

BRISTOL WATER plc

REPORT AND ACCOUNTS 2007

Registered number - 2662226

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BRISTOL WATER plc supplies water to over one million people and businesses in an area of almost 2,400 square kilometres centred on Bristol.

Bristol Water plc is a member of the Agbar group which provides water services to approximately 23 million people worldwide.

FINANCIAL HIGHLIGHTS

Year ended 31 March	2007	2006
Financial results under UK GAAP		
	£m	£m
Turnover	86.3	81.9
Operating profit	25.2	24.9
Profit before tax	18.9	18.4
Profit after tax	16.4	11.6
Regulatory Capital Value (RCV)	260.4	234.5
Net debt (excluding 8.75% irredeemable cumulative preference shares) as percentage of RCV	68%	71%

CHAIRMAN'S STATEMENT

Introduction

In June 2006 the acquisition of Bristol Water Group plc by Sociedad General de Aguas de Barcelona S.A. (Agbar) was completed. In connection with the acquisition we agreed with Ofwat a minor change to Condition P of our licence as a water undertaker.

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.

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
- A £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.

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.

Financial performance

Operating profit increased by £0.3m to £25.2m. This reflects the average 5.2% increase in charges to customers under the approved price limits, together with the impact of our continuing efficiency initiatives offset by increased energy costs, increased bad debt charges and additional depreciation related to the capital investment programme.

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.

Net interest charges, excluding those related to retirement benefits and the preference share dividend, increased by £0.4m to £6.7m. This reflects the increase in net debt resulting from the financing of the capital expenditure programme.

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

Net debt, excluding the irredeemable preference shares, increased to £176.3m (2006: £166.2m) and represents approximately 68% of Regulatory Capital Value at 31 March 2007. As previously indicated we currently anticipate that this ratio will increase to between 70% and 80% for the remainder of the 5-year regulatory period ending in March 2010.

Dividends

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.

A final dividend of £6.0m in respect of 2006/07 is proposed for payment.

Board structure

My thanks go to Professor David Blockley who retired on 23 May 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 Cyril Rozman, a senior financial manager with Agbar, who was appointed to the Board as a non-executive director on 23 May 2007.

Conclusion

The company is performing strongly and is well placed for the future. The transition to become part of the Agbar group has progressed smoothly. As ever my thanks go to all the employees of the company for their commitment to both customer service and the continuing success of the company.

Moger Woolley
Chairman

31 May 2007

DIRECTORS' REPORT AND BUSINESS REVIEW

For the year ended 31 March 2007

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).
- 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.

FINANCIAL PERFORMANCE

The company continues to report under UK GAAP.

Financial performance during the year was good with an increase in profit reflecting the impacts of the increase in price limits.

	2007	2006
	£m	£m
Turnover	86.3	81.9
Operating profit	25.2	24.9
Net finance costs	(6.3)	(6.5)
Profit before tax	18.9	18.4
Taxation	(2.5)	(6.8)
Profit after tax	16.4	11.6
Capital investment before grants & contributions	45.5	22.6
Net debt (excluding 8.75% irredeemable cumulative preference shares) at 31 March	176.3	166.2
Ratio of net debt (excluding 8.75% irredeemable cumulative preference shares): Regulatory Capital Value (RCV)	68%	71%

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

TREASURY

Net cash inflow from operating activities was £42.6m (2006: £35.1m) and the outflow from financing activities £2.5m (2006: £52.7m inflow). Net cash used in investing activities was £37.7m (2006: £40.9m including £21.5m advanced to BWG), and net cash used in investment returns and servicing finance was £4.8m (2006: £6.5m).

Net interest charges in the year totalled £6.3m (2006: £6.5m) and were covered 4.0 times (2006: 3.8 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. The pension 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		16910	16358
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
 - 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

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 on page 7.

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 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

DIRECTORS AND THEIR INTERESTS

During the year, and following the Agbar acquisition of BWG, all the directors' interests in shares, shares in the Share Incentive Plan and the Group Savings Related Share Option Scheme were sold, transferred, exercised or terminated. Some of the directors' interests have been rolled over into Agbar loan notes.

Agbar committed to a series of ex-gratia payments to all staff (including directors) who, due to the acquisition, had share plans terminated early. The payments are made through the Bristol Water plc payroll but are fully reimbursed by Agbar. Payments made to Directors to date are included in the schedule of Directors' remuneration on page 20. Some payments have been deferred in line with maturity dates of the original share plans and will be included with future remuneration disclosures.

Ordinary shares

The directors during the year, and their beneficial interests in the ordinary shares of the previous ultimate parent company Bristol Water Group plc (BWG) at 1 April 2006, were:

J M Woolley, <i>Chairman</i>	5,768
M Navarro, <i>Chief Executive*</i>	-
Dr A J Bates, <i>Director of Quality and Information Systems</i>	7,535
Professor D I Blockley, <i>Non-Executive</i>	356
M Cermerón, <i>Director of Organisation and Development*</i>	-
C J Curling, <i>Non-Executive</i>	-
J A Guijarro, <i>Non-Executive*</i>	-
P McIlwraith, <i>Non-Executive</i>	-
A S Nield, <i>Finance Director</i>	1,093
A Parsons, <i>Managing Director (previously Chief Executive)</i>	30,027
T Smallwood, <i>Non-Executive</i>	-

*Messrs Navarro, Cermerón and Guijarro were appointed on 19 June 2006.

Following the acquisition of Bristol Water Group plc by Agbar, no director held any beneficial interests in the ordinary shares of the previous ultimate parent company Bristol Water Group plc (BWG) at 31 March 2007.

On 23 May 2007, Professor Blockley resigned and Mr C Rozman was appointed as a director of the company.

Following the acquisition of Bristol Water Group plc by Agbar, no director held any beneficial interests in the ordinary shares of the previous ultimate parent company Bristol Water Group plc (BWG) at 31 March 2007.

Share incentive plan (SIP)

The numbers of ordinary shares above include the following numbers of shares acquired in accordance with the terms of the Bristol Water Group plc SIP:

	1 April 2006
A S Nield	74
A Parsons	74

In April 2006 Mr Parsons and Mr Nield continued to subscribe to the SIP under the conditions applicable to all employees. In May 2006 all SIP shares were sold or exchanged for Agbar loan notes. The plan was terminated following the acquisition of Bristol Water Group plc by Agbar.

Savings related option scheme

The table below summarises options over ordinary shares of BWG granted to the directors under the terms of the Group Savings Related Share Option Scheme:

	Date of grant	Options unexercised at 31.3.06	Exercise price £	Exercisable from	to
A Parsons	16.07.02	8,140	2.032	Sept 2007	March 2008
Dr A J Bates	16.07.02	8,140	2.032	Sept 2007	March 2008
A S Nield	13.07.01	10,310	1.636	Sept 2006	March 2007

In June 2006, related to the Agbar offer, Mr Parsons, Dr Bates and Mr Nield were required to exercise all their options accrued to that date. The remaining options have lapsed.

Savings related share option scheme options were issued at a 20% discount to the market price to any employee entering an Inland Revenue approved Save As You Earn contract for a period of three or five years. The market price of the relevant shares at 31 March 2006 was £9.095 and ranged from £8.94 to £10.75 during the period up to the scheme's termination following the acquisition of Bristol Water Group plc by Agbar.

Share dealings

In June 2006, related to the Agbar offer, all directors who were shareholders were required to dispose of all their shareholdings. The gains made thereby, including gains made by related parties, were as follows:

	Shares purchased through SIP	Shares purchased through savings related option scheme	Other shares	Total
	£ 000s	£ 000s	£ 000s	£ 000s
A Parsons	-	51	227	278
Dr A J Bates	-	51	66	117
A S Nield	-	86	10	96
J M Woolley	-	-	53	53
Professor D Blockley	-	-	3	3
	-	188	359	547

Service contracts and fees

All executive directors have service contracts with 12-month notice periods.

For part of the year Professor D I Blockley, Mr C Curling, Mr P Mcllwraith and Mr T Smallwood were also non-executive directors of Bristol Water Group Ltd (BWG). Mr J M Woolley was a director of BWG throughout the year. Their fees for the year are disclosed in the Remuneration Committee report on page 18.

