NORTHUMBRIAN WATER GROUP LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS FOR

THE YEAR ENDED

31 MARCH 2012

Registered Number 4760441

Contents

Cautionary statement
This annual report contains certain statements with respect to the future operations, performance and financial condition of the Group. By their nature, these statements involve uncertainty since future events and circumstances can cause results and developments to differ materially from those forecast. Such statements reflect knowledge and information available at the date of preparation of this annual report and the Company undertakes no obligation to update such statements. Nothing in this annual report should be construed as a profit forecast. Certain regulatory performance data contained in this annual report is subject to regulatory audit.

Directors' report

The directors of Northumbrian Water Group Limited (NWG or the Company) are pleased to present their report on the affairs of the Company, along with the audited financial statements and the auditor's report for the year ended 31 March 2012.

Business Overview

Change of controlling party
On 14 October 2011, Northumbrian Water Group plc was acquired by UK Water (2011) Limited (UKW), its shares were de-listed from the London Stock Exchange and it was re-registered as a private limited company. UKW is indirectly wholly owned by a consortium comprising Cheung Kong Infrastructure Holdings Limited, Cheung Kong (Holdings) Limited and Li Ka Shing Foundation Limited.

Directors
The directors who served during the year were as follows:

A J Hunter	Non-Executive Chairman (appointed 14/10/11)
H Mottram OBE	Chief Executive Officer
C M Green	Finance Director
M Fay CBE	Independent Non-Executive Director
Dr S Lyster	Independent Non-Executive Director (appointed 1/4/11)
L S Chan	Alternate Director (appointed 14/10/11)
F R Frame	Non-Executive Director (appointed 4/11/11)
T C E Ip	Non-Executive Director (appointed 14/10/11)
H L Kam	Non-Executive Director (appointed 14/10/11)
S H Luk	Alternate Director (appointed 14/10/11)
D N Macrae	Non-Executive Director (appointed 14/10/11)
M A B Nègre	Non-Executive Director
P F Rew	Independent Non-Executive Director
Sir D Wanless	Non-Executive Chairman (resigned 14/10/11)
A J Scott-Barrett	Independent Non-Executive Director (resigned 14/10/11)
Sir A P Brown	Non-Executive Director (resigned 20/10/11)
C R Lamoureux	Non-Executive Director (resigned 28/7/11)

The Board is very sorry to report the untimely death of Sir Derek Wanless, who died on 22 May 2012, after a short illness. Sir Derek joined the board of NWG in December 2003 and chaired its board between July 2006 and October 2011. The Board wishes to express its thanks for Sir Derek's tremendous contribution during a time of significant change.

Principal Activities

Northumbrian Water Group
NWG owns a number of companies which, together with NWG, form the Group. The largest of these companies, Northumbrian Water Limited (NWL), is one of the ten regulated water and sewerage

businesses in England and Wales. The emphasis given to NWL throughout this report, reflects its importance to the overall performance of the Group.

Northumbrian Water Limited
NWL operates in the north east of England, where it trades as Northumbrian Water, and in the south east of England, where it trades as Essex & Suffolk Water. Northumbrian Water currently provides water and sewerage services to 2.7 million people and Essex & Suffolk Water provides water services to 1.8 million people in a combined area of over 12,260 square kilometres.

NWL operates an extensive asset base, which includes:

44	impounding reservoirs
57	water treatment works
344	water pumping stations
338	water service reservoirs
25,545km	water mains
418	sewage treatment works
765	sewage pumping stations
29,724km	sewers, including the transfer of 13,510km of private drains and sewers on 1 October 2011

NWL currently supplies over 1,150 megalitres of drinking quality water per day. This water is drawn from reservoirs, where it is collected and stored, rivers and groundwater sources. It is treated at our works before it is delivered by a network of pipes to homes and businesses.

In the north east of England waste water is then collected from these properties via the sewerage network and treated at our works before it is returned to the environment as either clean water or sludge which can be recycled as fertiliser or used to generate energy.

Water and waste water contracts
NWG controls a number of special purpose companies which have water and waste water contracts in Scotland, Ireland and Gibraltar.

