4</u> | <u>42.2</u> | <u>33.1</u> | <u>0.3</u> | <u>33.4</u> |
| Returns on investments and servicing of finance - | | | | | | | |
| Other income received | | 0.4 | - | 0.4 | 0.4 | - | 0.4 |
| Interest received | | 6.0 | - | 6.0 | 5.3 | - | 5.3 |
| Interest paid on term loans and debentures | | (8.7) | - | (8.7) | (8.4) | - | (8.4) |
| Interest paid on finance leases | | (1.0) | - | (1.0) | (1.2) | - | (1.2) |
| Dividends paid on 8.75% irredeemable cumulative preference shares | | (1.1) | - | (1.1) | (1.1) | - | (1.1) |
| Net cost of issue of new loans | | - | - | - | (1.1) | - | (1.1) |
| | | <u>(4.4)</u> | <u>-</u> | <u>(4.4)</u> | <u>(6.1)</u> | <u>-</u> | <u>(6.1)</u> |
| Taxation - | | | | | | | |
| Corporation tax paid | | <u>(0.9)</u> | <u>(0.1)</u> | <u>(1.0)</u> | <u>(1.6)</u> | <u>(0.1)</u> | <u>(1.7)</u> |
| Capital expenditure and investing activities - | | | | | | | |
| Purchase of tangible fixed assets | | (28.6) | - | (28.6) | (13.7) | (0.1) | (13.8) |
| Less contributions received | | 3.5 | - | 3.5 | 4.2 | - | 4.2 |
| Infrastructure renewals expenditure | | (12.6) | - | (12.6) | (8.7) | - | (8.7) |
| Proceeds on disposal of tangible fixed assets | | - | - | - | 0.2 | - | 0.2 |
| Loan advanced to ultimate holding company | | - | - | - | (21.5) | - | (21.5) |
| | | <u>(37.7)</u> | <u>-</u> | <u>(37.7)</u> | <u>(39.5)</u> | <u>(0.1)</u> | <u>(39.6)</u> |
| Dividends paid on equity shares | | <u>(6.0)</u> | <u>(0.3)</u> | <u>(6.3)</u> | <u>(10.1)</u> | <u>(0.1)</u> | <u>(10.2)</u> |
| Net cash outflow before management of liquid resources and financing | | (7.2) | - | (7.2) | (24.2) | - | (24.2) |
| Management of liquid resources being decrease/(increase) in short-term deposits | | <u>11.5</u> | <u>-</u> | <u>11.5</u> | <u>(29.1)</u> | <u>-</u> | <u>(29.1)</u> |
| Financing - | | | | | | | |
| New term loans | | - | - | - | 57.0 | - | 57.0 |
| Capital element of lease repayments | | (2.2) | - | (2.2) | (1.9) | - | (1.9) |
| Loan repayments | | - | - | - | (1.8) | - | (1.8) |
| Payments in respect of swap liability | | (0.3) | - | (0.3) | (0.6) | - | (0.6) |
| Net cash (outflow)/inflow from financing | | <u>(2.5)</u> | <u>-</u> | <u>(2.5)</u> | <u>52.7</u> | <u>-</u> | <u>52.7</u> |
| Increase/(decrease) in cash | 21c | 1.8 | - | 1.8 | (0.6) | - | (0.6) |
| Cash, beginning of year | | 1.0 | - | 1.0 | 1.6 | - | 1.6 |
| Cash, end of year | | <u>2.8</u> | <u>-</u> | <u>2.8</u> | <u>1.0</u> | <u>-</u> | <u>1.0</u> |

The accompanying notes to the accounts form an integral part of this statement.

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS

NOTES TO THE ACCOUNTS

1. TURNOVER

Turnover is wholly derived from water supply and related activities in the United Kingdom. The maximum level of prices the company may levy for the majority of water charges is controlled by the Water Services Regulation Authority (Ofwat) through the RPI ± K price formula.

2. OPERATING COSTS

The directors believe that the nature of the company's business is such that the analysis of operating costs required by the Companies Act 1985 is not appropriate. As required by the Act the directors have therefore adapted the prescribed format so that disclosure of operating costs is appropriate to the company's principal business.

(a) Operating costs comprise -

| | 2007 | 2006 |
|---|-------------|-------------|
| | £m | £m |
| Wages, salaries and severance costs | 11.3 | 11.3 |
| Social security costs | 1.1 | 0.9 |
| Pension costs | 1.9 | 1.9 |
| Equity-settled share-based payments | - | 0.2 |
| Total payroll cost | <u>14.3</u> | <u>14.3</u> |
| less charged to fixed assets | (3.1) | (2.8) |
| Net payroll cost | <u>11.2</u> | <u>11.5</u> |
| Other operating costs | | |
| Operating lease rentals on plant and machinery | 0.1 | 0.2 |
| Research and development expenditure | 0.1 | 0.1 |
| Auditors' remuneration (note 2(e)) | 0.2 | 0.1 |
| Raw materials, consumables, bad debts and other charges less recoveries | 30.5 | 27.1 |
| Total other operating costs | <u>30.9</u> | <u>27.5</u> |
| Depreciation of tangible fixed assets (note 6) | | |
| On owned assets | 7.1 | 7.3 |
| On leased assets | 2.0 | 1.8 |
| Amortisation of related deferred income (note 13) | (0.3) | (0.3) |
| Net depreciation | <u>8.8</u> | <u>8.8</u> |
| Infrastructure renewals charge | 12.0 | 9.8 |
| Total operating costs | <u>62.9</u> | <u>57.6</u> |

The company has calculated the Infrastructure Renewals Charge, for regulatory accounting purposes only, over a fifteen year period. This is considered to be a reasonably long enough period over which to base the maintenance requirements of the company's infrastructure assets. There has been a change during 2006/07 to a forward looking span of fifteen years, instead of fifteen years beginning 2000/01, to achieve a charge which is more consistent year on year. A further change is the adjustment to bring the accrual at the end of 2020 to nil by incorporating the anticipated changes to the IRC following each five year regulatory period. In the statutory accounts, the infrastructure renewals charge included in depreciation, continues to be calculated based on infrastructure renewals expenditure for the current five year regulatory period, creating a difference with the operating costs in the regulatory accounts.

(b) Employee details -

The average number of employees (full time equivalents) during the year was as follows:

| | 2007 | 2006 |
|--|-------------|------|
| Water treatment and distribution | 224 | 215 |
| Support services | 92 | 101 |
| Administration | 35 | 37 |
| Recreations and other non-appointed activity | 50 | 46 |
| | 401 | 399 |

(c) Directors' emoluments -

| | 2007 | 2006 |
|--|-------------|------|
| | £m | £m |
| Aggregate emoluments of directors, being remuneration, bonus and benefits in kind | 0.9 | 1.0 |
| Payments to approved pension schemes, all in respect of executive directors | 0.1 | 0.1 |

Full details of directors' remuneration are disclosed in the report of the Remuneration Committee in the Statutory Annual Report and Accounts.

(d) Depreciation

The depreciation charge for the year is stated after charging £0.5m accelerated depreciation in respect of plant planned to be taken out of service before it is fully depreciated as part of a capital project to meet quality obligations and streamlining of treatment processes (2006 - £1.0m).

(e) Auditor's remuneration

| | 2007 | 2006 |
|--|---------------|--------|
| | £000's | £000's |
| The analysis of auditors' remuneration is as follows: | | |
| Fees payable to the company's auditors for the audit of the company's annual accounts | 48 | 39 |
| Other services pursuant to legislation | 98 | 24 |
| Tax services | 13 | 14 |
| Other services | 26 | 31 |
| Total non-audit fees | 137 | 69 |

Total non-audit fees payable in 2007 include £32,000 charged by the previous auditors.

3. OTHER NET INTEREST PAYABLE AND SIMILAR CHARGES

| | £m | 2007 £m | £m | 2006 £m |
|---|--------------------|--------------|--------------|--------------|
| Other net interest payable and similar charges relate to - | | | | |
| Bank borrowings | | 1.6 | | 1.7 |
| Term loans and debentures | - interest charges | 7.1 | | 6.8 |
| | - indexation | 2.9 | | 2.1 |
| Finance leases | | 1.0 | | 1.1 |
| | | <u>12.6</u> | | <u>11.7</u> |
| Less: | | | | |
| Loans to Bristol Water Group Ltd – interest receivable | (4.0) | | (3.7) | |
| Other external investments and deposits | <u>(1.9)</u> | | <u>(1.9)</u> | |
| | | <u>(5.9)</u> | | <u>(5.6)</u> |
| Fair value adjustment to swap liability | | 6.7 | | 6.1 |
| | | - | | 0.2 |
| Total other net interest payable and similar charges | | <u>6.7</u> | | <u>6.3</u> |
| Dividends on 8.75% irredeemable cumulative preference shares | | 1.1 | | 1.1 |
| Net finance income in respect of FRS 17 retirement benefit obligation | | (1.5) | | (0.9) |
| | | <u>6.3</u> | | <u>6.5</u> |

Dividends on the 8.75% irredeemable cumulative preference shares are payable at the fixed rate of 4.375% on 1 April and 1 October each year. Payment by the company to the share registrars is made two business days earlier. The payments are classified as interest in accordance with FRS 25.

4. TAXATION ON PROFIT ON ORDINARY ACTIVITIES

| | 2007 £m | 2006 £m |
|--|------------|------------|
| (a) Analysis of charge for the year, all arising in the United Kingdom: | | |
| Current tax: | | |
| Corporation tax at 30 % (2006 - 30%) | 2.4 | 3.4 |
| Advance Corporation Tax (ACT) previously recovered now written off | 0.5 | - |
| Adjustment to prior periods | (1.1) | (0.1) |
| | <u>1.8</u> | <u>3.3</u> |
| Deferred tax: | | |
| Current year movement | 2.7 | 2.8 |
| Adjustment to prior periods | 0.7 | 0.1 |
| Effect of discounting | (2.7) | 0.6 |
| | <u>0.7</u> | <u>3.5</u> |
| Tax on profit on ordinary activities | <u>2.5</u> | <u>6.8</u> |

In accordance with Ofwat guidelines, the overall tax charge is based on the charge in the statutory accounts and deferred tax has not been recalculated to take account of differences between the statutory and regulatory accounts.