Other interests

Mr J M Woolley, Mr C Curling and Mr T Smallwood will offer themselves for re-election at the Annual General Meeting. Mr C Rozman will stand for election at the Annual General Meeting.

At no time during the year has any director had a material interest in any contract of significance with any company in the Bristol Water Group group of companies, other than his service contract.

The interests in shares and other contracts of Mr M Navarro, Mr J Guijarro, Mr C Rozman and Mr M Cermerón with other companies within the Agbar group are not disclosed within this report.

ULTIMATE PARENT COMPANY

At 1 April 2006 Bristol Water Group plc (BWG) was the ultimate parent company of Bristol Water plc.

On 22 April 2006 a recommended cash offer was made by Sociedad General de Aguas de Barcelona S.A. (Agbar) for BWG, the then ultimate parent company. Agbar assumed control of BWG on 19 June 2006. BWG was delisted on 15 June 2006.

All of the company's 8.75% irredeemable cumulative preference shares are owned outside the Agbar group.

LAND AND BUILDINGS

In the opinion of the directors there is no material difference between the book value and the current open market value of land and buildings expected to be disposed of within the next twelve months.

POLICY AND PRACTICE ON PAYMENT OF CREDITORS

It is company policy to comply with the terms of payment agreed with a supplier. Where payment terms are not negotiated, the company endeavours to adhere to the supplier's standard terms. The company pays creditors in accordance with agreed payment terms on receipt of valid invoices. At the end of the year, trade creditors represented the equivalent of 35 days purchases (2006 - 26 days).

RESEARCH AND DEVELOPMENT

The company undertakes research and development projects in relation to its business. Expenditure during the year amounted to £0.1m (2006 - £0.1m).

INSTRUMENT OF APPOINTMENT AND REGULATORY ACCOUNTS

In accordance with its Instrument of Appointment made under the Water Industry Act 1991 as amended, the directors are of the opinion that the company is in compliance with paragraph 3.1 of Condition K of that Instrument, which relates to the control over the assets of the Appointed Business. Copies of the Regulatory Accounts required under the Instrument of Appointment will be available from the Company Secretary.

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 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; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping 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.

By order of the Board
S C Robson
Secretary
31 May 2007

DIRECTORS

John Moger Woolley DL Age 72

Non-executive Chairman, Member of Nomination and Remuneration Committees

Mr. Woolley was appointed to the board in 2005. He has been a director of Bristol Water Group Ltd (BWG) from 1996, becoming Chairman in 1998. He is Pro-Chancellor of The Council of the University of Bristol. He was the High Sheriff of Gloucestershire in 2002 and was formerly the Chief Executive of DRG plc.

Manuel Navarro Age 50

Chief Executive, Member of Nomination Committee

Mr Navarro was appointed to the board in June 2006. He has held a range of senior positions with Agbar since 1983. He is also Chief Executive of BWG.

Dr Arnold Bates Age 62

Quality and Information Systems Director

Dr Bates was appointed to the board in 1991. He is also a director of UKWIR.

Manuel Cermerón Age 37

Organisation and Development Director

Mr Cermerón was appointed to the board in June 2006. He has held a range of senior positions with Agbar since 2000.

Chris Curling Age 57

Non-executive, Member of Nomination and Remuneration Committees

Mr Curling was appointed to the board in 2004. He was a director of BWG from 2005 until his retirement from that board in June 2006. He has four non-executive directorships and is a member of the Council of Bristol University. Formerly he was Senior Partner with the legal firm Osborne Clarke.

Juan Antonio Guijarro Age 42

Non-executive

Mr Guijarro was appointed to the board in June 2006. He is General Manager of Agbar's water division (other than the Catalanian region), and has been with Agbar since 1989. He is also a director of BWG.

Peter McIlwraith Age 59

Non-executive, Chairman of Audit Committee and Member of Nomination and Remuneration Committees

Mr McIlwraith was appointed to the board in 2003. He was a director of BWG from 2001 until his retirement from that board in June 2006. He is the Chairman of @Bristol Limited. He was a partner with PricewaterhouseCoopers (and prior to that Price Waterhouse) until 2001 and was Regional Chairman for the West and Wales and Senior Partner in Bristol.

Andrew Simon Nield Age 51

Finance Director

Mr Nield was appointed to the board in 2000. He is Group Finance Director of BWG. He previously held a range of senior roles with the Anglian Water (now AWG) group. He is also a director of The Water Companies (Pension Fund) Trustee Company.

Alan Parsons Age 58

Managing Director and Member of Nomination Committee

Mr Parsons was appointed to the board in 1991 and appointed as Chief Executive in 2000. He became Managing Director in June 2006 following the appointment of Mr Navarro as Chief Executive. He is also a director of BWG and is a director of Water UK.

Ciril Rozman Age 42

Non-executive

Mr Rozman was appointed to the Board in May 2007. He is Finance Manager of Agbar's water division and has been with Agbar since 1995.

Trevor Smallwood DL OBE Age 59

Non-executive Director, Chairman of Remuneration Committee, Member of Audit and Nomination Committees

Mr Smallwood was appointed to the board in 2003. He was a director of BWG from 1999 until his retirement from that board in June 2006. He is President of Quartet Community Foundation (formerly the Greater Bristol Foundation). He has a number of other non-executive directorships. He was Chairman of FirstGroup plc until September 1999.

Notes:

Under a Scheme of Arrangement Bristol Water Holdings plc replaced Bristol Waterworks Company as the ultimate parent of the Bristol Water group in 1991. Under a further scheme of arrangement, Bristol Water Group Ltd (registered at the time as Bristol Water Group plc), replaced Bristol Water Holdings plc in 2003. References to Bristol Water Group Ltd (BWG) above include predecessor companies where appropriate.

Professor David Blockley was a director during the year but retired from the Board on 23 May 2007.

CORPORATE GOVERNANCE REPORT

DIRECTORS' STATEMENT

The Board is committed to ensuring that high standards of corporate governance are maintained by the company. In doing so it endorses the main and supporting principles and provisions set out in the Combined Code on Corporate Governance of the Financial Reporting Council (the Code) as revised in June 2006. For the year ended 31 March 2007 up to the date of approving the accounts the Board has applied the principles and complied with the provisions of Section 1 of the Code.

The directors report that, after making enquiries, they have a reasonable expectation that the company has adequate resources to continue in operation for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Board and Board Committees

At 31 March 2007 the Board of Bristol Water plc (the "Board") comprised the Chairman, five executive directors and five non-executive directors. Four of the non-executive directors are, in the opinion of the Board, independent. This assessment has been made by the Board based on their views of their performance on the Board and taking into account their experience, character and period served.

The following table sets out the attendance of directors at Board and committee meetings during 2006/07:

		Number of meetings attended		
		Board	Audit	Remuneration
		meetings	Committee	Committee
		(maximum 8)	meetings	meetings
			(maximum 4)	(maximum 4)
Chairman	J M Woolley	8		
Deputy Chairman, Senior Independent Director	T Smallwood	7	4	4
Chief Executive	M Navarro	7		
Independent non-executive director	Professor D I Blockley	8	3	
Independent non-executive director	C Curling	6		4
Independent non-executive director	P McIlwraith	7	4	4
Managing Director	A Parsons	8		
Finance Director	A S Nield	8		
Quality Director	Dr A J Bates	8		
Organisation and Development Director	M Cermerón	7		
Non-executive director	J A Guijarro	4		

The maximum number of Board meetings for Messrs Navarro, Cermerón and Guijarro from the date of their appointment on 19 June 2006 was 7. Mr C Rozman was appointed in May 2007 so is not listed here.

The Board executes overall control of the company's affairs by reference to the schedule of matters reserved for its decision. These include the approval of strategy, financial statements, major capital expenditure, authority levels for expenditure, treasury and risk management policies. In furtherance of its duties, there are agreed procedures for the directors to take independent professional advice, if necessary, at the company's expense. There is a clear segregation between the roles of chairman and chief executive to ensure appropriate Board balance. All directors have access to the advice and services of the Company Secretary.

The Board delegates day-to-day and business management control to the executive directors.