Our market

In the north east, NWL's business comprises the supply of both potable and raw water and the collection, treatment and disposal of sewage and sewage sludge. In this region, there has been a gradual fall in overall water demand in recent decades as a consequence of a reduction in industrial demand for water and this trend is expected to continue. The north east compares well to the rest of the country as far as water resources are concerned and our major regional rivers can all be supported by Kielder Water. This provides very high security of supply for our customers. We also provide the highest levels of compliance for waste water across this area ensuring that we can return the water and sewage sludge to the environment satisfactorily whilst meeting the demands of all customers. Bran Sands is particularly important in this respect as it supports the heavily industrialised area within Teesside by treating its waste. The advanced anaerobic digestion (AAD) plant there is now operating effectively and helping us to build our use of renewable energy. A second AAD plant at Howdon in Tyneside will come into operation in 2012.

In the south east, NWL supplies potable water only. This is a water scarce region that is forecast to experience further economic and population growth in the medium term. This area has also seen a reduction in demand from heavy industry, but there has been an increase in population with further increases forecast. Supplies are currently not secure in a severe drought but the project to increase the capacity of Abberton reservoir, near Colchester, coupled with ongoing demand management measures, will secure supplies to the Essex area for the foreseeable future. The Abberton scheme will be complete in 2013 and the additional capacity available for supply the following year.

Our water and sewerage services in the north east will cost, in 2012/13 prices, an average householder 96 pence per day and, in Essex and Suffolk, 60 pence for water only.

The Water Services Regulation Authority (Ofwat), as the economic regulator, sets price limits for companies in England and Wales every five years. 2011/12 was the second year in the current five year investment plan. This regulation is performance based and companies are measured in terms of efficiencies related to operating costs, capital programmes and financing as well as their general operations. The regulated revenue of NWL is set by reference to the rate of inflation, measured by the Retail Price Index (RPI), as well as an adjustment factor referred to as ‘k’. The profile of ‘k’ for the current five year period is shown below:

	2010/11	2011/12	2012/13	2013/14	2014/15
k (%)	5.0	3.8	0.9	0.0	(1.0)

Regulatory and legislative framework
As a monopoly supplier of an essential public service, the UK water industry operates within a demanding regulatory environment.

Ofwat regulates prices and levels of customer service, while the Drinking Water Inspectorate (DWI) monitors drinking water quality and the Environment Agency (EA) covers environmental protection. Customers’ interests are represented by the Consumer Council for Water (CCWater).

We aim to maintain good working relationships with our regulators and with regional organisations, such as local authorities, which have an interest in the services we provide and can influence our business. This is particularly important following Government reviews of the regulators, changes in regulatory reporting and proposals to legislate in the sector following the publication of a White Paper during the period.

We are an active member of Water UK, the industry association which represents all UK water and waste water service suppliers at national and European level. It provides a very effective framework for the industry to engage with Government, regulators, stakeholder organisations and the public and helps to develop policy and improve understanding of the industry. We also meet regularly with national, regional and local authorities and other appropriate organisations to explain our activities and related issues.

2011/12 Review

NWL was successful in meeting many of the targets in its detailed balanced scorecard during the year. We improved in 26 of our 28 targets and achieved or exceeded 19 of them. Most notable were the improvements in our Service Incentive Mechanism (SIM) score for customer service, the reduction in the number of interruptions to supply and our position on leakage. We were also very pleased to remain amongst the industry leaders in sewage treatment performance.

This report will focus on many highlights throughout the year but the development of our work to extend Abberton reservoir and the construction of our second AAD plant at Howdon, after the successful operation at Bran Sands, are particularly notable.

We also continued to receive external recognition for our activities. For the second year running, the Ethisphere Institute listed NWG as one of the most ethical companies in the world, one of only seven

UK only companies chosen and the only water utility selected worldwide. This recognises the impact we have on underpinning the communities in which we operate and also recognises the longstanding relationships with key industrial and commercial customers.

We continue to be actively involved in the business community in all operating areas through direct membership and involvement in the councils/boards of the Confederation of British Industry (CBI), Chambers of Commerce and other similar organisations. Our Chief Executive Officer (CEO), Heidi Mottram, is involved in a number of organisations which we believe can influence the future of the Company and locally, she is Deputy Chair of the CBI Council and a member of its national Infrastructure Board. Heidi has also joined the Government's Green Economy Council as the water industry representative and we hope that the Council can bring a real influence to the development of policy relating to a low carbon economy.