The charge for corporation tax includes amounts which may be paid in consideration of group relief surrendered by other companies.

The ACT written off relates to a reduction in the claims made in prior years as a result of a review of the taxation of capitalised contributions. The ACT asset generated by the reduction in claims is written off on the grounds that it is not expected to be recovered in the foreseeable future.

Discount rates have increased during the current year. Within the effect of discounting £2.7m, £1.0m is in respect of the restatement of the opening balance at the new rates.

Factors that may affect future tax charges

ACT is recognised as an asset to the extent that it is foreseen to be recoverable in the next 12 months. There is a further £3.9m (2006 - £3.4m) of unrecognised ACT carried forward at 31 March 2007.

The company also holds £3.0m of unrecognised capital losses, which are available to offset against any future capital gains.

In the 2007 Budget the Chancellor announced a number of measures that will affect the future tax charges of the company. For consistency with the Statutory Annual Report and Accounts, at which date none of the measures had been enacted or substantially enacted, they are not reflected in these financial statements even though some of the measures have now been substantially enacted. However the effect of the main issues is disclosed below.

- Reduction in corporation tax rate to 28% with effect from 1 April 2008. This will affect the deferred tax liability recognised at 31 March 2008, which will be based on the new rate. Based on the deferred tax liability stated within the 2007 accounts, the restatement of the overall liability as at 31 March 2007 will reduce the 2008 deferred tax charge by £2.6m before discounting (discounted: £1.5m).

- The abolition of industrial buildings allowances ('IBA') from 1 April 2011 was announced in the 2007 Budget but was not incorporated in the 2007 Finance Bill. Accordingly it is not expected to be enacted until June/July 2008 and if enacted would be reflected in the 2007/08 financial statements. However, under FRS 19, the withdrawal of the IBA pool must be recognised on 1 April 2007. The effect of the withdrawal of the IBA pool together with the reclassification of appropriate fixed assets as non-qualifying is expected to reduce the deferred tax liability stated as at 31 March 2007 by approximately £1m before discounting (discounted £0.2m reflecting the long term nature of the relief). However, it should be noted that the company will lose future allowance claims totalling £6.0m in respect of industrial buildings expenditure up to 31 March 2007.
- The capital allowance rates attributable to the plant and machinery pools are to be revised from 25% and 6% to 20% and 10% respectively. The withdrawal of industrial buildings allowances will be done by reducing the claimable allowances by 1% each year from 1 April 2008. These changes were also not incorporated into the 2007 Finance Bill and are not expected to be enacted until June/July 2008. The 2008 current tax charge will not be materially effected by the changes in relief, based on the claims expected in that year on the pools held at 31 March 2007.

(b) **Reconciliation of the current tax charge**

The current tax rate for the year is lower (2006 - lower) than the standard rate of Corporation Tax in the United Kingdom (30%). The differences are explained below:

| | 2007 | 2006 |
|---|-------------------|------------|
| | £m | £m |
| Profit on ordinary activities before tax | <u>17.0</u> | 17.7 |
| Profit on ordinary activities multiplied by standard rate of Corporation Tax in the United Kingdom at 30% (2006 - 30%) | 5.1 | 5.3 |
| Effects of: | | |
| Differences between profit in regulatory accounts compared to Statutory Annual Report and Accounts which have no associated tax charge/credit | 0.6 | 0.2 |
| Expenses, including 8.75% irredeemable cumulative preference share dividends, not deductible for tax | 0.5 | 0.4 |
| Capital allowances in excess of depreciation | (1.6) | (0.9) |
| Additional retirement benefit contributions | (1.0) | (1.2) |
| Tax credit arising on closure of equity settled share based payment scheme | (1.0) | - |
| Other net charges | (0.2) | (0.4) |
| | <u>2.4</u> | 3.4 |
| Adjustment to tax in respect of prior periods | (1.1) | (0.1) |
| Adjustment in respect of Advance Corporation Tax for prior years | 0.5 | - |
| Total current tax charge | <u>1.8</u> | <u>3.3</u> |

5. DIVIDENDS IN RESPECT OF ORDINARY SHARES

| | 2007 £m | 2006 £m |
|--|------------|-------------|
| Dividends paid | | |
| • Dividend in respect of 2004/05: Final dividend of 88.00 pence per share approved at the Annual General Meeting on 18 July 2005 | - | 5.3 |
| • Dividend in respect of 2005/06: First interim dividend of 19.62 pence per share, approved by the Board on 29 September 2005 | - | 1.2 |
| Second interim dividend of 38.68 pence per share, approved by the Board on 8 December 2005 | - | 2.3 |
| Third interim dividend of 23.53 pence per share, approved by the Board on 28 March 2006 | - | 1.4 |
| Fourth and final dividend of 58.02 pence per share, approved by the Board on 16 May 2006 | 3.5 | - |
| • Dividend in respect of 2006/07: First interim dividend of 23.60 pence per share, approved by the Board on 28 September 2006 | 1.4 | - |
| Second interim dividend of 23.47 pence per share, approved by the Board on 22 March 2007 | 1.4 | - |
| | 6.3 | 10.2 |

On 31 May 2007 the Board proposed a final dividend of 100.03 pence per share, totalling £6.0m, in respect of the year ended 31 March 2007. In accordance with FRS 21 this dividend is not recognised in these accounts as a liability.

Dividend policy

The company policy is to pay an annual level of ordinary dividends comprising:

- A base level reflecting the cost of capital allowed by Ofwat in the 5-year determination of price limits, adjusted to reflect actual gearing levels and where appropriate actual performance relative to Ofwat's assumptions.
- An amount equal to the post-tax interest receivable from Bristol Water Group Ltd (the ultimate UK parent company) in respect of intercompany loans.

During the year ordinary dividend payments were:

- Base level – fourth interim and final dividend in respect of the 2005/06 trading year of £3.5m.
- Interim dividends for 2006/07 in respect of the intercompany loan interest element of £2.8m.

6. TANGIBLE FIXED ASSETS

(a) The movements for the year comprise –

| | Freehold land & operational structures £m | Plant and equipment £m | Infra- structure assets £m | Assets under construction £m | Total £m |
|--|---|------------------------------|-------------------------------------|---------------------------------------|--------------|
| Cost | | | | | |
| At 1 April 2006 | 161.5 | 28.6 | 85.9 | 4.8 | 280.8 |
| Additions | - | - | - | 32.9 | 32.9 |
| Capitalisation of completed assets | 3.6 | 2.5 | 4.1 | (10.2) | - |
| Disposals | (0.1) | (1.1) | - | - | (1.2) |
| Grants and contributions | (0.1) | - | (3.8) | - | (3.9) |
| At 31 March 2007 | 164.9 | 30.0 | 86.2 | 27.5 | 308.6 |
| Depreciation | | | | | |
| At 1 April 2006 | 64.4 | 18.8 | - | - | 83.2 |
| Charge for year | 5.9 | 3.2 | - | - | 9.1 |
| Disposals | (0.1) | (1.1) | - | - | (1.2) |
| At 31 March 2007 | 70.2 | 20.9 | - | - | 91.1 |
| Net book value at 31 March 2007 | 94.7 | 9.1 | 86.2 | 27.5 | 217.5 |
| At 31 March 2006 | 97.1 | 9.8 | 85.9 | 4.8 | 197.6 |

Assets under construction include all expenditure on plant, vehicles and other assets up to the point at which they are brought into use upon completion.

(b) Included above at 31 March 2007 is freehold land, not subjected to depreciation in the year, of £1.3m (2006 - £1.3m).

(c) Included above at 31 March 2007 are fixed assets held under finance leases analysed by asset type as follows -

| | Freehold land & operational structures £m | Plant and equipment £m | Infra- structure assets £m | Total £m |
|-------------------------|--|------------------------------|-------------------------------------|-------------|
| At 31 March 2007 | | | | |
| Cost | 37.9 | 6.9 | 1.2 | 46.0 |
| Depreciation | (20.1) | (6.6) | - | (26.7) |
| Net book value | 17.8 | 0.3 | 1.2 | 19.3 |
| At 31 March 2006 | | | | |
| Cost | 38.0 | 7.7 | 1.2 | 46.9 |
| Depreciation | (18.0) | (7.2) | - | (25.2) |
| Net book value | 20.0 | 0.5 | 1.2 | 21.7 |

(d) The net book value of infrastructure assets is stated after the deduction of contributions of £46.6m (2006 - £44.7m) as explained in Accounting Policy d.

7. INVESTMENT - LOANS TO BRISTOL WATER GROUP LTD

| | 2007 | 2006 |
|----------------------|-------------|------|
| | £m | £m |
| At 1 April 2006 | 68.5 | 47.0 |
| Advanced during year | - | 21.5 |
| At 31 March 2007 | 68.5 | 68.5 |

The loans were advanced to Bristol Water Group Ltd and details are as follows:

| Agreement date | Loan advance date | Fixed interest rate | Loan repayment date | Principal Outstanding £m |
|-----------------|-------------------|---------------------|---------------------|--------------------------|
| 4 December 2003 | 12 February 2004 | 6.042% | 30 September 2033 | 47.0 |
| 10 June 2005 | 13 July 2005 | 5.550% | 30 September 2032 | 21.5 |

8. STOCKS

Stocks comprise consumable stores. The replacement cost of stocks is not considered to be materially different from their carrying value in the balance sheet.

9. DEBTORS

| Debtors comprise - | 2007 | 2006 |
|---|-------------|------|
| | £m | £m |
| Trade debtors | 9.0 | 8.2 |
| Due from group and associated companies | 1.5 | 2.0 |
| Other debtors | 1.7 | 1.2 |
| Prepayments and accrued income | 8.6 | 7.7 |
| | 20.8 | 19.1 |

The sum of £0.4m (2006 - £0.4m) is included within the heading "Due from group and associated companies" in respect of amounts advanced to Bristol Wessex Billing Services Limited, a joint venture company within the BWG group, to fund the purchase of fixed assets. This amount has no fixed repayment date.

10. CREDITORS – SHORT TERM BORROWINGS FALLING DUE WITHIN ONE YEAR

| | 2007 | 2006 |
|---------------------------------------|-------------|------|
| | £m | £m |
| Finance leases | 2.5 | 2.2 |
| Financial derivative - swap liability | - | 0.3 |
| | 2.5 | 2.5 |

All borrowings due within one year are unsecured.