The Board considers the Chairman to be the principal point of reference to whom concerns of whatever nature may be conveyed. In the event that an individual does not wish to raise a concern with him, the Board has identified Mr T Smallwood as the senior independent member of the Board to whom such concerns may be addressed.

Under its Instrument of Appointment as a water undertaker, the company is subject to a number of ringfencing conditions to protect it from the risks arising from other activities which may be carried out by other companies within the group so that the company does not, whether through its involvement in those activities or by its financial policies, put at risk its ability either to carry out its functions as a water undertaker or to finance them.

Audit Committee

The Audit Committee's terms of reference include the points recommended by the Combined Code. Its duties include monitoring internal controls, approving the accounting policies and reviewing the interim and annual financial statements before submission to the Board. The Committee is chaired by Mr P McIlwraith and currently comprises two other non-executive directors Professor Blockley and Mr T Smallwood. The external auditors attended all meetings in the year.

The Committee is formally constituted with terms of reference. A copy of the terms of reference is available to shareholders by writing to the Company Secretary, Mr S C Robson.

Bristol Water plc has an Auditor Independence policy which considers services that the external auditors may and may not provide such that their independence and objectivity is not impaired, as well as establishing a formal authorisation process, including the pre-approval by the Audit Committee for allowable non-audit work that they may perform.

The Audit Committee reviews remuneration received by external auditors for audit services and non-audit services, with the aim of seeking to balance objectivity, value for money and compliance with the latest auditor independence guidance and regulations.

The Committee concluded that no conflict of interest exists between audit and non-audit work for the company and the Bristol Water group and that this was the most cost effective way of conducting the company's business.

Remuneration Committee

The role and composition of the Remuneration Committee are set out in the report on page 18.

Nomination Committee

The Nomination Committee now comprises the Chairman, Mr C Curling, Mr P McIlwraith, Mr T Smallwood, Mr A Parsons and Mr M Navarro. It is responsible for selecting, appointing and re-appointing the company's executive and non-executive directors and considers such matters as required. All directors must retire by rotation every 3 years and any non-executive with more than 9 years' service will stand for re-election on an annual basis. Following the takeover by Agbar the full board considered the appointment of Messrs Navarro, Cermerón and Guijarro. The Committee met in respect of the appointment of Mr C Rozman in May 2007.

The Committee is formally constituted with terms of reference. A copy of the terms of reference is available to shareholders by writing to the Company Secretary, Mr S C Robson.

Internal Controls

The company, as required by the Financial Services Authority, has complied and continues to comply with the Code provisions on internal control having established the procedures necessary to implement the guidance issued in September 1999 (the Turnbull Committee report) and by regular review and reporting in accordance with that guidance.

The Board has overall responsibility for the system of internal control, and for reviewing its effectiveness, whilst the role of management is to implement Board policies on risk and control. The system of internal control is designed to manage risks to appropriate minima rather than eliminate any risk of failure in achieving business objectives. In pursuing these objectives, internal controls can only provide reasonable and not absolute assurance against material misstatement or loss.

The Board encourages a culture of risk identification and management across all aspects of the business, and uses the following main processes to review the effectiveness of the system of internal control:

The executive directors:

- have delegated authority to manage the business and to implement internal control and risk management processes
- have established a system of Key Performance Indicators and risk identification matrices.

The company operates through a formal board structure, which:

- considers material financing and investment decisions
- reviews the role of insurance in managing risks
- reviews and approves financial budgets and emerging financial results
- reviews on a regular basis detailed Key Performance Indicators reports which include the identification of material risks and the actions taken to manage such risks.

The Audit Committee:

- reviews internal and external audit work plans and commissions, where appropriate, reviews of specific issues
- considers reports from management, internal and external auditors on the system of internal control and any material control weaknesses identified
- discusses with management the actions taken on any problem areas identified by Board members and management or in the internal and external audit reports
- the Chairman of the Committee reports the outcome of the Audit Committee meetings to the Board and the Board receives the minutes of all Audit Committee meetings.

The Board:

- considers material financing and investment decisions including the giving of guarantees and indemnities, and monitors policy and control mechanisms for managing treasury risk
- reviews on a regular basis a summary Key Performance Indicators report which includes the identification of material risks and the actions taken to manage such risks
- reviews the effectiveness of the risk management process and significant risk issues
- reviews and approves financial budgets and emerging financial results.

The Board undertook its latest formal assessment of risk management and control arrangements on 23 May 2007 in order to form a view on the overall effectiveness of the system of internal control. This review included an assessment of the effectiveness of internal controls within the group's joint venture, Bristol Wessex Billing Services Limited.

The Board concluded that the overall internal control framework was working effectively.

Following the delisting of BWG and changes to its Board membership, corporate governance matters and compliance are carried out by the directors of the company.

By order of the Board
S C Robson, Secretary
31 May 2007

REMUNERATION COMMITTEE REPORT

This Report sets out the remuneration policy operated by the company in respect of the executive directors, together with disclosures on directors' remuneration to comply with the Directors' Remuneration Report Regulations 2002, (the "Regulations"). The auditors are required to report on the 'auditable' part of this Report and to state whether, in their opinion, that part of the Report has been properly prepared in accordance with the Companies Act 1985 (as amended by the Regulations). The Report is therefore divided into separate sections for audited and unaudited information.

Unauditable element of the Remuneration Committee Report

The Board have reviewed the company's compliance with the Combined Code ('the Code') on remuneration related matters. It is the opinion of the Board that the company complied with all remuneration related aspects of the Code during the year.

The Report will be put to shareholders for approval at the annual general meeting.

Role and Composition of the Remuneration Committee

The Remuneration Committee determines the remuneration and other employment conditions of the executive directors and senior executives of Bristol Water plc. It consists solely of independent non-executive directors. The membership of the Committee during the year comprised Mr T Smallwood (Chairman), Mr P McIlwraith, Professor D I Blockley and Mr C Curling. Attendances at committee meetings are set out on page 15.

The Committee is formally constituted with written terms of reference. A copy of the terms of reference is available to shareholders by writing to the Company Secretary, Mr S C Robson.

In deciding appropriate levels of executive remuneration, the Committee typically relies on external research from independent remuneration consultants which gives up-to-date information on a comparator group of companies. This year the Committee made no adjustments to the directors' existing remuneration arrangements other than an inflationary pay award.

During the year M Navarro (Chief Executive), JA Guijarro, A Parsons (Managing Director), A Nield (Finance Director) and S Robson (Company Secretary) also provided material advice and services to the Committee. No director played a part in any discussions about his own remuneration. None of the Committee has any personal financial interest or conflict of interest arising from cross-directorships or from day-to-day involvement in running the business.

Remuneration Policy

The key principle underpinning remuneration policy is the need to offer remuneration packages which can attract, motivate and retain directors and senior managers of the calibre needed to execute the company's business strategy thereby enhancing shareholder value and improving the service to customers. The company's policy is that a substantial proportion of the remuneration of the executive Directors should be performance related.

The current policy on executive remuneration is to fix salaries and other elements of the remuneration package primarily having regard to salary levels indicated by independent research and to reward directors both for enhancing value to shareholders and for delivering quality service to customers.

Two new executive directors were appointed in this period and their arrangements were arrived at in conjunction with the group's parent company, Agbar. The arrangements were designed to fit within the existing structure of the pay arrangements of the company, reflecting the skill, experience and expected contribution of the new directors.

There are three main elements of the current remuneration package for executive directors:

Basic annual salary - factors taken into account when determining basic annual salary levels are objective research based on independent salary reviews; the individual executive director's performance during the year; and pay and conditions throughout the company. Basic annual salary is reviewed each year but no adjustments save for cost of living increases have been made in the last year.

Annual bonus - based on the achievement of water quality, customer service, leakage and financial targets, together with an assessment of personal performance, and is restricted in 2006/07 to a maximum (save in exceptional circumstances) of either 30% or 50% of basic salary (2005/06 – maximum of 50%).

Taxable benefits in kind - reflecting market practice and comprising the provision of a company car and private medical and life insurance.

In addition, some expatriate benefits provided to Messrs Navarro and Cermerón are borne by Bristol Water Group Limited. These include free furnished accommodation, heating, lighting, tax advice and private school /nursery fees.