This year, industrial demand has deteriorated, with some prolonged shutdowns as a result of the economic situation and lower volumes at many of our smaller commercial customers. Domestic demand has also started to reduce in some areas, as customers have become aware of the restrictions in other parts of the country and the importance of using water wisely. We continue to monitor the situation and work closely with our key industrial customers. The collection of income remains a key focus for us, particularly in a difficult economic climate.

Transferred drains and sewers

Water and sewerage companies were required to adopt certain drains and sewers on 1 October 2011, which were previously in private ownership. For NWL, the estimated length of adopted assets is 13,510km, nearly doubling the length of sewers to be operated and maintained. Whilst the transfer took place smoothly, this generated a major increase in activity for the business which, in turn, increased operating costs. Although customer contact and job volumes were initially lower than anticipated, they have been gradually increasing month on month. Positive feedback has been received from our customers via our customer feedback surveys. We are continuing to work closely with other water companies to share information and experiences to ensure we deliver the most practical and cost effective solutions for customers. The transfer was valued at a nil fair value, as the net present value of the incremental cash flows arising as a result of the adoption were considered insignificant.

Legislative changes

We broadly support the Government's policy intention for the water industry, as laid out in the Water White Paper – 'Water for life'. We welcome the desire to build on the strengths of the current industry structure and strongly agree that a stable business and regulatory environment is vital if investor confidence is to be retained, so that the investment required over the coming decades can continue to be financed at a cost our customers can afford.

NWL is very keen to work closely with Defra and the industry regulators to ensure the Government's policies are implemented successfully.

We are pleased to have had the opportunity to contribute to the consultation on draft regulation from Defra to introduce a duty on landlords to provide water companies with relevant details so that accurate bills can be issued to tenants. Applying section 45 of the Flood and Water Management Act 2010 should assist in collecting income from the private rented sector where bad debts have been relatively high.

Regulatory reform

NWL strongly supports Ofwat's newly introduced proportionate and risk-based approach to regulation. The decision to end the requirement for water companies to submit a lengthy annual report to Ofwat (the 'June Return'), and replace this with a Regulatory Risk and Compliance

Statement (RRCS) and a set of high level key performance indicators (KPIs), will significantly reduce the burden of regulatory reporting whilst enhancing companies' accountability.

This set of high level KPIs was published along with the RRCS on the NWL's website. To deliver the Company's vision of being 'the national leader in water and waste water services', we have incorporated these targets within our own internal targets.

Ofwat has recently published its 'Future price limits - statement of principles' document setting out the high level principles it intends to use to set price limits in the future. We welcome the six key principles: targeted price controls; proportionate price setting; effective incentives; ownership, accountability and innovation; flexibility and responsiveness; transparency and predictability. Establishing these principles should help to provide stable and predictable regulation in the longer term.

NWL particularly welcomes the continued commitment to the Regulatory Capital Value for the long term and confirmation that RPI remains the most appropriate index to use for tariff setting and strongly supports the focus on outcome based regulation and the increased role for customers at price reviews. We support the introduction of separate wholesale and retail price controls in line with the White Paper.

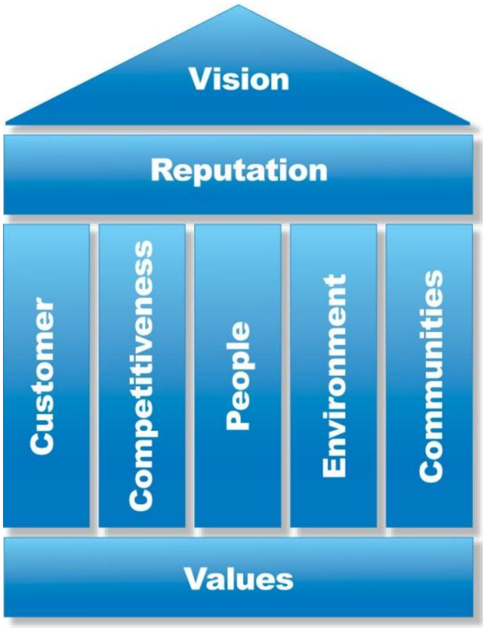
Some of Ofwat's more detailed proposals, including a water service network plus non-binding price control, require further justification. The additional incentive mechanisms proposed, including the totex mechanism, add substantial complexity and a lot of work is required to develop these concepts into a workable methodology. We have signalled our willingness to work constructively with Ofwat and offer any assistance we can in developing a practical and robust price review methodology that will deliver the right outcome for customers.