11. OTHER CREDITORS DUE WITHIN ONE YEAR

| Other creditors due within one year comprise - | 2007 | 2006 |
|--|-------------|------|
| | £m | £m |
| Receipts in advance | 8.0 | 7.2 |
| Trade creditors | 7.5 | 3.5 |
| Due to group and associated companies | 0.5 | 1.7 |
| Tax, social security and payroll deductions | 0.7 | 0.6 |
| Corporation tax payable | 1.5 | 0.4 |
| Accruals and deposits received | 5.9 | 5.8 |
| | 24.1 | 19.2 |

12. CREDITORS – AMOUNTS FALLING DUE AFTER ONE YEAR

| | 2007 £m | 2006 £m |
|--|--------------|--------------|
| Bank and other term loans – all secured | 180.7 | 177.5 |
| Debentures | 1.6 | 1.6 |
| Finance leases | 17.5 | 20.1 |
| Net unamortised debt issue premiums/(issue costs) arising on issue of term loans | 4.8 | 5.0 |
| Total excluding 8.75% irredeemable cumulative preference shares | <u>204.6</u> | 204.2 |
| 8.75% irredeemable cumulative preference shares | 12.5 | 12.5 |
| Total | <u>217.1</u> | <u>216.7</u> |

The 8.75% irredeemable cumulative preference shares, which do not carry any voting rights, were issued in 1992 at £1 per share. Shareholders are entitled to receive dividends at 8.75% per annum on the par value of these shares on a cumulative basis; these dividends are payable half yearly on 1 April and 1 October. On winding up, the preference shareholders rank ahead of ordinary shareholders and are entitled to receive £1 per share and any dividends accrued but unpaid in respect of their shares. In the event that dividends on the preference shares are in arrears for six months or more, holders of the preference shares become entitled to vote at general meetings of members. In accordance with FRS25 the shares are classified as long-term debt.

The authorised preference share capital consists of 14,000,000 8.75% irredeemable cumulative preference shares of £1 each. Of these, 12,500,000 have been issued and are fully paid (31 March 2006: 12,500,000).

New borrowings

There were no new borrowings during the year.

The movements in unamortised debt issue premiums/(issue costs) were as follows:

| | 2007 £m | 2006 £m |
|---|------------|------------|
| Professional fees and expenses | - | (0.5) |
| Payment to bank under terms of gilt locks entered into prior to and in connection with loans raised | - | (0.6) |
| Net premiums on receipt of new loans | - | 6.8 |
| Net premiums of issue arising in the year | <u>-</u> | 5.7 |
| Unamortised premiums/(issue costs) at beginning of the year | 5.0 | (0.6) |
| Amortised during the year | (0.2) | (0.1) |
| Unamortised premiums at end of the year | <u>4.8</u> | <u>5.0</u> |

The net premiums/(costs) of issue of new loans are amortised over the terms of the respective loans at £0.2m credit per annum. Amortisation credits due in future years are as follows:

| | 2007 £m | 2006 £m |
|----------------------------|------------|------------|
| Within one year | 0.2 | 0.2 |
| Between one and two years | 0.2 | 0.2 |
| Between two and five years | 0.6 | 0.6 |
| After five years | 3.8 | 4.0 |
| | <u>4.8</u> | <u>5.0</u> |

Security for borrowings

The majority of the company's financial liabilities are secured. The security is given:

In respect of the company:

- by way of first fixed charges over any of its freehold or leasehold property belonging to it now or acquired in the future (other than protected land under the Water Industry Act 1991), its present and future goodwill, all rights and claims in relation to charged bank accounts, all book debts, all insurances, all rights, title and interest to all investments and all plant and machinery, and
- a floating charge over the whole of its undertaking.

Prior to enforcement of the security by the lender, the company is entitled to exercise all its rights, and perform its obligations in relation to the charged assets in accordance with the provisions set out in the Security and Intercreditor Deed.

In respect of Bristol Water Core Holdings Ltd (the immediate parent of Bristol Water plc), as security for the obligations of the company:

- a fixed charge over its shares in the company together with a floating charge over the whole of its undertaking.

Net borrowings and maturities

At 31 March 2007 net borrowings comprise -

| | Term loans less cash | Finance leases | Debentures and irredeemable preference shares | Total 2007 | Total 2006 |
|---|-------------------------------|-------------------|--|-----------------------|---------------|
| | £m | £m | £m | £m | £m |
| Repayment due: | | | | | |
| Between one and two years | 25.0 | 1.9 | - | 26.9 | 2.5 |
| Between two and five years | - | 8.1 | - | 8.1 | 31.6 |
| After five years: | | | | | |
| Other than by instalment – term loans | | | | | |
| Secured, repayable 2032, principal index-linked to RPI, fixed interest at 3.635%* on the indexed principal | 98.2 | - | - | 98.2 | 95.0 |
| Secured, repayable 2033, fixed interest at 6.01%* | 57.5 | - | - | 57.5 | 57.5 |
| By instalments | | | | | |
| Finance leases | - | 7.5 | - | 7.5 | 11.0 |
| Net unamortised debt issue premiums/ (issue costs) | 4.8 | - | - | 4.8 | 5.0 |
| Debentures (listed on the London Stock Exchange) - | - | - | | | |
| 4.00% Consolidated irredeemable 4.25%, 4.00% and 3.50% perpetual irredeemable debentures (in total, each under £0.1m individually) | - | - | 1.4 | 1.4 | 1.4 |
| | - | - | 0.2 | 0.2 | 0.2 |
| Total borrowings due after one year excluding 8.75% irredeemable cumulative preference shares | 185.5 | 17.5 | 1.6 | 204.6 | 204.2 |
| Current portion of debt | - | 2.5 | - | 2.5 | 2.2 |
| Current portion of swap liability | - | - | - | - | 0.3 |
| | 185.5 | 20.0 | 1.6 | 207.1 | 206.7 |
| Cash balances and short-term deposits | (30.8) | - | - | (30.8) | (40.5) |
| Net borrowings excluding 8.75% irredeemable cumulative preference shares | 154.7 | 20.0 | 1.6 | 176.3 | 166.2 |
| 8.75% irredeemable cumulative preference shares | - | - | 12.5 | 12.5 | 12.5 |
| Net borrowings including 8.75% irredeemable cumulative preference shares | 154.7 | 20.0 | 14.1 | 188.8 | 178.7 |

*Coupons as specified in loan documentation. At the time of pricing of these loans, premia/discounts were determined to reflect prevailing market conditions. The net premia/discounts are included in unamortised issue costs as set out above.

Borrowing facilities

Unutilised borrowing facilities as at 31 March are as follows:

| | 2007 | 2006 |
|---------------------------------|-------------|------|
| | £m | £m |
| Expiring in more than two years | 30.0 | 30.0 |

The facilities are floating rate and incur non-utilisation fees at market rates.

Minimum lease payments under finance leases

Amounts fall due as follows:

| | 2007 | 2006 |
|----------------------------|-------------|------|
| | £m | £m |
| Within one year | 2.5 | 2.2 |
| Between one and two years | 1.9 | 2.5 |
| Between two and five years | 8.1 | 6.6 |
| After five years | 7.5 | 11.0 |
| | 20.0 | 22.3 |

13. DEFERRED INCOME

Deferred income represents grants and contributions received in respect of non-infrastructure assets less amounts amortised to the profit and loss account.

| | 2007 | 2006 |
|------------------------|--------------|-------|
| | £m | £m |
| Beginning of year | 8.9 | 8.6 |
| Contributions received | 0.8 | 0.6 |
| Less amortised | (0.3) | (0.3) |
| End of year | 9.4 | 8.9 |

14. FINANCIAL RISK MANAGEMENT

Full disclosure is given in note 14 "Financial Risk Management" of the Statutory Annual Report and Accounts. The non-appointed element of the company is not significant in respect of this note.

15. FINANCIAL INSTRUMENTS

Full disclosure is given in note 15 "Financial Instruments" of the Statutory Annual Report and Accounts. The non-appointed element of the company is not significant in respect of this note.

16. PROVISIONS FOR LIABILITIES AND CHARGES

| | 2007 | 2006 |
|--|---------------|--------|
| | £m | £m |
| (a) Deferred tax (excluding deferred tax on retirement benefit obligations) – note 16 (b) | 19.7 | 18.8 |
| Infrastructure accrual – note 16 (c) | 1.4 | 2.0 |
| | 21.1 | 20.8 |
| (b) Provision for deferred tax comprises - | | |
| Accelerated capital allowances and capital element of finance leases | 38.5 | 36.7 |
| Deferred income | (2.0) | (2.5) |
| Short term timing differences | (1.1) | (1.7) |
| Arising on equity-settled share based payments | - | (0.6) |
| Retirement benefit obligations | 3.3 | 1.3 |
| | 38.7 | 33.2 |
| Effect of discounting: | | |
| Retirement benefit obligations | (0.3) | - |
| Other | (15.7) | (13.1) |
| | (16.0) | (13.1) |
| Net provision, including deferred tax on retirement benefit obligations | 22.7 | 20.1 |
| Less, attributable to retirement benefit obligations | (3.0) | (1.3) |
| Net provision, excluding deferred tax on retirement benefit obligations | 19.7 | 18.8 |
| Deferred tax movement: | 2007 | 2006 |
| | £m | £m |
| Beginning of year | 20.1 | 15.1 |
| Charge to Profit and Loss Account (note 4) | 0.7 | 3.5 |
| Charge to Statement of Total Recognised Gains and Losses in respect of pension actuarial gains in the year | 1.3 | 2.1 |
| Charge to Statement of Total Recognised Gains and Losses in respect of equity-settled share based payment | - | (0.6) |
| Credit to share options reserve | 0.6 | - |
| Provision carried forward at 31 March | 22.7 | 20.1 |
| (c) Infrastructure accrual | | |
| The movement on the infrastructure renewals account is as follows: | | |
| | 2007 | 2006 |
| | £m | £m |
| Beginning of year | 2.0 | 0.9 |
| Charge for the year | 12.0 | 9.8 |
| Expenditure | (12.6) | (8.7) |
| End of year | 1.4 | 2.0 |