Annual Bonus Scheme

Annual bonus awards for bonus year 2006/07 (accrued and approved but not paid as at 31 March 2007) were based on performance against a range of financial, service and personal performance targets. The awards are shown in the sections headed Details of Directors' Remuneration, Pension Benefits and Share Options.

Share Options and Long-Term Incentive Schemes

The Bristol Water Group Ltd (BWG) Executive Share Option Scheme was in place until its closure following the acquisition of BWG by Agbar. No awards were made during the year and no options were outstanding at 31 March 2007.

There is currently no Long-term Incentive Scheme in place.

From 1 April 2006 until the acquisition of BWG by Agbar all employees of the group were able to take part in the Bristol Water Group Savings Related Share Option Scheme, subject to certain eligibility limits. Following the Agbar acquisition of BWG the scheme has been terminated.

Share Incentive Plan (SIP)

From 1 April 2006 until the acquisition of BWG by Agbar an all-employee SIP was in place. Executive directors were entitled to participate in this plan on the same basis as all other employees. The SIP was an Inland Revenue approved plan open to all Bristol Water Group Ltd employees. Eligible employees could contribute a maximum of £125 each month and the trustees of the plan used the money to buy shares on their behalf. Following the Agbar acquisition of BWG the shares in the scheme have been sold or exchanged for Agbar loan notes and the scheme has been terminated.

Agbar Ex Gratia Payments

Following the acquisition of BWG, Agbar committed to a series of ex-gratia payments to all staff (including directors) who, due to the acquisition, had SIP and/or share option plans terminated early. The payments are made through the company payroll but had already been fully funded by Agbar.

During the year directors received taxable payments as follows:

	Re SIP scheme	Re share option scheme	Total
	£ 000s	£ 000s	£ 000s
A Parsons	1	-	1
A S Nield	1	41	42
	<u>2</u>	<u>41</u>	<u>43</u>

Some payments have been deferred in line with maturity dates of the original share plans and will be included with future remuneration disclosures.

Service Contracts

Details of the employment contracts of the executive directors who served during the year are as follows:

	Contract date	Unexpired term	Notice period
M Navarro (appointed 19 June 2006)	28 February 2007	rolling 1 year	1 year
A Parsons	13 July 2004	rolling 1 year	1 year
A S Nield	13 July 2004	rolling 1 year	1 year
Dr A J Bates	7 February 2001	rolling 1 year	1 year
M Cermerón (appointed 19 June 2006)	29 January 2007	rolling 1 year	1 year

The service contracts of Messrs M Navarro and M Cermerón took effect from 1st January 2007.

Mr Parsons and Dr Bates have a provision in their service contracts for the enhancement of their Water Companies' Pension Scheme pensionable service by a maximum of 6½ years in the event of redundancy only.

Under the normal rules of the Water Companies' Pension Scheme any employee or director is entitled to a non-actuarially reduced pension if they are 50 or more years old and their service contract were terminated in certain circumstances.

Directors' contracts do not provide for other compensation payable on early termination.

Directors' Pension Arrangements

Until 5 December 2001, newly appointed executive directors were eligible to become contributory members of the Water Companies' Pension Scheme, a defined benefits, final salary scheme. Under the terms of that scheme the only elements of remuneration other than basic salary which are pensionable relate to the taxable benefits associated with company car provision for directors who first became company car holders before 4 July 1994, so retaining on a personal basis the contractual entitlements of such individuals at the date this change in remuneration policy was introduced. Since April 2001 a notional figure, indexed annually, has been used for this purpose based on the value of the taxable benefit as at 6 April 2001.

Any newly-appointed executive directors recruited externally will be offered membership of a company designated stakeholder pension scheme or the option of a company contribution to a personal pension plan.

Non-Executive Directors

The remuneration of the non-executive directors is determined by the Board and has been based upon independent surveys of fees paid to non-executive directors in companies of comparable size and on the basis of time commitments. Additional responsibilities are also taken into account.

During the year some of the non-executive directors' fees were paid by BWG and recharged to the company. Non-executive directors do not have contracts of service, do not participate in company pension, share or bonus schemes and do not receive any taxable benefits in kind. The terms of appointment do not entitle non-executive directors to receive compensation in the event of early termination of their appointment.

Auditable element of the Remuneration Committee Report

Details of Directors' Remuneration, Pensions Benefits and Share Options

This report includes the statutory disclosures required by the Companies Act 1985, as amended by the Company Accounts (Disclosure of Directors' Emoluments) Regulations 1997 and the Directors' Remuneration Report Regulations 2002, which are subject to audit. Full details of all elements in the remuneration package of each director and share options are set out below. Details of directors' share interests are given in the Directors' Report.

(a) Directors' Remuneration			2007	2006			
	Notes		Total £000	Total £000			
		Salary / fees £000	Benefits £000	Bonus £000			
J M Woolley	2	Non-executive	52	-	52	44	
T Smallwood	2	Non-executive	34	-	34	32	
Professor D I Blockley	2	Non-executive	28	-	28	27	
C Curling	2	Non-executive	28	-	28	26	
P McIlwraith	2	Non-executive	32	-	32	31	
J A Guijarro	5	Non-executive	-	-	-	-	
M Navarro	1	Executive	44	5	9	58	
A S Nield		Executive	149	12	49	210	
A Parsons		Executive	180	14	59	253	
Dr A J Bates		Executive	89	11	29	129	
M Cermerón	1	Executive	21	5	5	31	
P D Knowlson	4	Executive	-	-	-	-	
R W Wyatt	3	Executive	-	-	-	-	
Charge to Profit and Loss account			657	47	151	855	1,026

Notes

- 1 Appointed 19 June 2006; salaries and fees are for the period from 1 January 2007 to 31 March 2007. Salaries, fees, benefits and bonuses exclude those incurred by BWG and/or Agbar during the year.
- 2 Some remuneration for the non-executive directors in 2006 was borne by Bristol Water Group Ltd and recharged to the company and reported as operating expenditure.
- 3 Retired 31 March 2006
- 4 Retired 30 September 2005
- 5 Appointed 19 June 2006; no fees have been paid by the company.

Benefits in kind include the provision of a company car, fuel and medical and life insurance.

Bonus represents amounts accrued and approved, but not paid, as at 31 March 2007.

The table excludes Agbar ex-gratia payments which are set out on page 19.

No director waived emoluments in respect of the year ended 31 March 2007.

(b) **Accrued pension scheme benefits earned by directors**

	A S Nield £000	A Parsons £000	A J Bates £000
Listing Rules disclosure			
Increase in accrued pension during 2006/07 in excess of inflation	2	3	2
Increase in accrued lump sum during 2006/07 in excess of inflation	6	8	4
Accumulated pension per annum at 31 March 2007	50	46	43
Accumulated lump sum at 31 March 2007	149	139	128
Transfer value of increase	32	58	36
Transfer value of increase less director's contributions	20	43	28
Schedule 7A disclosure			
Increase in accrued pension during 2006/07	4	4	3
Increase in accrued lump sum during 2006/07	11	12	9
Accumulated pension per annum at 31 March 2007	50	46	43
Accumulated lump sum at 31 March 2007	149	139	128
Transfer value			
As at 31 March 2006	725	939	1051
As at 31 March 2007	842	1048	1025
Increase in transfer value	117	109	(26)
Increase in transfer value less director's contributions	104	93	(34)

Mr Parsons' benefits include Additional Voluntary Contributions (AVCs) to allow him to purchase added years, to which he has contributed up to 31 March 2007.

Only Messrs Parsons and Nield and Dr Bates accrued retirement benefits under the Bristol Water plc defined benefits scheme during the year.

The transfer values disclosed above do not represent sums paid or payable to the individual directors; they represent a potential liability of the pension scheme.

Messrs Navarro and Cermerón have not joined the company designated stakeholder pension plan and the company is not making any contribution to any private pension scheme on their behalf.

(c) **Share options**

At 1 April 2006 unexercised options over ordinary shares in the company had been granted to directors under the terms of the Group Savings Related Share Option Scheme. Details of these and of options exercised by the directors in consequence of the acquisition of BWG by Agbar are disclosed in the Directors Report. No other options were issued or exercised during the year.