Business Strategy and Objectives

Our vision
The Group's vision is to be the national leader in the provision of sustainable water and waste water services.

Strategic direction
We want to continue to deliver value to customers and other stakeholders by focusing on our core competencies of water and waste water management. We underpin our drive to be the best with five strategic themes containing goals and targets that, when reached, will see our vision and our values delivered. 'Our Vision Our Values Our Way' has been shared with all our employees during a series of annual interactive roadshows and, as a result, there is clarity and energy throughout the Group which is driving the business forward.

The five themes described below are mutually supportive and achieving the right balance between them is essential to our success and reputation.



Customer focuses on delivering industry-leading customer service. Our relationship with customers is core to the success of our business and it is essential that they trust our service. Customer service is at the heart of the Company and all employees have a clear focus on getting things 'right first time every time'. Although we are required to meet regulated standards for customer service, this should not define our aspiration as the quality of our service must go beyond that.

Competitiveness will drive us to greater efficiency and, indeed, to be the most efficient water company. It is not just about driving cost down but using innovation to support our activities.

People are our greatest asset and we want to be recognised as a great company to work for with high levels of satisfaction from our employees. We will provide support and training and promote excellent employee relations.

Environment is critical to us and our stakeholders and we acknowledge our responsibilities to protect and enhance the natural environment. Our carbon management plan will help reduce our carbon footprint and we will adopt good environmental practice in all aspects of our activities.

Communities are important to us and we want to build strong relationships with the communities we serve. We will ensure that corporate responsibility is embedded in performance management and that we benchmark ourselves against the best companies.

We have agreed specific goals to help us achieve our vision against these themes, and have clear accountability for their achievement throughout the Company. These are measured in a balanced scorecard which assesses our performance against KPIs. This is reviewed by the Board, management team and employees on a monthly basis.

We believe that clear direction and goals are key to success, but just as important is a clear sense of values, and how we do things 'around here'. We have made a clear commitment to five core values.

One team – we work together consistently, promoting co-operation, to achieve our corporate objectives.

Customer focused – we aim to exceed the expectations of our external and internal customers.

Results driven – we take personal responsibility for achieving excellent business results.

Creative – we continuously strive for innovative and better ways to deliver our business.

Ethical – we are open and honest in meeting our commitments, with a responsible approach to the environment and our communities.

Corporate Responsibility

NWL is expected to provide a secure supply of water, a basic necessity for health, and to protect or enhance the environment when we return waste to it. Our stakeholders also expect us to:

- behave fairly and responsibly;
- use resources wisely;
- improve quality of life; and
- contribute to economic development.

We believe that sustainability helps to improve the performance of the Group and to achieve our business strategy and objectives. This is reflected in our business plan where our sustainability objectives are woven into our core business strategy. Our credentials for our work have been recognised and our customer research also highlights that customers value our work in the community and for the environment and it helps to build their trust in our work. Each aspect of the highlighted work in this report has a direct benefit to the Group, its community and its environment, such as cost saving, carbon reduction, environmental impact, skills development or leverage.

To ensure that sustainability runs throughout the business, we ensure that all parts of the Group are involved from the Board through to all employees.

Up to the point of the change of control, governance of our sustainability activity was led by our Corporate Responsibility Committee, a subcommittee of the NWL Board. From October 2011, governance was led by our Corporate Responsibility Management Group (CRMG) a sub-committee of the NWL Management Team. The CRMG will meet four times a year and non-executive directors and the CEO (who is directly accountable to the NWL and NWG boards for both the environment and sustainable development policies) will attend at least once to develop strategy and to inform the Board.

In addition, two Corporate Responsibility Advisory Groups (CRAGs) (one for each of Northumbrian and Essex & Suffolk regions) act as ‘critical friend’, helping to validate, guide and challenge NWL’s sustainability strategy and activities. The CRAGs are made up of senior representatives from key stakeholder organisations to reflect the main areas of our environment and communities’ strategy.

Performance measures

In order to measure delivery of our business plan and goals, the Group monitors performance using a balanced scorecard of KPIs. These indicators are spread across the themes of customer, competitiveness, people, environment and communities and targets have been set on a trajectory to deliver the company vision of being ‘the national leader in water and waste water services’.