17. CALLED UP ORDINARY SHARE CAPITAL

The authorised and issued ordinary share capital of the company is

| | Authorised | | Issued and fully paid | |
|--------------------------------------|------------|------------|-----------------------|------------|
| | 2007 £m | 2006 £m | 2007 £m | 2006 £m |
| 5,998,025 ordinary shares of £1 each | 6.0 | 6.0 | 6.0 | 6.0 |

18. MOVEMENT IN SHAREHOLDERS' FUNDS

| | Share capital | Share premium account | Share option reserve | Capital redemption reserve | Profit and loss | Total 2007 | Total 2006 |
|--|---------------|-----------------------|----------------------|----------------------------|-----------------|--------------|------------|
| | £m | £m | £m | £m | £m | £m | £m |
| Beginning of year | 6.0 | 4.4 | 0.8 | 5.8 | 44.4 | 61.4 | 54.2 |
| Regulatory profit for year | - | - | - | - | 14.5 | 14.5 | 10.9 |
| Actuarial gains recognised in respect of retirement benefit obligations | - | - | - | - | 4.8 | 4.8 | 7.8 |
| Attributable deferred taxation | - | - | - | - | (1.3) | (1.3) | (2.1) |
| Charged against operating profit for equity-settled share based payment | - | - | - | - | - | - | 0.2 |
| Attributable deferred taxation | - | - | - | - | - | - | 0.6 |
| Deferred tax asset written off upon closure of equity-settled share based payment scheme | - | - | (0.6) | - | - | (0.6) | - |
| Transfer arising on closure of equity-settled share based payment scheme | - | - | (0.2) | - | 0.2 | - | - |
| Dividends | - | - | - | - | (6.3) | (6.3) | (10.2) |
| Shareholders funds per regulatory accounts | 6.0 | 4.4 | - | 5.8 | 56.3 | 72.5 | 61.4 |

Details of the irredeemable cumulative preference shares are set out in note 12.

19. COMMITMENTS AND CONTINGENCIES

(a) Capital commitments at 31 March 2007 contracted for but not provided were £14.9m (2006 - £7.7m). The increase is due to the large number of new capital projects now in progress within the framework of the 2005/10 regulatory settlement.

(b) The company has the following non-cancellable operating lease commitments in respect of plant and machinery payable during the next financial year -

| | 2007 £m | 2006 £m |
|-----------------------------|------------|------------|
| Operating leases expiring - | | |
| Within one to two years | 0.1 | 0.1 |
| Within two to five years | - | 0.1 |
| | 0.1 | 0.2 |

(c) Contingencies - The company is a member of a VAT group and is jointly liable for the VAT liabilities of Bristol Water Group plc and certain other companies within the Bristol Water Group Ltd group. Other than as shown in these accounts the directors are not aware of any other contingent liabilities that require disclosure.

20. RETIREMENT BENEFIT OBLIGATIONS

Full disclosure is given in note 21 "Retirement Benefit Obligations" of the Statutory Annual Report and Accounts. The non-appointed element of the company is not significant in respect of this note.

21. ADDITIONAL INFORMATION TO THE CASH FLOW STATEMENT

(a) Reconciliation of operating profit to net cash inflow from operating activities -

| | 2007 | 2006 |
|--|--------------|-------|
| | £m | £m |
| Operating profit | 22.9 | 23.8 |
| Depreciation | 8.8 | 8.8 |
| Difference between pension charges and normal contributions | 0.5 | 0.6 |
| Equity-settled share based payments | - | 0.2 |
| Infrastructure Renewals Charge | 12.0 | 9.8 |
| Cash flow from operations | 44.2 | 43.2 |
| Working capital movements - | | |
| Stocks | (0.1) | (0.1) |
| Debtors | (1.8) | (0.5) |
| Creditors and provisions | 0.9 | (0.7) |
| Additional contributions to pension scheme, including payments in respect of restructuring | (1.0) | (8.5) |
| Net cash inflow from operating activities | 42.2 | 33.4 |

(b) Reconciliation of net cash flow to movement in net borrowings -

| | 2007 | 2006 |
|---|----------------|---------|
| | £m | £m |
| Increase/(decrease) in net cash in year | 1.8 | (0.6) |
| Cash used to repay borrowings | 2.5 | 4.3 |
| Cash from new borrowings | - | (57.0) |
| Net costs of issue of loans | - | 1.1 |
| Cash from (decrease)/increase in short term deposits | (11.5) | 29.1 |
| | (7.2) | (23.1) |
| New debt increase not affecting cash flow | (2.9) | (2.3) |
| Net borrowings at beginning of year including 8.75% irredeemable cumulative preference shares | (178.7) | (153.3) |
| Net borrowings at end of year including 8.75% irredeemable cumulative preference shares | (188.8) | (178.7) |

(c) Analysis of changes in net borrowings during the year -

| | Opening net borrowings £m | Cash flows in year £m | Maturity profile £m | New debt not affecting cash flow* £m | Closing net Borrowings £m |
|--|------------------------------------|--------------------------------|---------------------------|---|---------------------------------|
| Cash at bank | 1.0 | 1.8 | - | - | 2.8 |
| Short term deposits | 39.5 | (11.5) | - | - | 28.0 |
| <hr/> | | | | | |
| Cash at bank including overnight deposits | 40.5 | (9.7) | - | - | 30.8 |
| Swap liability due within one year | (0.3) | 0.3 | - | - | - |
| Borrowings due within one year | (2.2) | 2.2 | (2.5) | - | (2.5) |
| Borrowings due after one year, including 8.75% irredeemable cumulative preference shares and unamortised premiums/(issue costs) in respect of loans | (216.7) | - | 2.5 | (2.9) | (217.1) |
| <hr/> | | | | | |
| Net borrowings including 8.75% irredeemable cumulative preference shares | (178.7) | (7.2) | - | (2.9) | (188.8) |

* Represents indexation of term loans less amortisation of net premia on borrowings

22. SHARE-BASED PAYMENTS

Full disclosure is given in note 23 "Share-Based Payments" of the Statutory Annual Report and Accounts. The non-appointed element of the company is not significant in respect of this note.

23. RELATED PARTY TRANSACTIONS

Related parties include members and joint ventures of the BWG group of companies, members of the Agbar group of companies and key management personnel. The principal related parties are:

Sociedad General de Aguas de Barcelona S.A. (Agbar), registered in Spain and since June 2006 the ultimate parent company of Bristol Water plc.

Bristol Water Group Ltd, registered in England and Wales, whose year-end is 31 December, is the ultimate UK holding company of Bristol Water plc and is a subsidiary of Agbar.

Bristol Wessex Billing Services Limited (BWBSL), registered in England and Wales, whose year-end is 31 March. The joint venture interest is held by Bristol Water Holdings Limited, a fellow subsidiary and intermediate holding company within the BWG group, which owns 100 class 'B' shares in the company, representing a holding of 50% of the voting and equity rights of the company. BWBSL has contracted to provide billing and customer services to both Bristol Water plc and Wessex Water Services Limited, under a cost sharing arrangement. Costs are shared in proportion to business activity.

Basis of cost allocations used for management charges and allocations between the appointed and non-appointed businesses of Bristol Water plc

Costs are attributed to appropriate cost centres in the company's accounting system, which are identified as regulated or non-regulated. The majority of non-regulated costs are incurred directly with the remainder allocated on a time apportionment basis.

Services received/supplied by the regulated business from associated companies in excess of £100,000 -

| Nature of service | Associate | Turnover of associate | Terms of supply | Value of service received | Value of service supplied |
|--------------------------------|--|-----------------------|--------------------|---------------------------|---------------------------|
| | | £m | | £m | £m |
| Management charge | Bristol Water Holdings plc/ Bristol Water Group plc | 0.2 | At cost | 0.2 | 0.1 |
| Insurance costs passed through | Bristol Water Group plc | 0.2 | At cost | 1.0 | - |
| Managed Billing Service | Bristol Wessex Billing Services Ltd | 10.7 | Competitive tender | 2.0 | - |
| Recharge of court costs | Bristol Wessex Billing Services Ltd | 10.7 | At cost | 0.2 | - |

Group Tax Relief

Bristol Water plc claims group tax relief on losses surrendered from other companies in the Bristol Water Group. The amount of the group relief claim for 2006/07 is not yet ascertained. In the 2005/06 computations the group relief surrendered was £4.5m. Bristol Water plc pays the standard tax rate (currently 30%) of the surrendered losses to the surrendering company, producing a nil net effect on the tax charge in Bristol Water plc.

Agbar ex-gratia payments

As part of the acquisition of Bristol Water Group plc (BWG) by Agbar, BWG's SAYE share option scheme was terminated and Bristol Water plc employees were able to exercise their options. Because of the early termination some share options lapsed. To compensate for this Agbar agreed, subject to conditions, to make a series of ex-gratia payments to employees. The first of these payments was made in September 2006 and for administrative services was paid through the Bristol Water payroll at a total cost of c£0.5m. Agbar made a payment to Bristol Water plc to fully meet this cost prior to the payroll date. Further payments will be made over the next few years, payments will be made through the Bristol Water plc payroll and will be fully reimbursed by Agbar.

Pensions

Pension arrangements for the majority of the company's employees are provided through the company's membership of the Water Companies' Pension Scheme (WCPS), which provides defined benefits based on final pensionable pay.

In addition to providing benefits to employees and ex-employees of Bristol Water plc, the section provides benefits to employees and ex-employees of Bristol Water Holdings Ltd and former Bristol Water plc employees who transferred to Bristol Wessex Billing Services Ltd. The majority of the section assets and liabilities relate to Bristol Water plc employees and ex-employees.

BWG also provides pensions through a separate pension section of the WCPS for its previous non-regulated activities. A review with the scheme administrator/trustee is in process, of transfers of staff between the sections, to ensure that appropriate transfer values are made between the two sections of WCPS.

To the best of the directors' knowledge, all appropriate material transactions with associated companies have been disclosed.

| Balances outstanding at year end | Amounts due from | | Amounts due to | |
|---|------------------|------|----------------|------|
| | 2007 | 2006 | 2007 | 2006 |
| | £m | £m | £m | £m |
| Members of the BWG group | | | | |
| Bristol Water Group plc | 0.1 | - | 0.1 | 0.9 |
| Bristol Water Services Ltd | - | - | - | 0.1 |
| Verdan Group Ltd | - | - | - | 0.4 |
| Joint ventures of the BWG group | | | | |
| Bristol Wessex Billing Services Limited (BWBSL) | 1.4 | 2.0 | 0.4 | 0.3 |
| | 1.5 | 2.0 | 0.5 | 1.7 |

The amounts due from BWBSL are mainly cash in transit.