This report was approved by the Board of Directors on 23 May 2007 and signed on its behalf by:

Trevor Smallwood
Chairman of Remuneration Committee
31 May 2007

ACCOUNTING POLICIES

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 and the disclosure of operating costs as explained in note 2.

During the year the treatment of receipts under S41 of the Water Industry Act 1991 was amended. They are no longer credited to deferred income and released to the profit and loss account over a three-year period, but are now deducted from the cost of the related infrastructure assets. Amounts for the previous year have not been restated as the adjustment is not material. The change was made to bring the treatment of these receipts into line with generally accepted practice in the water industry.

The effect of the change in accounting policy is:

- to decrease profit after tax by £0.6m including £0.2m in relation to the previous year (year ended 31 March 2006: Nil)
- to decrease total recognised gains and losses for the year by £0.6m including £0.2m in relation to the previous year (year ended 31 March 2006: Nil)
- to decrease net assets as at 31 March 2007 by £0.6m including £0.2m in relation to the previous year (as at 31 March 2006: Nil)

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. Turnover is recognised upon delivery of water or completion of other services.

Income from metered supplies is based upon actual 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 any 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 under renewals accounting takes account of planned expenditure levels to maintain the operating capability of the company's infrastructure assets in perpetuity.

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

The treatment of receipts under S41 of the Water Industry Act 1991 was changed during the year, as described in section (a) above.

Contributions received in respect of tangible assets, other than those received in respect of infrastructure assets, are treated as deferred income and amortised in 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

The charge for taxation is computed based on the profit for the period adjusted according to tax legislation.

Advance Corporation Tax (ACT) in respect of dividends in previous years is 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 has an interest rate swap which is 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 was 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.

PROFIT AND LOSS ACCOUNT

for the year ended 31 March 2007

		2007	2006
	Note	£m	£m
Turnover	1	86.3	81.9
Operating costs	2	<u>(61.1)</u>	<u>(57.0)</u>
Operating profit		25.2	24.9
Dividends on 8.75% irredeemable cumulative preference shares	3	(1.1)	(1.1)
Interest in respect of retirement benefit scheme surplus	3	1.5	0.9
Other net interest payable and similar charges	3	(6.7)	(6.3)
Profit on ordinary activities before taxation		18.9	18.4
Taxation on profit on ordinary activities	4	(2.5)	(6.8)
Profit on ordinary activities after taxation		16.4	11.6
Earnings per ordinary share	5	273.0p	193.0p
Dividends per ordinary share			
- declared or proposed in respect of the period	19	<u>147.10p</u>	139.85p
- paid during the period	19	<u>105.09p</u>	169.83p

All activities above relate to the continuing activities of the company.

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

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

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

for the year ended 31 March 2007

		2007	2006
	Note	£m	£m
Profit attributable to Bristol Water plc shareholders		16.4	11.6
Actuarial gains recognised in respect of retirement benefit obligations	21	4.8	7.8
Attributable deferred taxation	16	(1.3)	(2.1)
Charged against operating profit for equity-settled share-based payment	23	-	0.2
Attributable deferred taxation	16	-	0.6
Deferred tax asset reversal upon closure of equity-settled share based payment scheme		(0.6)	-
Total recognised gains for the year		19.3	18.1

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

BALANCE SHEET

at 31 March 2007

		2007	2006
	Note	£m	£m
Fixed assets	6	218.7	197.0
Investments - Loans to ultimate UK holding company	7	68.5	68.5
Current assets			
Stocks	8	0.8	0.7
Debtors	9	20.8	19.1
Other investments	12	28.0	39.5
Cash at bank	12	2.8	1.0
		<u>52.4</u>	<u>60.3</u>
Creditors: amounts falling due within one year			
Short term borrowings and derivatives	10 and 12	(2.5)	(2.5)
Other creditors	11	(24.1)	(19.2)
		<u>(26.6)</u>	<u>(21.7)</u>
Net current assets		<u>25.8</u>	<u>38.6</u>
Total assets less current liabilities		313.0	304.1
Creditors: amounts falling due after more than one year	12	(204.6)	(204.2)
8.75% irredeemable cumulative preference shares	12	(12.5)	(12.5)
Deferred income	13	(9.4)	(9.6)
Provisions for liabilities	16	(19.7)	(18.8)
Retirement benefit scheme surplus, net of attributable deferred taxation	21	8.3	3.1
Net assets		<u>75.1</u>	<u>62.1</u>
Capital and reserves			
Called up share capital	17	6.0	6.0
Share premium account	18	4.4	4.4
Share option reserve	18	-	0.8
Other reserves	18	5.8	5.8
Profit and loss account	18	58.9	45.1
Shareholders' funds		<u>75.1</u>	<u>62.1</u>

The accounts were approved by the Board on 31 May 2007 and signed on its behalf by -

A Parsons, Director

A Nield, Director

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

CASH FLOW STATEMENT

for the year ended 31 March 2007

		2007	2006
	Note	£m	£m
Net cash inflow from operating activities	22(a)	42.6	35.1
Returns on investments and servicing of finance			
Interest received		6.0	5.3
Interest paid on term loans and debentures		(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		(1.0)	(1.7)
Capital expenditure and investing activities			
Purchase of tangible fixed assets		(41.2)	(22.5)
Contributions received		3.5	3.1
Loan advanced to ultimate UK holding company		-	(21.5)
		(37.7)	(40.9)
Equity dividends paid	19	(6.3)	(10.2)
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)
		(2.5)	52.7
Increase/(decrease) in cash	22(b)	1.8	(0.6)
Cash, beginning of year		1.0	1.6
Cash, end of year		2.8	1.0

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

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
	11.3	
Wages, salaries and severance costs		11.3
Social security costs	1.1	0.9
Pension costs (note 21(b))	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	<u>(3.1)</u>	<u>(2.8)</u>
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	30.6	27.2
Total other operating costs	<u>31.0</u>	<u>27.6</u>
Depreciation of tangible fixed assets (note 6)		
On owned assets	16.9	16.8
On leased assets	2.0	1.8
Amortisation of related deferred income (note 13)	(0.3)	(0.4)
Amortisation of S41 contributions received in 2005/06, now reversed	0.3	(0.3)
Net depreciation	<u>18.9</u>	<u>17.9</u>
Total operating costs	<u>61.1</u>	<u>57.0</u>

- (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 on pages 18 - 22.

- (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

	2007		2006	
	£m	£m	£m	£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:				
Loan 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>
		6.7		6.1
Fair value adjustment to swap liability		-		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 FRS25.

4. TAXATION ON PROFIT ON ORDINARY ACTIVITIES

	2007	2006
	£m	£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	<u>(1.1)</u>	<u>(0.1)</u>
	<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	<u>(2.7)</u>	<u>0.6</u>
	<u>0.7</u>	<u>3.5</u>
Tax on profit on ordinary activities	<u>2.5</u>	<u>6.8</u>

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. None of these measures have as yet been enacted and are therefore not reflected in these financial statements. 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	18.9	18.4
Profit on ordinary activities multiplied by standard rate of Corporation Tax in the United Kingdom at 30% (2006 - 30%)	5.7	5.5
Effects of:		
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)
	2.4	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	1.8	3.3

5. EARNINGS PER ORDINARY SHARE

	2007	2006
	m	m
Earnings per ordinary share have been calculated as follows -		
On average number of ordinary shares in issue during the year -		
Earnings attributable to ordinary shares	£16.4	£11.6
Weighted average number of ordinary shares	6.0	6.0

As the company has no obligation to issue further shares, disclosure of earnings per share on a fully diluted basis is not required.

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	175.2	4.8	370.1
Additions	-	-	-	45.5	45.5
Capitalisation of completed assets	3.6	2.5	16.7	(22.8)	-
Disposals	(0.1)	(1.1)	-	-	(1.2)
Grants and contributions	(0.1)	-	(3.8)	-	(3.9)
Contributions received in 2005/06 now reclassified (accounting policy note (a))	-	-	(1.0)	-	(1.0)
At 31 March 2007	164.9	30.0	187.1	27.5	409.5
Depreciation					
At 1 April 2006	64.4	18.8	89.9	-	173.1
Charge for year	5.9	3.2	9.8	-	18.9
Disposals	(0.1)	(1.1)	-	-	(1.2)
At 31 March 2007	70.2	20.9	99.7	-	190.8
Net book value at 31 March 2007	94.7	9.1	87.4	27.5	218.7
At 31 March 2006	97.1	9.8	85.3	4.8	197.0

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

For the purpose of this table no apportionment has been made of the infrastructure renewals charge included within depreciation in note 6(a) above.