Performance against additional financial KPIs is reported within the financial performance section later in this report.

In order to ensure alignment of the management team, this balanced scorecard now represents 80% of the criteria contributing to their annual bonus, with a further 20% available for the achievement of bespoke personal targets.

The table below details performance in 2011/12 against those KPIs and the targets that have been set for 2012/13. Performance in 2011/12 is discussed within the operating performance section later in this report. The definition of each measure is set out on pages 28 and 29.

Scorecard measure	Target 2011/12	Performance 2011/12	Target 2012/13
Customer			
Customer satisfaction			
- SIM quantitative score	174	162	115
- SIM qualitative score	4.40	4.33	4.50
Unplanned interruptions >6 hours			
- north	900	445	n/a
- south	600	161	n/a
- combined	n/a	n/a	1,500
Coliform incidents (no.)	15	21	7
Competitiveness [1]			
Profit before tax	set by Board	achieved	n/a
Capital efficiency	set by Board	removed	n/a
Earnings before interest and tax	n/a	n/a	set by Board
Cash available for distribution [1]	n/a	n/a	set by Board
People			
Engagement and satisfaction index (%) [2]	81	78	n/a
Employee engagement score [2]	n/a	n/a	1* best companies
Lost time reportable accidents (no.)	11	8	10
Environment			
Leakage (Mld)			
- north	147	130	147
- south	66	59	66
Sewage treatment works compliance (%)	100	99.4	100
Pollution incidents (categories 1 & 2)	3	11	3
Communities			
FTSE4Good accreditation [3]	retain status	n/a	n/a
BITC Platinum Plus accreditation	retain status	retained	retain status
Just an Hour participation (%) [3]	n/a	n/a	50

1 The competitiveness KPIs have been revised to take account of the new owners’ objectives. During the year, the capital efficiency target was removed.
2 The engagement and satisfaction index is derived from an internal employee survey. The employee engagement score is derived from the Sunday Times Best Companies survey. These surveys are carried out in alternate years.
3 FTSE4Good accreditation is no longer possible due to the Group’s de-listing, therefore, it has been replaced by a new KPI of ‘Just an Hour participation’.

Financial performance

NWG and NWL use a range of financial KPIs to monitor the financial standing of the businesses and to ensure that strong credit ratings are maintained. The definition of each measure is shown on page 29.

Performance against the financial KPIs is set out below:

	Target		Performance			
			Current year		Previous year	
KPI	NWG	NWL	NWG	NWL	NWG restated	NWL
Gearing to RCV (%)	<75	<70[1]	74	64[2]	68	56
Cash interest cover (times)	>2.5	>3.0	3.3	4.2	3.2	4
Cash flow to net debt (%)	>13	>13	15	18	16	20

Notes:
1. Less than 65% for the regulated business of NWL.
2. NWL's RCV, as advised by Ofwat, at 31 March 2012 was £3,550.0 million (2011: £3,318.4 million).

The basis of the Group gearing to RCV ratio has been revised to reflect net debt, excluding the fair value of loans acquired in 2003, divided by NWL's RCV, because the directors believe this is a better measure of the Group's credit risk. The prior year measure has been restated on a consistent basis.

The Group's gearing on the revised basis has increased from 68% to 74%, with net debt increasing by £352.9 million (15.6%) to £2,651.5 million over the year, while RCV has increased by 7.0% due principally to the increase in RPI.

Gearing at NWL, and for the regulated business, has increased to 64% and 63%, respectively, from 56%. This is principally due to increased net debt as a result of the payment of intra-Group dividends after the previous balance sheet date and a special dividend of £232.0m which was paid during the year, following the change of control.

The Group also prepares detailed medium term business plans and annual budgets, which are reviewed and submitted to the Board for approval. Targets are set to measure performance and regular financial forecasts are made. Business plans and budgets include an assessment of the key risks and success factors facing each business unit. On a monthly basis, management compares the actual operational and financial performance of each business with plan and budget and this is reported to the Board.

Financial results and dividends

NWG

Revenue for the year ended 31 March 2012 increased by 7.0% to £789.5 million (2011: £738.1 million). Water and sewerage charges at the Group's principal subsidiary, NWL, increased in line with the price review (final determination) allowance of 3.8% plus the November 2010 RPI of 4.7%. Income from the Group's water and waste water contracts increased by 5.3%.