Bristol Water plc advanced £0.1m to BWBSL during the year for the purchase of fixed assets, mainly property improvements. Bristol Water plc also paid Wessex Water plc £0.4m (2006: £0.1m) for a share of other assets used operationally by BWBSL but capitalised by Bristol Water plc.

The amounts outstanding are unsecured and will be settled in cash. No guarantees have been given or received. No provisions have been made, or are considered necessary, for doubtful debts in respect of the amounts due from related parties.

Borrowing / lending with associated companies and related facilities -

A loan of £47m was made to Bristol Water Group Limited (ultimate parent company until June 2006) in 2003/04. The unsecured loan was advanced on 12 February 2004, under an agreement dated 4 December 2003, out of the proceeds of the new Artesian loans entered into during the year. The loan is due for repayment on 30 September 2033 and bears a fixed interest rate of 6.042%. Interest income of £2.8m was received in relation to the loan during 2006/07.

A further loan of £21.5m was made to Bristol Water Group Limited, in 2005/06. The unsecured loan was advanced on 13 July 2005, under an agreement dated 10 June 2005, out of proceeds of the new Artesian loan entered into in that year. The loan is due for repayment on 30 September 2032 and bears a fixed interest rate of 5.55%. Interest income of £1.2m was received in relation to the loan in 2006/07.

Dividends paid to parent company

Details on dividend policy and dividends paid in respect of ordinary shares are set out in note 5.

Remuneration of key management personnel

Information about the remuneration of individual directors is provided in the audited part of the Remuneration Committee Report in the Statutory Annual Report and Accounts, and in Note 2.

24. ULTIMATE PARENT COMPANY AND RELATED PARTY TRANSACTIONS

At 31 March 2007 the ultimate UK parent and controlling company was Bristol Water Group Ltd. The ultimate holding company is believed by the Directors to be Sociedad General de Aguas de Barcelona S.A. (Agbar), a company incorporated in Spain.

At the 31 March 2007 approximately 49.7% of the share capital of Agbar was controlled by the French group Suez and the Spanish bank La Caixa. In April 2007 Suez, La Caixa and their joint venture Hisusa undertook to make a bid for the entire share capital of Agbar. They had already secured a further 6.7% through an irrevocable undertaking. The necessary regulatory approvals are currently being sought. The outcome of this bid may change the identity of Bristol Water plc's ultimate holding company. Ofwat are also monitoring the position in respect of Condition P of Bristol Water's Instrument of Appointment as a water undertaker and the undertakings required from the ultimate parent.

25. AUDITORS

Following the acquisition of Bristol Water Group plc by Agbar during the year, PricewaterhouseCoopers LLP resigned as auditors and Deloitte & Touche LLP were appointed in their place.

BRISTOL WATER plc
APPOINTED BUSINESS

REGULATORY ACCOUNTING STATEMENTS

CURRENT COST ACCOUNTING STATEMENTS
for the year ended 31 March 2007

BRISTOL WATER plc**REGULATORY ACCOUNTING STATEMENTS****CURRENT COST PROFIT AND LOSS ACCOUNT FOR THE APPOINTED BUSINESS
for the year ended 31 March 2007**

| | Notes | 2007 £m | 2006 £m |
|---|-------|---------------|------------|
| Turnover | C3 | 83.6 | 79.7 |
| Current cost operating costs | C4 | (67.4) | (61.8) |
| Working capital adjustment | | (0.1) | - |
| Current cost operating profit | | 16.1 | 17.9 |
| Other income | | 0.4 | 0.4 |
| Net interest payable and similar charges | | (6.7) | (6.3) |
| Dividends on 8.75% irredeemable cumulative preference shares | | (1.1) | (1.1) |
| Net finance income in respect of retirement benefit obligations | | 1.5 | 0.9 |
| Financing adjustment | | 5.4 | 3.2 |
| Current cost profit before taxation | | 15.6 | 15.0 |
| Taxation | | | |
| Current tax | | (1.8) | (3.3) |
| Deferred tax | | (0.6) | (3.5) |
| Current cost profit on ordinary activities | | 13.2 | 8.2 |
| Dividends on ordinary shares | | (6.0) | (10.1) |
| Current cost profit/(loss) retained | | 7.2 | (1.9) |

The accompanying notes to the accounts form an integral part of this statement.

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS

**CURRENT COST STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
for the year ended 31 March 2007**

| | 2007 | 2006 |
|---|--------------|-------|
| | £m | £m |
| Current cost profit on ordinary activities | 13.2 | 8.2 |
| Actuarial gains recognised in respect of retirement benefit obligations | 4.8 | 7.8 |
| Attributable deferred taxation | (1.3) | (2.1) |
| Charged against operating profit for equity-settled share-based payment | - | 0.2 |
| Attributable deferred taxation | - | 0.6 |
| Deferred tax asset reversal upon closure of equity-settled share based payment scheme | (0.6) | - |
| Total current cost recognised gains for the year | 16.1 | 14.7 |

The accompanying notes to the accounts form an integral part of this statement.

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS

**CURRENT COST BALANCE SHEET
FOR THE APPOINTED BUSINESS
at 31 March 2007**

| | Notes | 2007 £m | 2006 Restated £m |
|--|-------|----------------|------------------------|
| Fixed assets | | | |
| Tangible fixed assets | C5 | 1,724.7 | 1,628.9 |
| Third party contributions since 1 April 1990 | | (73.2) | (65.6) |
| | | <u>1,651.5</u> | <u>1,563.3</u> |
| Working capital | | | |
| Cash | C6 | (0.4) | 2.2 |
| Short term deposits | | 2.8 | 1.0 |
| Bank overdrafts | | 28.0 | 39.4 |
| Infrastructure renewals accrual | | (0.1) | - |
| | | (1.4) | (2.0) |
| | | <u>1,680.4</u> | <u>1,603.9</u> |
| Net operating assets | | | |
| Non-operating assets and liabilities | | | |
| Borrowings | | (2.5) | (2.5) |
| Non-trade debtors | | 1.7 | 1.1 |
| Non-trade creditors due within one year | | (0.7) | (0.8) |
| Investments – Intragroup loans | | 68.5 | 68.5 |
| Corporation tax payable | | (1.6) | (0.6) |
| | | <u>65.4</u> | <u>65.7</u> |
| Creditors: amounts falling due after more than one year | | | |
| Borrowings | | (203.0) | (202.6) |
| Other creditors | | (1.6) | (1.6) |
| | | <u>(204.6)</u> | <u>(204.2)</u> |
| 8.75% irredeemable cumulative preference Shares | | | |
| | | (12.5) | (12.5) |
| Provisions for liabilities and charges | | | |
| Deferred tax provision | | (19.7) | (18.8) |
| Retirement benefit obligations net of associated deferred taxation | | 8.3 | 3.1 |
| | | <u>1,517.3</u> | <u>1,437.2</u> |
| Net assets employed | | | |
| Capital and reserves | | | |
| Called up share capital | | 6.0 | 6.0 |
| Share premium account | | 4.4 | 4.4 |
| Share option reserve | | - | 0.8 |
| Other reserves | | 5.8 | 5.8 |
| Profit and loss account | | 21.5 | 10.6 |
| Current cost reserve | C7 | 1,479.6 | 1,409.6 |
| | C12 | <u>1,517.3</u> | <u>1,437.2</u> |

The accounts were approved by a Committee of the Board on 13 July 2007 and signed on its behalf by -

A Parsons, Managing Director
A Nield, Finance Director

The accompanying notes to the accounts form an integral part of this statement.

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS

**CURRENT COST CASH FLOW STATEMENT
FOR THE APPOINTED BUSINESS
for the year ended 31 March 2007**

| | Notes | 2007 £m | 2006 Restated £m |
|---|-------|---------------|------------------------|
| Net cash inflow from operating activities | C8 | 42.2 | 33.5 |
| Returns on investments and servicing of finance - | | | |
| Interest received | | 6.0 | 5.3 |
| Interest paid | | (8.7) | (8.4) |
| Interest paid on finance leases | | (1.0) | (1.2) |
| Dividends paid on 8.75% irredeemable cumulative preference shares | | (1.1) | (1.1) |
| Net costs of issue of new loans | | - | (1.1) |
| | | (4.8) | (6.5) |
| Taxation - | | | |
| Corporation tax paid | | (0.9) | (1.6) |
| Capital expenditure and investing activities - | | | |
| Purchase of fixed assets | | (28.6) | (13.7) |
| less contributions received | | 3.5 | 4.2 |
| Infrastructure renewals expenditure | | (12.6) | (8.7) |
| Proceeds on disposal of fixed assets | | - | 0.2 |
| Loan advanced to ultimate UK holding company | | - | (21.5) |
| | | (37.7) | (39.5) |
| Dividends paid on equity shares | | (6.0) | (10.1) |
| Net cash outflow before management of liquid resources and financing | | (7.2) | (24.2) |
| Management of liquid resources being decrease/(increase) in short-term deposits | | 11.5 | (29.1) |
| Financing - | | | |
| New term loans | | - | 57.0 |
| Capital element of lease repayments | | (2.2) | (1.9) |
| Loan repayments | | - | (1.8) |
| Payments in respect of swap liability | | (0.3) | (0.6) |
| Net cash (outflow)/inflow from financing | | (2.5) | 52.7 |
| Increase/(decrease) in cash | | 1.8 | (0.6) |
| Cash, beginning of year | | 1.0 | 1.6 |
| Cash, end of year | C9 | 2.8 | 1.0 |

The accompanying notes to the accounts form an integral part of this statement.

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS

NOTES TO THE CURRENT COST ACCOUNTS FOR THE APPOINTED BUSINESS

C1. Current cost accounting policies

These accounts have been prepared for the Appointed Business of Bristol Water plc in accordance with guidance issued by the Director General of Water Services for modified real terms financial statements suitable for regulation in the water industry. They measure profitability on the basis of real financial capital maintenance in the context of assets which are valued at their current cost value to the business with the exception of assets acquired prior to 31 March 1990.