- (d) The net book value of infrastructure assets is stated after the deduction of contributions of £46.6m (2006 - £42.7m) as explained in Accounting Policy d.

7. INVESTMENT - LOANS TO BRISTOL WATER GROUP LTD

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

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	2006
	£m	£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/(issue costs) arising in the year	-	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	4.8	5.0

The net premiums/(issue 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	2006
	£m	£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
	4.8	5.0

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
Unamortised debt issue premiums/(costs)	4.8	-	-	4.8	5.0
Debentures (listed on the London Stock Exchange) -					
4.00% Consolidated irredeemable	-	-	1.4	1.4	1.4
4.25%, 4.00% and 3.50% perpetual irredeemable debentures (in total, each under £0.1m individually)	-	-	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, premiums/discounts were determined to reflect prevailing market conditions. The net premiums/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	9.6	8.6
Less adjustment in respect of revised accounting policy (note a)	(0.7)	-
	8.9	8.6
Contributions received	0.8	1.7
Less amortised	(0.3)	(0.7)
End of year	9.4	9.6

14 FINANCIAL RISK MANAGEMENT

Financial risk factors

The company's main financial instruments comprise:

- 8.75% irredeemable cumulative preference shares
- borrowings and cash
- various items, such as trade debtors and trade creditors, that arise directly from its operations
- two long-term loans made to Bristol Water Group Ltd.

The company has in previous years also entered into interest rate swaps (the last of which expired this year) and gilt locks to manage the interest rate risk arising from its operations and sources of finance. It is the company's policy not to trade in financial instruments.

The company's significant debt financing exposes it to a variety of financial risks that include the effect of changes in debt market prices, credit risks, liquidity and interest rates. The company has in place a risk management programme that seeks to limit the adverse effects on the financial performance of the group.

The Board is responsible for setting the risk management policies applied by the company. The policies are implemented by the treasury department. The treasury department has a policies and procedures manual that sets out specific guidelines to manage interest rate risk, credit risk and the use of financial instruments to manage these risks.

(a) Foreign exchange risk

The company trades almost exclusively within the United Kingdom and all material purchases of capital equipment are denominated in sterling. Accordingly the company has no material foreign exchange risk.

(b) Interest rate risk of financial assets

The financial assets include cash at bank and short-term deposits which are all denominated in sterling. Cash and short-term deposits have been placed with banks and building societies on a rolling basis of up to one year earning interest based on LIBID equivalents. There are also interest-bearing fixed rate loans totalling £68.5m (2006 - £68.5m) to Bristol Water Group Ltd.

(c) Interest rate risk of financial liabilities

The financial liabilities consist of interest-bearing loans, debentures, finance leases and 8.75% irredeemable cumulative preference shares. The company has used an interest-rate swap as a cash flow hedge of future interest payments, which has the effect of increasing the proportion of fixed interest debt.

The company's policy is to maintain the majority of its net debt on a fixed or index-linked interest basis. At the year-end 42% (2006 - 51%) of the company's financial liabilities, including the 8.75% irredeemable cumulative preference shares, were at fixed rates, and 86% (2006 - 94%) of the company's financial liabilities, including the 8.75% irredeemable cumulative preference shares, were at fixed or indexed rates. The residue were at floating rates.

The company's current intention is to maintain a future interest rate management profile consisting of financial liabilities at either fixed or index-linked rates amounting to 70% or more of such liabilities. This policy will be kept under review.

(d) Credit risk

The company is required by the Water Industry Act 1991 to supply water to all potential customers. In the event of non-payment by commercial customers, but not domestic customers, the company has a right of disconnection. For all customers the company has implemented policies and procedures designed to assess the risk of further non-payment and recoup debts.

(e) Liquidity risk

It is company policy to ensure continuity of funding. At the year-end 82% (2006 - 83%) of its financial liabilities, including 8.75% irredeemable cumulative preference shares, mature after five years or are irredeemable.

The company actively maintains a mixture of long-term and short-term committed facilities that are designed to ensure the company has sufficient funds for operations.

At 31 March 2006 and 31 March 2007, the company had a £30m committed undrawn borrowing facility with an expiry date of May 2010. The facility is floating rate and incurs non-utilisation fees at market rates.

Under the terms of the Artesian loan agreements the company is required to maintain a specified sum in nominated accounts to cover estimated debt service payments arising during the following year. These funds, currently amounting to approximately £5.5m, are therefore not available for other operational use or distribution to shareholders.

(f) Price risk

The company is exposed to risk in prices for materials and services used in its treatment processes, including for chemicals and electricity. Risk is minimised through actively monitoring the market and by the use of fixed price supply contracts extending over more than one year where considered appropriate.

(g) Covenant compliance risk

Under the terms of its principal debt agreements the company is required to comply with covenants relating to minimum levels of interest cover and to maximum levels of net debt in relation to regulatory capital value. Failure to comply may result in various restrictions being imposed upon the company. Risk is minimised through continuous monitoring of the relevant ratios in both emerging and forecast results, and by close control of operating cash flows and capital investment programmes.

Derivative financial instruments and hedge accounting

The company documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The company also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair value or cash flows of hedged items.

In accordance with the provisions of FRS25, 'Financial Instruments: Disclosure and Presentation', and FRS26, 'Financial Instruments: Recognition and Measurement', the company valued its interest-rate swap at fair value at 31 March 2006. The swap expired on 25 September 2006. All other financial instruments are stated at cost, indexed cost or amortised cost.

15. FINANCIAL INSTRUMENTS

Fair value estimation

The fair value of the company's interest-rate swap was based on the market price of comparable instruments at the balance sheet date where they are publicly traded.

The fair values of short-term deposits, loans and overdrafts with a maturity of less than one year are assumed to approximate to their book values.

In the case of bank loans and other loans due in more than one year the fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate available to the company for similar financial instruments.

The fair value of the company's debentures has been calculated by discounting the expected cash flows at prevailing market rates including an estimated margin over gilts. Fixed rate bank loans and leases have been discounted on a similar basis but to LIBOR futures. In the case of floating rate facilities the fair values approximate to the carrying values as payments are reset to market rates at intervals of one year or less. Fixed rate loans from Artesian Finance II plc have been discounted by reference to the UK Government fixed rate gilt 2028 plus an estimated margin. Index-linked loans from Artesian Finance plc have been discounted by reference to the UK Government index-linked gilt 2035 plus an estimated margin.

The company's preference shares (shown as debt within these financial statements) are listed on the London Stock Exchange and their fair value is assumed to be their quoted market price.

The long-term loans to Bristol Water Group Ltd have been discounted by reference to the UK Government fixed rate gilt 2028 plus an estimated margin.

Interest rate swap

At 31 March 2006, the company was party to one interest rate swap which expired on 25 September 2006. The swap was designated against a £10m variable rate bank loan and £10m of variable rate leases. The swap exchanged LIBOR rates on a 3 monthly basis for a fixed rate of 7.72%. In accordance with FRS26, the liability arising under the swap agreement was recognised in the 2006 financial statements, as follows:

	2007	2006
	£m	£m
Liability:		
Due within one year	-	0.3
Due after one year	-	-
	<u>-</u>	<u>0.3</u>

Amounts recorded in the profit and loss account:

	£m	£m
Fair value adjustment (note 3)	<u>-</u>	<u>0.2</u>

In accordance with FRS26 "Financial Instruments: Recognition and Measurement" the company has reviewed all material contracts for embedded derivatives that are required to be separately accounted for if they do not meet the requirements set out in the standard. As a result of this review no embedded derivatives were identified.

There were no derivatives outstanding at the balance sheet date that were designated as cash flow or fair value hedges.