Operating costs increased by £24.6 million (5.7%) to £458.5 million, principally reflecting movements at NWL, which are detailed below. Profit on ordinary activities before interest for the year was £331.0 million (2011: £304.2 million), an increase of 8.8%.

Net interest charges increased by £14.0 million within which net cash interest charges increased by £12.0 million. The non-cash element of the increase principally reflects inflation of the principal on the index linked bonds (£1.9 million) and the non-recurrence of one-off credits in the prior year relating to the acquisition of subordinated loan stock in CES and a termination discount on a finance lease (£7.5 million). There were partially offset by lower interest relating to the pension scheme (£5.8 million), higher capitalised interest (£1.3 million) and lower amortisation of fees and fair value adjustments (£0.3 million).

Profit on ordinary activities before tax for the year was £193.9 million, 7.1% higher than the previous year (2011: £181.0 million). The current tax charge reduced to £30.8 million (2011: £33.1 million) reflecting a reduction in the tax rate from 28% to 26%.

The deferred tax credit of £23.3 million (2011: £30.5 million) reflects a decrease in the Group's deferred tax liability of £43.1 million following the enactment of a reduction in the UK corporation tax rate from 26% to 24% with effect from 1 April 2012.

The effective tax rate for the period was 3.9% (2011: 1.4%) reflecting the impact of the deferred tax rate change. In the absence of the rate change, and other prior year items, the effective rate would have been 26%.

Capital investment for the Group was £310.2 million (2011: £219.9 million), including recognition of £23.0 million for assets adopted at £nil cash consideration, as required under IFRIC 18 Transfers of Assets from Customers (2011: £13.9 million).

NWL

Revenue was £737.4 million for the year ended 31 March 2012 (2011: £689.4 million). The increase is mainly due to the application of the final determination increase of 3.8%, and 4.7% in respect of RPI, on water and sewerage charges, which has been partially offset by lower demand from industrial customers.

Operating costs increased by £6.8 million (1.7%) to £398.6 million, principally reflecting increases in depreciation, manpower costs and carbon reduction commitment charges, partially offset by lower power commodity prices and the benefits of an efficiency programme.

Profit on ordinary activities before interest for the year was £338.8 million (2011: £297.6 million).

Capital investment in the regulated business for the period was £292.0 million, under regulatory accounting guidelines (2011: £221.5 million). This is slightly higher than the final determination profile, deflated by the Construction Industry Price Index, as a result of increased maintenance investment recovering from severe winter weather experienced the previous year. The construction works for the £150.0 million Abberton scheme, to secure water supply to 1.5 million customers in Essex, continued to make good progress and the scheme is ahead of schedule.

The efficiency programme instigated in the previous year progressed well, focussing on identifying and implementing sustainable operating cost efficiencies in order to achieve our medium term goal of being in the top efficiency band for both water and sewerage, as measured by Ofwat, by 2013/14.

Water and waste water contracts

Our water and waste water contracts in Scotland, Ireland and Gibraltar are all performing well and are in line with expectations. Revenue for the contracts increased to £42.1 million for the year ended 31 March 2012 (2011: £40.0 million), principally as a result of higher volumes in Gibraltar and Ayrshire. Profit on ordinary activities before interest was £10.0 million (2011: £9.5 million), due to the increased revenue partially offset by higher operating costs, particularly power.

The Group is involved in two projects to deliver long term PFI contracts with Scottish Water for waste water treatment. At CES, the Group has a 100% shareholding in both project and operating companies and the benefit of a 40 year contract. Funding was provided through a 37 year fixed interest rate corporate bond with the principal amortising from 2008. In Ayrshire, the Group has a 75% shareholding in the project company and a 100% shareholding in the company that operates the three effluent treatment plants that comprise this 30 year contract. Finance was provided through a 27 year loan on a fixed interest basis with the principal amortising from 2003.

In Ireland, the Group is part of a contractual consortium that designed and built a waste water treatment plant for Cork City Council. Under the consortium agreement, the Group has responsibility for a 20 year contract for the operation and maintenance of the plant. In May 2011 the Group commenced a new 20 year operation and maintenance contract for the Fermoy and Mallow waste water treatment works, with Cork County Council.