The company has not adopted International Financial Reporting Standards (IFRS) for its financial statements for the year ended 31 March 2007, and has no current plans to do so until UK GAAP and IFRS are fully harmonised. This is in line with the guidance issued by Ofwat in RD 06/06 for regulatory accounting statements.

Where the revised regulatory accounting guidelines required a change in presentation, the 2006 figures are shown as 'restated'.

The accounting policies used are the same as those adopted in the statutory Historical Cost Accounts, except as set out below:

(a) Tangible fixed assets

The valuation of all assets, except vehicles and mobile plant (see Other fixed assets note below), is based on the modern equivalent asset valuation produced by the Asset Management Plan (AMP) valuation at 31 March 1998, as amended for additions, disposals, and retail price index adjustments after this date to the period ended 31 March 2007. This equates to a proxy for depreciated 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 pre-31 March 1990 assets by contributions from third parties and to the extent that some of those assets would on replacement be so funded, replacement cost again differs from value to the business. Redundant assets are valued at their recoverable amounts.

Land and buildings

Non-specialised operational properties were valued on the basis of open market value for existing use at 31 March 1998 and have been expressed in real terms by indexing using the Retail Price Index ("RPI") since that date.

Specialised operational properties at 31 March 1998 were valued at the lower of depreciated replacement cost and recoverable amount and have been restated by adjusting for inflation as measured by changes in the RPI. The unamortised portion of third party contributions received since 31 March 1990 is deducted in arriving at net operating assets (as described below).

The valuation of land and buildings for both specialised and non-specialised properties is undertaken by a Chartered Surveyor employed by the company.

Infrastructure assets

Mains, impounding and pumped raw water storage reservoirs and dams are valued at a proxy replacement cost determined principally on the basis of data provided by AMP. A continuing process of refinement of asset records is expected to produce adjustments to existing values when periodic reviews of the AMP takes place. This is in conjunction with the determination of price limits by Ofwat at 5 yearly intervals. 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 except vehicles and mobile plant are valued periodically at depreciated replacement cost. The last valuation being the 31 March 1998. Between periodic reviews, values are restated for inflation as measured by changes in the RPI. Vehicles and mobile plant are stated at depreciated historical cost as differences between historical cost and current cost values are not considered material.

Surplus land

Surplus land is valued at recoverable amounts taking into account that part of any proceeds to be passed onto customers under Condition B of the Licence of Appointment.

(b) 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 brought forward is restated for the change in RPI for the year prior to inclusion in the carried forward balance.

(c) Real financial capital maintenance adjustments

These adjustments are made to the 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 RPI over the year to the opening working capital.

Financing adjustment

This is calculated by applying the change in 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
- deferred tax provision
- retirement benefit obligations net of associated deferred taxation

(d) Basis of allocation and apportionment of costs and assets

- between Bristol Water plc and its associated companies is at arm's length and no cross subsidy is occurring.
- between appointed and non-appointed businesses, costs are attributed to the appropriate cost centres in the company's accounting system, which are identified as appointed or non-appointed. The majority of non-appointed costs are incurred directly with the remainder allocated on a time apportionment basis.
- operational costs of day to day collection, storage, treatment and supply of water are allocated as operating costs along with the costs of technical and administrative support.

- capital costs are defined as those costs which are incurred in providing an additional or a replacement non-infrastructure asset. In addition, costs in respect of the provision of additional infrastructure capacity or enhancement of the network are also capitalised. These costs are incorporated in the Balance Sheet as additions to fixed assets. Where non-infrastructure assets have been replaced, their cost is removed from the Balance Sheet. There is no rule which requires capitalisation of any costs in excess of a specific value. However, it is unlikely that items with a value less than £1,000 in total would be capitalised.
- costs in respect of the maintenance of the network of pipes and pumped raw water storage reservoirs are treated as infrastructure maintenance and are charged as infrastructure renewals expenditure.
- costs are directly attributed to appropriate cost centres in the accounting system which are allocated as above. Manpower costs include an appropriate proportion of overheads in their allocation.

(e) **Pension costs**

The company has adopted FRS 17, as included in note 20 to the Historical Cost Accounts and note 21 'Retirement benefit obligations' in the statutory accounts.

C2. Appointed Business

Appointed business for the purpose of these accounts is defined as the activities necessary for the company to fulfil its duties and functions as a Water Undertaker under its licence issued by the Department for Environment, Food and Rural Affairs. All other activities are classified as non-appointed business.

C3. Analysis of turnover for the Appointed Business

| | 2007 | 2006 |
|---|-------------|------|
| | £m | £m |
| Measured | 29.6 | 27.2 |
| Unmeasured | 47.0 | 45.9 |
| Large user revenues and special agreements | 5.1 | 4.6 |
| Non potable large user and special agreements | 0.4 | 0.4 |
| Rechargeable works | 0.5 | 0.5 |
| Bulk supplies | 0.6 | 0.6 |
| Other turnover | 0.4 | 0.5 |
| Total turnover | 83.6 | 79.7 |

C4. Analysis of operating costs of the Appointed Business

Cost allocation

Costs are allocated in the following way:

All operational costs of day to day collection, storage, treatment and supply of water are allocated as operating costs along with the costs of technical and administrative support.

All costs are directly attributed to appropriate cost centres in the accounting system which are allocated as above. Manpower costs include an appropriate proportion of overheads in their allocation.

Commentary on the 2006/07 operating costs is set out in the Operating and Financial Review.

C4. (Continued) Analysis of operating costs of the Appointed Business for 2006/07

| | Service analysis | | |
|--|--------------------------------|--------------------|-----------------|
| | Resources & treatment £m | Distribution £m | Sub-total £m |
| Direct costs - | | | |
| Employment costs | 1.9 | 2.6 | 4.5 |
| Power | 2.5 | 2.3 | 4.8 |
| Hired and contracted services | 2.6 | 2.7 | 5.3 |
| Materials and consumables | 2.0 | 0.4 | 2.4 |
| Service charges | 2.5 | - | 2.5 |
| Bulk supply imports | 0.1 | - | 0.1 |
| Other direct costs | 0.6 | 0.4 | 1.0 |
| Total direct costs | 12.2 | 8.4 | 20.6 |
| General & support costs | 3.7 | 3.7 | 7.4 |
| Functional expenditure * | 15.9 | 12.1 | 28.0 |
| Business activities | | | |
| Customer services | | | 2.6 |
| Scientific services | | | 1.7 |
| Other business activities | | | 0.8 |
| Business activities sub total | | | 5.1 |
| Local authority rates | | | 3.7 |
| Bad and doubtful debts | | | 2.3 |
| Total operating expenditure less third party costs | | | 39.1 |
| Third party operating expenditure | | | 1.2 |
| Total operating expenditure | | | 40.3 |
| Capital costs - | | | |
| Infrastructure renewals charge | 2.3 | 9.7 | 12.0 |
| Current cost depreciation | 10.3 | 5.1 | 15.4 |
| Amortisation of deferred credits | | | (0.3) |
| Total capital maintenance | | | 27.1 |
| Total operating costs | | | 67.4 |
| *included within these costs is £2.7m in respect of reactive maintenance of infrastructure assets, planned maintenance is included within infrastructure renewals expenditure. Also included is £2.2m in respect of planned and reactive maintenance of non-infrastructure assets. | | | |
| Current cost Modern Equivalent Asset values - | | | |
| Service activities and water supply total | 614.8 | 1,094.6 | 1,709.4 |
| Services for third parties | 1.8 | 13.5 | 15.3 |
| Total | 616.6 | 1,108.1 | 1,724.7 |

C4. (Continued) Analysis of operating costs of the Appointed Business for 2005/06

| | Service analysis | | Sub-total £m |
|--|--------------------------------|-------------------------|-----------------|
| | Resources & treatment £m | Distri- bution £m | |
| Direct costs - | | | |
| Employment costs | 1.9 | 2.3 | 4.2 |
| Power | 2.0 | 1.7 | 3.7 |
| Hired & contracted services | 2.3 | 1.8 | 4.1 |
| Materials and consumables | 1.7 | 0.3 | 2.0 |
| Service charges | | | |
| Environment Agency | 2.4 | - | 2.4 |
| Bulk supply imports | 0.1 | - | 0.1 |
| Other direct costs | 0.7 | 0.4 | 1.1 |
| Total direct costs | 11.1 | 6.5 | 17.6 |
| General & support costs | 4.3 | 3.9 | 8.2 |
| Functional expenditure * | 15.4 | 10.4 | 25.8 |
| Business activities | | | |
| Customer services | | | 2.7 |
| Scientific services | | | 2.1 |
| Other business activities | | | 0.6 |
| Business activities sub total | | | 5.4 |
| Rates | | | 3.6 |
| Bad and doubtful debts | | | 1.6 |
| Total operating expenditure less third party costs | | | 36.4 |
| Third party operating expenditure | | | 1.2 |
| Total operating expenditure | | | 37.6 |
| Capital costs - | | | |
| Infrastructure renewals charge | 1.1 | 8.7 | 9.8 |
| Current cost depreciation | 10.0 | 4.7 | 14.7 |
| Amortisation of deferred credits | | | (0.3) |
| Total capital maintenance | | | 24.2 |
| Total operating costs | | | 61.8 |
| *included within these costs is £2.9m in respect of reactive maintenance of infrastructure assets, planned maintenance is included within infrastructure renewals expenditure. Also included is £2.1m in respect of planned and reactive maintenance to non-infrastructure assets. | | | |
| Current cost Modern Equivalent | | | |
| Asset values - | | | |
| Service activities and water supply total | 583.4 | 1,030.8 | 1,614.2 |
| Services for third parties | 1.8 | 12.9 | 14.7 |
| Total | 585.2 | 1,043.7 | 1,628.9 |

C5. Analysis of current cost fixed assets for the Appointed Business

All the fixed assets of the Appointed Business are used in the water supply service.