Fair values of financial assets and financial liabilities

Although the company does not intend to trade in any financial instruments, the following table provides a comparison, by category, of the carrying amounts and the fair value of the company's financial assets and financial liabilities. Where available, market values have been used to determine fair values. Where market values are not available, fair values have been calculated by discounting expected cash flows at prevailing interest rates.

Fair values of non-current borrowings

	31 March 2007		31 March 2006	
	Book value	Fair value	Book value	Fair value
	£m	£m	£m	£m
Primary financial instruments issued to finance the company				
Long-term borrowings	(204.6)	(226.8)	(204.2)	(233.5)
8.75% irredeemable cumulative preference shares	(12.5)	(17.7)	(12.5)	(19.2)
Primary financial instruments issued to finance Bristol Water Group Ltd				
Long-term loans	68.5	70.2	68.5	72.8
	<u>(148.6)</u>	<u>(174.3)</u>	<u>(148.2)</u>	<u>(179.9)</u>

The movement in the excess of the fair value of the long-term borrowings over book value is due to fluctuations in long-term discount rates.

Fair values of other financial assets and liabilities

	31 March 2007		31 March 2006	
	Book value	Fair value	Book value	Fair value
	£m	£m	£m	£m
Primary financial instruments held or issued to finance the company's operations:				
Cash at bank and short term deposits	30.8	30.8	40.5	40.5
Short-term borrowings	(2.5)	(2.5)	(2.2)	(2.2)
Derivative financial instruments held to manage the interest rate profile:				
Interest rate swaps - within one year	-	-	(0.3)	(0.3)
	28.3	28.3	38.0	38.0

In accordance with the terms of the Artesian loan agreements, cash at bank and on deposit includes the sum of £5.5m (2006 - £5.5m) held within nominated accounts to cover estimated debt service payments arising during the following year. These funds are therefore not available for other operational use or distribution to shareholders.

16. PROVISIONS FOR LIABILITIES

	2007 £m	2006 £m
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
	<u>38.7</u>	<u>33.2</u>
Effect of discounting:		
Retirement benefit obligations	(0.3)	-
Other	(15.7)	(13.1)
	<u>(16.0)</u>	<u>(13.1)</u>
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	<u>19.7</u>	<u>18.8</u>

Deferred tax movement:	2007 £m	2006 £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 scheme actuarial gains in the year	1.3	2.1
Charge (credit) to share options reserve	0.6	(0.6)
Provision carried forward at 31 March	<u>22.7</u>	<u>20.1</u>

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	<u>6.0</u>	<u>6.0</u>	<u>6.0</u>	<u>6.0</u>

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	45.1	62.1	54.2
Profit for year	-	-	-	-	16.4	16.4	11.6
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)
End of year	<u>6.0</u>	<u>4.4</u>	<u>-</u>	<u>5.8</u>	<u>58.9</u>	<u>75.1</u>	<u>62.1</u>

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

19. 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 FRS21 this dividend is not recognised in these accounts as a liability.

20. 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 Ltd 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.

21. RETIREMENT BENEFIT OBLIGATIONS

(a) Pension arrangements

Defined contribution schemes

The company operates defined contribution retirement benefit schemes for a number of employees. The total cost charged to income of £0.1m (2006: £0.1m) represents contributions payable to the scheme. As at 31 March 2007 and at the prior balance sheet date, all contributions due in respect of the current and prior reporting periods have been paid over to the scheme.

Defined benefit schemes

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. The company's membership of WCPS is through a separate section of the scheme. The assets of the section are held separately from those of the company and are invested by discretionary fund managers appointed by the trustees of the Scheme. The section has been closed to new entrants and all new eligible employees are offered stakeholder pensions.

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.

The financial position of the section is determined by an independent actuary (Lane, Clark & Peacock). The most recent actuarial valuation of the scheme was carried out at 1 April 2005 by Lane, Clark & Peacock.

In 2006/07, in connection with new financing and return to shareholders by the then ultimate parent company, the company made a one-off contribution to WCPS of £7.0m. The company also agreed to make additional contributions of £1m in each of the four years beginning 1 April 2006 and a further £0.9m in 2010/11. The amounts are in addition to the normal pension contributions required by the WCPS trustee.

(b) Accounting under FRS17 "Retirement Benefits"

Basis of valuation

The formal actuarial valuation of the Bristol Water plc section of the Water Companies' Pension Scheme as at 1 April 2005 was updated to 31 March 2007, by Lane, Clark & Peacock, using the following major assumptions in accordance with FRS17:

	2007	2006	2005
Assumptions:			
RPI Inflation	3.2%	3.0%	2.9%
Pension increases in payment (RPI)	3.2%	3.0%	2.9%
Pension increases in payment (LPI)	3.1%	3.0%	2.7%
Salary increases	5.2%	5.0%	4.9%
Discount rate	5.4%	5.0%	5.4%

Asset distribution and expected return

The following table sets out the key assumptions used for the valuation of the company's section of WCPS. The table also sets out as at the accounting date the fair value of the assets, a breakdown of the assets into the main asset classes, the present value of the section liabilities, and the resulting surplus/(deficit).

	Expected long term rate of return			Market values of section assets		
	2007	2006	2005	2007	2006	2005
				£m	£m	£m
Equities	7.8%	7.4%	7.7%	61.9	78.8	63.2
Bonds	4.7%	4.3%	4.7%	69.3	46.9	34.9
Cash	5.4%	4.5%	4.7%	0.1	0.1	0.1
Market value of section assets				131.3	125.8	98.2
Present value of liabilities				(120.0)	(121.4)	(110.1)
Surplus/(deficit) in the section				11.3	4.4	(11.9)
Deferred taxation				(3.0)	(1.3)	3.3
Net pension asset/(liability)				8.3	3.1	(8.6)

Contributions

Contributions paid in the year to the section including those from Bristol Wessex Billing Services Ltd were £2.4m (2006 - £9.8m). Contributions this year include £1.4m of regular employer contributions and £1.0m of additional contribution as described previously. For normal employer contributions, during the year the company was required to contribute at the rates of 21% (2006 - 21%) of relevant payroll costs for the main sub section and 10% (2006 - 10%) for the alternative benefits sub section.

As described in note 21(a), the company has agreed to make further additional contributions to the scheme.

Analysis of charges to Profit and Loss Account:

	2007	2006
	£m	£m
Analysis of the amount charged to operating profit		
Employer's part of current service cost	1.9	1.9
Past service cost	-	0.4
	1.9	2.3
Less, past service costs charged to restructuring provision	-	(0.4)
Total operating charge	1.9	1.9
	2007	2006
	£m	£m
Analysis of the amount credited/(charged) to other finance income		
Expected return on pension section assets	7.5	6.8
Interest on post-retirement liabilities	(6.0)	(5.9)
Net return – credit to other finance income	1.5	0.9

	2007 £m	2006 £m
Analysis of amount recognised in the Statement of Total Recognised Gains and Losses (STRGL)		
Actual return less expected return on pension section assets	(0.2)	15.2
Experience gains arising on section liabilities	0.7	2.1
Changes in assumptions underlying the present value of section liabilities	4.3	(9.5)
Actuarial gain recognised in STRGL	4.8	7.8

	2007 £m	2006 £m
Movement in section pre tax financial position during the year		
Surplus (deficit) in section at beginning of the year	4.4	(11.9)
Movement in year:		
Current service cost (employee and employer)	(2.4)	(2.3)
Aggregate regular contributions (employee and employer)	2.0	1.8
Additional contributions	1.0	7.0
Additional contribution in relation to restructuring	-	1.5
Past service cost	-	(0.4)
Credit to other finance income	1.5	0.9
Actuarial gain recognised in STRGL	4.8	7.8
Surplus in section at end of the year	11.3	4.4

The history of experience gains and losses is:

Difference between expected and actual return on section assets:

Amount	(0.2)	15.2
Percentage of section assets	0%	12%

Experience gains and losses on section liabilities

Amount – gain	0.7	2.1
Percentage of the present value of the section liabilities	1%	2%

Changes in assumptions underlying the FRS17 value of the section liabilities

Amount – gain/(loss)	4.3	(9.5)
Percentage of the present value of the section liabilities	4%	(8)%

Total amount recognised in STRGL

Amount – gain	4.8	7.8
Percentage of the present value of the section liabilities	4%	6%