AquaGib Limited, which is two thirds owned by the Group in a joint venture with the Government of Gibraltar, operates Gibraltar's dual drinking water and sea water distribution systems under its 30 year contract with the Government of Gibraltar.

Dividends

A final dividend of 9.57 pence per share for the year ended 31 March 2011 was paid on 9 September 2011, prior to the de-listing of the Group. Following the change of control, a special dividend of 44.73 pence per share was paid reflecting the Group's past outperformance. The directors recommend a final dividend of £nil.

The board of our main subsidiary, NWL, has proposed a dividend policy consistent with the underlying growth assumptions adopted by Ofwat at the price review in 2009. In addition, NWL paid a special dividend reflecting past outperformance.

Accounting policies

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union as it applies to the financial statements of the Group for the year ended 31 March 2012.

Capital structure and liquidity

In April 2011 the Group received the proceeds of a new £100.0 million US private placement with a ten year maturity at a coupon of 5.82%. The receipts, plus existing cash reserves, were used to refinance £125.0 million of intermediate holding company debt maturing in May 2011.

In June 2011 NWL agreed a new £150.0 million facility from the European Investment Bank (EIB) and the first £50.0 million tranche was drawn on a variable rate basis in November 2011. The remainder of the facility will be drawn in two further £50.0 million tranches in 2012 and 2013 at interest rates to be determined at the time of drawdown.

NWL, through its finance subsidiary, Northumbrian Water Finance plc (NWF), issued £360.0 million Guaranteed Eurobonds in January 2012, maturing January 2042, with an annual coupon of 5.125%.

The Group and NWL's regulated business debt structure remain largely unchanged with 75% (NWL: 70%) fixed at an average rate of 5.73% (NWL: 5.80%), 18% (NWL: 22%) index linked at an average real rate of 1.85% (all NWL) and 7% (NWL: 8%) on a variable rate basis. The blended average rate for the Group and NWL's regulated business for the year ended 31 March 2012 was 5.53% and 5.54% (2011: 5.80%, 5.93%), respectively, reflecting reduced RPI.

Cash interest cover has remained stable for the year as have the credit ratings for NWL at BBB+ stable (Fitch and Standard & Poors) and Baa1 stable (Moody's).

Total cash, cash equivalents and short term cash deposits available at 31 March 2012 amounted to £172.8 million. In addition to the undrawn element of the EIB facility, the Group has substantial undrawn committed five year bank facilities, amounting to £450.0 million at 31 March 2012, available to maintain general liquidity. These resources are sufficient to meet the requirements of the business through to July 2016.

Treasury policy

The main purposes of the Group's treasury function are to assess the Group's ongoing capital requirement, to maintain short term liquidity, ensuring access to medium term committed back up facilities, and to raise funding, taking advantage of any favourable market opportunities.

It also invests any surplus funds the Group may have, based on its forecast requirements and in accordance with the Group's treasury policy. On occasions, derivatives are used as part of this process, but the Group's policies prohibit their use for speculation. Full details are provided in note 20 to the financial statements. The Group is operating in compliance with its policies.

Pensions

The Group operates both a defined benefit pension scheme, which is closed to new entrants, and an occupational defined contribution arrangement.

The deficit (under International Accounting Standard (IAS) 19 Retirement Benefits) of the defined benefit scheme has increased from £46.0 million, at 31 March 2011, to £84.1 million at 31 March 2012. This is due to an increase in the liabilities of the scheme (£63.1 million), partially offset by an increase in the value of scheme assets (£25.0 million).

With the agreement of the Scheme Trustee, the Group has made capital contributions to the scheme totalling £70.0 million for the period to 31 March 2015. These payments comprise employers' contributions, the deficit recovery funding assumed in the final determination and employees contributions under a salary sacrifice arrangement.

The most recent actuarial valuation of the scheme was as at 31 December 2010. The results of the valuation are reported in note 25.

Operating performance

We use a range of KPIs to measure non-financial performance in the business and these indicators are reviewed by the management team each month. Performance for the year has been reported in the performance measures section on page 8 but is discussed in more detail in this section.

Customer

Putting customers first
Customer service is at the heart of the company and the culture of getting things ‘right first time every time’ is embedded in the business. We keep customers informed about our activities through leaflets with bills and our websites at www.nwl.co.uk and www.eswater.co.uk. The sites include information about our services and now allow customers to ask questions and investigate work being carried out in their area. We also communicate more broadly with local communities through public meetings and customer information events.