| | Specialised Operational Assets £m | Non- Specialised Operational Assets £m | Infra- structure Assets £m | Other Tangible Assets £m | Total £m |
|--|--|--|-------------------------------------|-----------------------------------|----------------|
| Gross replacement cost - | | | | | |
| Balance 1 April 2006 | 550.8 | 17.0 | 1,410.4 | 3.2 | 1,981.4 |
| RPI Adjustment | 26.6 | 0.8 | 68.0 | - | 95.4 |
| Disposals | (0.8) | - | - | (0.3) | (1.1) |
| Additions | 18.6 | - | 13.3 | 0.8 | 32.7 |
| Balance 31 March 2007 | 595.2 | 17.8 | 1,491.7 | 3.7 | 2,108.4 |
| Depreciation - | | | | | |
| Balance 1 April 2006 | 349.0 | 1.3 | - | 2.2 | 352.5 |
| RPI Adjustment | 16.8 | 0.1 | - | - | 16.9 |
| Disposals | (0.7) | - | - | (0.4) | (1.1) |
| Charge for year | 14.9 | 0.1 | - | 0.4 | 15.4 |
| Balance 31 March 2007 | 380.0 | 1.5 | - | 2.2 | 383.7 |
| Net Book Value at 31 March 2007 | 215.2 | 16.3 | 1,491.7 | 1.5 | 1,724.7 |
| Net Book Value at 1 April 2006 | 201.8 | 15.7 | 1,410.4 | 1.0 | 1,628.9 |

C6. Working capital

| | 2007 £m | 2006 Restated £m |
|-------------------------------|--------------|------------------------|
| Stocks | 0.7 | 0.6 |
| Trade debtors | | |
| - measured household | 2.1 | 1.9 |
| - unmeasured household | 3.3 | 3.1 |
| - measured non-household | 2.9 | 3.0 |
| - unmeasured non-household | 0.1 | - |
| Other trade debtors | 0.5 | 0.3 |
| Measured income accrual | 7.6 | 6.8 |
| Prepayments and other debtors | 2.5 | 2.8 |
| Trade creditors | (1.0) | (1.2) |
| Receipts in advance | (8.0) | (7.2) |
| Short-term capital creditors | (6.4) | (2.3) |
| Accruals and other creditors | (4.7) | (5.6) |
| | (0.4) | 2.2 |

C7. Movement on current cost reserve

| | 2007 £m | 2006 £m |
|----------------------------|----------------|----------------|
| Balance at 1 April | 1,409.6 | 1,376.0 |
| RPI adjustments - | | |
| Fixed assets | 78.5 | 38.3 |
| Working capital | 0.1 | - |
| Financing | (5.4) | (3.2) |
| Grants and contributions | (3.2) | (1.5) |
| Balance at 31 March | 1,479.6 | 1,409.6 |

C8. Reconciliation of current cost operating profit to net cashflow from operating activities

| | 2007 | 2006 |
|---|--------------|----------------|
| | £m | Restated £m |
| Current cost operating profit | 16.1 | 17.9 |
| Working capital adjustment | 0.1 | - |
| Movement in working capital | (1.5) | (0.1) |
| Receipts from other income | 0.4 | 0.4 |
| Current cost depreciation | 15.1 | 14.4 |
| Infrastructure renewals charge | 12.0 | 9.8 |
| Additional contributions to pension scheme, including payments in respect of early retirements | (1.0) | (8.5) |
| Movements in provisions | 1.0 | (0.4) |
| Net cash inflow from operating activities | 42.2 | 33.5 |

C9. Net debt analysis

| | Interest rate risk profile | | | 2007 | 2006 |
|--|----------------------------|------------------|-----------------|---------------|--------|
| | Fixed rate | Floating rate | Index linked | Total | Total |
| | £m | £m | £m | £m | £m |
| Maturity profile | | | | | |
| Less than one year | - | 2.5 | - | 2.5 | 2.5 |
| Between one and two years | 25.0 | 1.9 | - | 26.9 | 2.5 |
| Between two and five years | - | 8.1 | - | 8.1 | 31.6 |
| Between five and twenty years | - | 7.5 | - | 7.5 | 11.0 |
| In more than twenty years | 57.5 | - | 98.2 | 155.7 | 152.5 |
| Unamortised debt issue premiums/ (costs) | 4.8 | - | - | 4.8 | 5.0 |
| Irredeemable debentures | 1.6 | - | - | 1.6 | 1.6 |
| Borrowings (excluding irredeemable preference shares) | 88.9 | 20.0 | 98.2 | 207.1 | 206.7 |
| Irredeemable preference share capital | | | | 12.5 | 12.5 |
| Total borrowings | | | | 219.6 | 219.2 |
| Cash | | | | (2.8) | (1.0) |
| Short term deposits | | | | (28.0) | (39.4) |
| Net Debt including irredeemable preference shares | | | | 188.8 | 178.8 |

C10. Regulatory Capital Value (RCV)

| | |
|--|---------------------|
| | £m |
| Closing RCV for 2005/06 | 234.5 |
| Indexation to 2006/07 year end price base | 11.3 |
| | <u>245.8</u> |
| Capital expenditure (excluding infrastructure renewals charge) | 34.4 |
| Infrastructure renewals expenditure | 9.4 |
| Infrastructure renewals charge | (10.4) |
| Grants and contributions | (3.1) |
| Depreciation | (15.3) |
| Outperformance of regulatory assumptions in previous periods | (0.4) |
| Closing RCV carried forward at 31 March 2007 at year end price base | <u>260.4</u> |
| Average regulatory capital value for 2006/7 at average 2006/07 price base | <u>248.0</u> |

The RCV shown is the value and calculation used by Ofwat in setting the price limits for the period 2005/06 to 2009/10, and is equivalent to the values set out in RD 08/06 inflated to 2006/07 prices. The closing RCV at 31 March 2007 is in line with the value set out in RD 09/07.

The differences from the actual capital expenditure and the depreciation will not affect price limits in the current period. Capital efficiencies will be taken into account in the calculation for the next periodic review in 2009.

The reconciliation of the opening and closing RCVs uses year end RPI to index from 2002/03 prices to 2006/07 prices. (2002/03 was the base year for PRO4 and therefore all adjustments about inflation are made relative to that point). The average RCV is presented using year average RPI to index to 2006/07 prices. The average RCV cannot therefore be calculated as the simple average of the opening and closing RCVs.

RCV is inflated by RPI each year during 5 year PRO4 regulatory periods. At the start of the next regulatory period (PR09) an adjustment is made to reflect differential rates of inflation relative to RPI for capital expenditure as measured by COPI compared to the PRO4 Final Determination assumptions.

C11. Appointed business-Reconciliation of Current cost profit/(loss) to Historical cost profit retained

| | 2007 | 2006 |
|--------------------------------------|--------------|-------|
| | £m | £m |
| Current cost profit/(loss) retained | 7.2 | (1.9) |
| Current cost depreciation adjustment | 6.3 | 5.8 |
| Working capital adjustment | 0.1 | - |
| Financing adjustment | (5.4) | (3.2) |
| Historical cost profit retained | 8.2 | 0.7 |

C12. Movement in capital and reserves

| | Share capital | Share premium account | Share option reserve | Capital redemption reserve | Profit and loss | Current Cost Reserve | Total 2007 | Total 2006 |
|--|---------------|-----------------------|----------------------|----------------------------|-----------------|----------------------|-------------------|----------------|
| | £m | £m | £m | £m | £m | £m | £m | £m |
| Beginning of year | 6.0 | 4.4 | 0.8 | 5.8 | 10.6 | 1,409.6 | 1,437.2 | 1,399.1 |
| Current cost profit for year | - | - | - | - | 13.2 | - | 13.2 | 8.2 |
| Actuarial gains recognised in respect of retirement benefit obligations | - | - | - | - | 4.8 | - | 4.8 | 7.8 |
| Attributable deferred taxation | - | - | - | - | (1.3) | - | (1.3) | (2.2) |
| Charged against operating profit for equity-settled share based payment | - | - | - | - | - | - | - | 0.2 |
| Deferred tax asset written off upon closure of equity-settled share based payment scheme | - | - | (0.6) | - | - | - | (0.6) | - |
| Transfer arising on closure of equity-settled share based payment scheme | - | - | (0.2) | - | 0.2 | - | - | - |
| Attributable deferred taxation | - | - | - | - | - | - | - | 0.6 |
| Ordinary dividends | - | - | - | - | (6.0) | - | (6.0) | (10.1) |
| RPI adjustments | - | - | - | - | - | 70.0 | 70.0 | 33.6 |
| End of year | 6.0 | 4.4 | - | 5.8 | 21.5 | 1,479.6 | 1,517.3 | 1,437.2 |

BRISTOL WATER plc

REGULATORY ACCOUNTING STATEMENTS for the year ended 31 March 2007

DIRECTORS' REMUNERATION

The Statutory Annual Report and Accounts for Bristol Water plc include a detailed Remuneration Committee report. This is not repeated within the Regulatory Accounting Statements.

The Remuneration Committee report sets out details of Directors' remuneration and notes that Executive Directors' annual bonuses are based on the achievement of water quality, customer service, leakage and financial targets, together with an assessment of personal performance, and was limited in 2006/07 to a maximum of either 30% or 50% of basic salary.

Bonus eligibility is based on the following components:

| | % of maximum potential bonus | |
|---|------------------------------|------------|
| | % | % |
| Level of profit before tax for year relative to budget targets (PBT vs budget) | | 20 |
| Cumulative level of profit before tax for PRO4 period relative to Ofwat Final Determination assumptions (adjusted to reflect a number of factors) (PBT vs PRO4) | | 40 |
| Level of achievement for year against service performance targets: | | |
| Water quality | 5.0 | |
| Discoloured water complaints | 5.0 | |
| Leakage target | 4.0 | |
| DG3 interruptions | 3.0 | |
| DG7 complaints | 1.5 | |
| DG9 telephone answering | 1.5 | |
| | | 20 |
| Personal performance | | 20 |
| | | <u>100</u> |

Non-Executive Directors are not entitled to bonuses from Bristol Water plc.