22. SUPPLEMENTARY CASH FLOW INFORMATION

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

	2007	2006
	£m	£m
Operating profit	25.2	24.9
Depreciation, net of amortisation of deferred income	18.9	17.9
Difference between pension charges and normal contributions	0.5	0.6
Equity-settled share based payments non-cash charge	-	0.2
	<hr/>	
Cash flow from operations	44.6	43.6
Working capital movements -		
Stocks	(0.1)	(0.1)
Debtors	(1.8)	(0.5)
Creditors and provisions	0.9	0.6
Additional contributions to pension scheme, including payments in respect of restructuring	(1.0)	(8.5)
	<hr/>	
Net cash inflow from operating activities	42.6	35.1

(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
	<hr/>	
	(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)
	<hr/>	
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

23. SHARE-BASED PAYMENTS

Equity-settled share option plan

From 1 April 2006 until the acquisition of BWG by Agbar, the Bristol Water Group plc Savings Related Share Option Scheme was open to all employees who had attained one year's service with the group. The plan provided for a purchase price equal to the daily average market price of the group shares on the date of grant, less 20 per cent. Share options could be granted during a 4-week period each year. The share options so granted were exercisable at the end of an employee share savings plan with a life of either 3 or 5 years. Options remaining unexercised after a period of 3 years and 6 months or 5 years and 6 months from the date of grant expired. Furthermore, options were forfeited if the employee left the group before the options vested.

Potential issues of ordinary shares

At 1 April 2006 the total number of shares subject to options in the Employee Share Options Scheme (including those granted prior to 7 November 2002) and the periods in which they may be exercised are as follows:

	At £1.636	At £2.032	At £1.904	At £3.180	At £5.452
Exercise period					
2006-07	52,355	-	192,310	-	-
2007-08	-	75,995	-	63,983	-
2008-09	-	-	71,005	-	45,543
2009-10	-	-	-	26,750	-
2010-11	-	-	-	-	22,500

The company has fair valued share options granted since 7 November 2002. Options granted since that date were valued using the Black-Scholes option-pricing model. The fair value per option granted and the assumptions used in the calculation were as follows:

	18 July 2005	16 July 2004	15 July 2003
Grant date			
Share price at grant date	£6.815	£3.975	£2.380
Exercise price	£5.452	£3.180	£1.904
Shares under option	69,880	100,081	353,775
Vesting period (years)	3 & 5	3 & 5	3 & 5
Expected volatility	21.07%	22.69%	20.58%
Option life (years)	3, 5	3, 5	3, 5
Expected life (years)	3, 5	3, 5	3, 5
Risk free rate	4.50%	4.50%	4.50%
Expected dividends expressed as a dividend yield	5.00%	5.00%	5.75%
Possibility of ceasing employment before vesting	5.00%	5.00%	5.00%
Weighted average fair value per option	126.40p	76.84p	43.63p

The expected volatility was based on historical volatility over a 5-year period. The expected life was the average expected period to exercise. The risk free rate of return was the yield on zero-coupon UK government bonds of a term consistent with the assumed option life.

A reconciliation of option movements during the period from 1 April 2006 to the closure of the plan in June 2006 is shown below:

	Number	Weighted average exercise price (£)
Outstanding at 1 April 2006	420,091	2.750
Granted	-	-
Forfeited	(129,483)	3.720
Exercised	(292,608)	2.321
Outstanding at 31 March 2007	Nil	
Exercisable at 31 March 2007	Nil	

The plan was terminated following the acquisition of Bristol Water Group plc by Agbar.

24. 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:

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.

Trading transactions

During the year the company entered into the following trading transactions with related parties

	Sales of goods and services		Purchases of goods and services	
	2007	2006	2007	2006
	£m	£m	£m	£m
Members of the BWG group				
Bristol Water Group plc management charges	0.1	-	0.2	0.3
Joint ventures of the BWG group				
Bristol Wessex Billing Services Limited (BWBSL)				
- management charges	-	-	2.0	1.9
- capital expenditure	-	-	-	0.2
- other recharges	-	-	0.2	0.1
	0.1	-	2.4	2.5
	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

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.

Remuneration of key management personnel

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

25. 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.

Approximately 49.7% of the share capital of Agbar is currently controlled by the French group Suez and the Spanish bank La Caixa. In April 2007 Suez, La Caixa and their joint venture Hisusa made a bid for the entire share capital of Agbar. They had already secured a further 6.7% through an irrevocable undertaking. 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.

26. 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.

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF BRISTOL WATER PLC

We have audited the financial statements of Bristol Water plc for the year ended 31 March 2007 which comprise the Profit and Loss Account, the Balance Sheet, the Cash Flow Statement, the Statement of Total Recognised Gains and Losses and the related notes 1 to 26. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

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

We review whether the Corporate Governance Statement reflects the company's compliance with the nine provisions of the 2003 Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the company's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report as described in the contents section and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any further information outside the Annual Report.

Basis of audit opinion

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

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

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 March 2007 and of its profit for the year then ended;
- the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.

Deloitte & Touche LLP

Chartered Accountants and Registered Auditors

Bristol, United Kingdom

31 May 2007

Note: *The maintenance and integrity of the Bristol Water website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.*

FINANCIAL HISTORY

PROFIT AND LOSS ACCOUNTS	2007	2006	2005	2004	2003
Years ended 31 March	£m	£m	£m	£m	£m
Turnover	86.3	81.9	70.6	70.6	70.0
Operating profit	25.2	24.9	17.1	19.6	19.4
Interest and irredeemable preference share dividends	(7.8)	(7.4)	(7.2)	(6.2)	(7.0)
Net finance income/(expense) on retirement benefit obligations	1.5	0.9	0.8	(0.2)	2.3
Profit before taxation	18.9	18.4	10.7	13.2	14.7
Taxation	(2.5)	(6.8)	(1.6)	(2.5)	(7.8)
Profit after taxation	16.4	11.6	9.1	10.7	6.9
Dividends paid	6.3	10.2	7.3	15.9	5.6
BALANCE SHEETS	2007	2006	2005	2004	2003
At 31 March	£m	£m	£m	£m	£m
Fixed assets	218.7	197.0	195.6	193.8	184.7
Loan to Bristol Water Group Ltd	68.5	68.5	47.0	47.0	-
Net current assets	25.8	38.6	9.2	11.6	0.4
Total assets less current liabilities	313.0	304.1	251.8	252.4	185.1
Debt due after one year, excluding irredeemable preference shares	(204.6)	(204.2)	(148.6)	(151.5)	(79.3)
Irredeemable preference shares	(12.5)	(12.5)	(12.5)	(12.5)	(12.5)
Deferred income	(9.4)	(9.6)	(8.6)	(8.5)	(8.4)
Provisions	(19.7)	(18.8)	(19.3)	(18.7)	(18.8)
Retirement benefit obligations net of deferred taxation	8.3	3.1	(8.6)	(10.0)	(13.7)
Net operating assets	75.1	62.1	54.2	51.2	52.4
CASH FLOW	2007	2006	2005	2004	2003
Years ended 31 March	£m	£m	£m	£m	£m
Cash flow from operations	42.6	35.1	34.1	33.4	29.7
Interest and irredeemable preference share dividends paid	(4.8)	(6.5)	(6.4)	(7.8)	(6.7)
Tax paid	(1.0)	(1.7)	(1.9)	(3.0)	(3.0)
Capital expenditure net of contributions	(37.7)	(19.4)	(16.4)	(24.6)	(16.1)
Loan to Bristol Water Group Ltd	-	(21.5)	-	(47.0)	-
Dividends paid on equity shares	(6.3)	(10.2)	(7.3)	(15.9)	(5.6)
Cash flow before management of liquid resources and financing	(7.2)	(24.2)	2.1	(64.9)	(1.7)
Management of liquid resources	11.5	(29.1)	5.4	(9.4)	7.5
Net (decrease)/increase in financing	(2.5)	52.7	(7.5)	72.7	(3.3)
Increase/(decrease) in cash	1.8	(0.6)	-	(1.6)	2.5

Notes: All comparative data have been restated where necessary, and possible, to conform to current accounting practices except as indicated in accounting policy note a. All data includes exceptional items where relevant.