The table below sets out for individual directors the maximum bonus entitlement % and bonus awarded for 2006/07:

| | | Maximum bonus entitlement as % of base salary | 2006/07 awarded as % of maximum | | | | Total | 2006/07 Bonus as % of Base Salary | 2006/07 Bonus entitlement |
|------------|-------------------------------------|---|---------------------------------|-------------|---------|----------|-------|-----------------------------------|---------------------------|
| | | | PBT vs budget | PBT vs PRO4 | Service | Personal | | | |
| | | % | % | % | % | % | % | £000 | |
| A Bates | Quality Director | 50 | 10.7 | 40.0 | 10.1 | 5.0 | 65.8 | 32.9 | 29 |
| M Cermeron | Organisation & Development Director | 30 | 10.7 | 40.0 | 10.1 | 10.0 | 70.8 | 21.2 | 5 |
| M Navarro | Chief Executive | 30 | 10.7 | 40.0 | 10.1 | 10.0 | 70.8 | 21.2 | 9 |
| A Nield | Finance Director | 50 | 10.7 | 40.0 | 10.1 | 5.0 | 65.8 | 32.9 | 49 |
| A Parsons | Managing Director | 50 | 10.7 | 40.0 | 10.1 | 5.0 | 65.8 | 32.9 | 59 |

Notes:

- M Navarro's & M Cermeron's bonuses relate to the period 1 January to 31 March 2007 only.
- 2006/07 bonus entitlements were paid in June 2007.

BRISTOL WATER plc
REGULATORY ACCOUNTING STATEMENTS

**INDEPENDENT ACCOUNTANTS' REPORT TO THE DIRECTOR GENERAL OF WATER SERVICES
("THE REGULATOR") AND THE DIRECTORS OF BRISTOL WATER plc**

We have audited the Regulatory Accounts of the Company for the year ended 31 March 2007 on pages 16 to 41 and 43 to 54 which comprise;

- the regulatory historical cost accounting statements, comprising the regulatory historical cost profit and loss account and the regulatory historical cost balance sheet; and
- the regulatory current cost accounting statements for the Appointed Business, comprising the current cost profit and loss account, the current cost balance sheet, the current cost cash flow statement and the related notes numbered C1 to C12 to the current cost financial statements including the statement of accounting policies on which the Regulatory Accounts have been prepared.

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 undertaker under the Water Industry Act 1991 (the "Regulatory Licence"). Our audit work has been undertaken so that we might state to the Company and the Regulator those matters that we have agreed to state to them in our report, in order (a) to assist the Company to meet its obligation under the Regulatory Licence to procure such a report and (b) to facilitate the carrying out by the 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 Company and the WSRA, for our audit work, for this report, or for the opinions we have formed.

Basis of preparation

The Regulatory Accounts have been prepared in accordance with Condition F of the appointment and the Regulatory Accounting Guidelines (being versions 1.04, 2.03, 3.06, 4.03 and 5.04), 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. There are differences between United Kingdom Generally Accepted Accounting Principles ("UK GAAP") and the basis of preparation of information provided in the Regulatory Accounts because the Regulatory Accounting Guidelines specify alternative treatment or disclosure in certain respects. Where the Regulatory Accounting Guidelines do not specifically address an accounting issue, then they require UK GAAP to be followed. Financial information other than that prepared wholly on the basis of UK GAAP may not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in financial statements prepared in accordance with the Companies Act 1985.

Respective responsibilities of the WSRA, the Directors and auditors

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 WSRA's purposes. Accordingly we make no such assessment.

The Directors' responsibilities for preparing the Regulatory Accounts in accordance with Regulatory Accounting Guidelines are set out in the statement of directors' responsibilities for regulatory information in the Operating and Financial Review on page 11.

Our responsibility is to audit the Regulatory Accounts in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board, except as stated in the 'Basis of opinion', below and having regard to the guidance contained in Audit Technical Release 05/03 '*Reporting to Regulators of Regulated Entities*'.

We report to you our opinion as to whether the regulatory historical cost accounting statements present fairly, under the historical cost convention, the revenues and costs, asset and liabilities of the Appointee in accordance with the Company's Instrument of Appointment and Regulatory Accounting Guideline 2.03 (Guidelines for the classification of expenditure), Regulatory Accounting Guideline 3.06 (Guideline for the contents of regulatory accounts) and Regulatory Accounting Guideline 4.03 (Guideline for the analysis of operating costs and assets) and whether the regulatory current cost accounting statements on pages 43 to 54 have been properly prepared in accordance with Regulatory Accounting Guideline 1.04 (Guideline for accounting for current costs and regulatory capital values), Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03. We also report to you if, in our opinion, the Company has not kept proper accounting records as required by paragraph 3 of Condition F of the Regulatory Licence and whether the information is in agreement with the Appointee's underlying accounting records and has been properly prepared in accordance with the requirements of Condition F and, as appropriate, Regulatory Accounting Guideline 1.04, Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.06, and Regulatory Accounting Guideline 4.03.

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

Basis of audit opinion

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

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Regulatory Accounts are free from material misstatement, whether caused by fraud or other irregularity or error. However, as the nature, form and content of Regulatory Accounts are determined by the 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 Auditing Standards.

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

The regulatory historical cost accounting statements on pages 16 to 41 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 Principles, and a reconciliation of the balance sheet drawn upon this basis with that drawn upon under Companies Act 1985 is given on page 13.

Audit opinion

In our opinion the Regulatory Accounts of the Company for the year ended 31 March 2007 fairly present in accordance with Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water undertaker under the Water Industry Act 1991, the Regulatory Accounting Guidelines issued by the WSRA and the accounting policies set out on pages 16 to 18 and 47 to 49, the state of the Company's affairs at 31 March 2007 on an historical cost and current cost basis, the historical cost and current cost profit for the year and the current cost cash flow for the year and have been properly prepared in accordance with those Conditions, Guidelines and accounting policies.

We are also required to report in respect of various specific obligations of the Company as set out in its Instrument of Appointment. In respect of these obligations, we report that in our opinion:-

- a) proper accounting records have been kept by the Appointee as required by paragraph 3 of Condition F of the instrument;
- (b) the information is in agreement with the appointee's accounting records and has been properly prepared in accordance with the requirements of Condition F and, as appropriate, Regulatory Accounting Guideline 1.04, Regulatory Accounting Guideline 2.03, Regulatory Accounting guideline 3.06 and Regulatory Accounting Guideline 4.03 issued by the WSRA;
- (c) the regulatory historical cost accounting statements on pages 16 to 41 present fairly, under the historical cost convention, the revenues and costs, assets and liabilities of the appointee and its appointed business in accordance with the company's Instrument of Appointment and Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03 issued by the WSRA;
- (d) the regulatory current cost accounting statements on pages 43 to 54 have been properly prepared in accordance with Regulatory Accounting Guideline 1.04, Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03 issued by the WSRA.

Deloitte & Touche LLP
Chartered Accountants
Bristol, United Kingdom

13 July 2007

BRISTOL WATER plc
REGULATORY CERTIFICATE BY THE DIRECTORS

As required under condition F6A.2A of its Instrument of Appointment the Directors of Bristol Water plc confirm:

- (1) That in the opinion of the Directors the Appointee will have available to it sufficient financial resources and facilities to enable it to carry out, for at least the next 12 months, the Regulated Activities (including the investment programme necessary to fulfil the Appointee's obligations under the Appointment); and
- (2) That in the opinion of the Directors the Appointee will, for at least the next 12 months, have available to it management resources which are sufficient to enable it to carry out those functions; and
- (3) That in the opinion of the Directors, all contracts entered into with any Associated Company include all necessary provisions and requirements concerning the standard of service to be supplied to the Appointee, to ensure that it is able to meet all its obligations as a water undertaker.

As required by condition F6A.2B(1) the main factors that the Directors have taken into account in giving this certificate:

(1) Financial resources:

- Profit and loss budget for 2007/08 and capital programme for 2005/06 to 2009/10 approved by the Board
- Monthly management accounts prepared for periods prior to the certificate date
- Longer term financial projections prepared as part of routine financial management
- Cash at bank/on deposit held in the Bristol Water balance sheet of approximately £31m at 31 March 2007
- Unutilised committed term facilities of £30m with the Royal Bank of Scotland
- Positive initial discussions with both RBS and HSBC regarding extension/replacement of term loans totalling £25m that mature during 2008

(2) Management resources:

- Bristol Water plc has a stable and experienced senior management team
- Agbar, the ultimate parent company following their acquisition of Bristol Water Group plc during summer 2006, has introduced two executive director appointees onto the Board, M Navarro as Chief Executive and M Cermeron as Organisation and Development Director. This has supplemented the existing Executive Directors team.

(3) Associated company contracts:

- The company currently has very limited contracts with Associates; the only operational contract of significance being with Bristol Wessex Billing Services Limited (BWBSL) for the provision of billing services. The contract with BWBSL has been working effectively for a number of years and the Board is confident of BWBSL's ability to deliver the required outputs.
- Agbar is now an Associate of the Company. Any future contracts between members of the Agbar group and Bristol Water plc will need to comply with the ringfencing conditions set out in the Instrument of Appointment. For 2006/07 'contracts' are limited to the salaries and associated costs of Agbar appointees.

Approved by the Board on 23 May 2007 and signed on its behalf on 13 July 2007 by:

Alan Parsons Managing Director

Andy Nield Finance Director

BRISTOL WATER plc

BOARD MINUTE APPROVING REGULATORY CERTIFICATE BY THE DIRECTORS

Extract

BRISTOL WATER PLC (THE "COMPANY")

(COMPANY NUMBER: 2662226)

MINUTES OF A MEETING OF THE BOARD OF DIRECTORS
HELD AT 218 BRIDGWATER ROAD, BRISTOL

AT 2.00 PM ON 23 MAY 2007

PRESENT:

J M Woolley
T Smallwood
P McIlwraith
Prof D I Blockley
C Curling
Juan Antonio Guijarro
Manuel Navarro
Manuel Cermerón
C Rozman
A Parsons
A S Nield
Dr A J Bates

IN ATTENDANCE:

S C Robson – Company Secretary
M Stephenson (*Item W/0[52]/07 only*)

1. (W/045/07) OPENING and preliminaries

1.1 Moger Woolley took the chair and declared the meeting open.

[11]. REGULATORY REPORTS

11. 3 After review, the Committee of the Board approved the certificate of sufficient resources for Ofwat as required under Licence condition F6A 2A and authorised the Sub committee to sign and release it to Ofwat.

Extract

S C Robson
Secretary

APPENDIX

STATUTORY ANNUAL REPORT AND ACCOUNTS

YEAR ENDED 31 MARCH 2007