Customer satisfaction
Ofwat introduced the SIM in 2010/11, which monitors both quantitative and qualitative aspects of customer service. This mechanism financially incentivises the best performing companies and penalises the worst, endeavouring to simulate competition and encourage excellent service throughout the industry. Our aim is to be the leading company for SIM.

The quantitative aspect of SIM includes metrics for all lines busy and abandoned calls, unwanted calls, written complaints and CCWater investigations, each of which attract a number of penalty points depending upon the severity. Results across all metrics improved during the year and our quantitative SIM contact levels score reduced to 162 for 2011/12 from 212 for 2010/11.

The qualitative aspect of SIM takes the form of a survey, which is conducted each quarter across every water company and asks customers who have made contact with us about their experience. Our cumulative score for the four quarterly surveys was 4.33 out of 5, an improvement on the previous year’s score of 4.14.

Affordability
In the current economic climate, we know that affordability continues to be a genuine concern for many customers and we continue to be considerate of their circumstances, ensuring they can choose suitable payment options and that our recovery techniques are appropriate and effective. However, customers who deliberately avoid paying charges are pursued for payment. We are working closely with Ofwat and Defra to seek changes to legislation which will assist the industry to identify those responsible for charges more easily. We are also working with credit reference agencies to improve the quality of our customer information and enhance the effectiveness of our collection processes.

Water quality
The quality of water is critical to our customers and samples are taken on a daily basis for analysis under regulations monitored by the DWI. The quality in all areas served remained high and a sustained level of compliance has been achieved with fewer failures at customer taps and a reduction in the number of health-related failures at water treatment works and service reservoirs.

Significant improvements have been seen in iron and manganese compliance in 2011. In addition, there has been a further reduction in customer contacts relating to discoloured water. This has been helped by the cleaning of 150km of large diameter water mains in Tyneside and South East Northumberland, which was completed in June 2011. A similar three year programme of work was started in 2012, this time targeting larger mains in Gateshead and Newcastle as part of an ongoing strategy to improve the acceptability of water to consumers.

Business customers
The economic situation has had a significant impact on some business sectors in our operating regions and we have been working closely with major customers to mitigate the impact where possible. Due to the challenging economic conditions a number of large industrial customers temporarily ceased production for periods during the year whilst a number of other smaller commercial customers have ceased trading altogether. This has led to a downturn in water demand from industrial and commercial customers. However, this should be partially offset in 2012/13 largely due to SSI UK restarting steel production on Teesside.

We are active in the business communities where we are a member of the CBI, Chambers of Commerce and North East of England Process Industry Cluster. By supporting these and other smaller groups, NWL can help business growth and development in the areas we serve as well as retaining contact with organisations which represent customers. Business customer satisfaction is tracked on a regular basis and levels of satisfaction are high.

Competitiveness

We have instigated an efficiency programme focused on identifying and implementing sustainable operating cost efficiencies in order to achieve our medium term goal of being in the top efficiency band for both water and sewerage, as measured by Ofwat.

Efficiency programme
The efficiency programme identified around 100 projects and initiatives from across the whole business, ranging from large scale strategic reviews to smaller improvements at a local level. These efficiencies are in addition to the benefits already secured through buying our full energy requirements to March 2015 in advance. Delivery of the programme continues to be on schedule and, as a result, we are ahead of the final determination profile.

Other aspects of performance in relation to our competitiveness theme are included in the financial performance section on page 9.

Research and development
We invest in a programme of research and development to ensure we can meet the needs of our customers and to support the sustainable and cost effective operation of our business, now and into the future. Our research and innovation activities include the development of technical solutions for water and waste water management, collaborative research within the sector and partnerships with suppliers, universities and research organisations.

During the year, the Group invested £1.1 million (2011: £2.3 million) in research and development.

People

People strategy and policy
Our approach to strategy development focuses on achieving the medium term goals and specific business objectives in all parts of the Company. Our policies aim to nurture a mindset where our people will consistently choose to go the extra mile in delivering great service to customers every day. People are clear about our vision and values and the Code of Conduct sets out our approach to doing business. The CEO has responsibility at Board level for the People strategy and policy.

We aim to recruit and retain the best people, with a diverse range of skills, experience and backgrounds, who are committed to our vision and values. In return, we aim to provide opportunities for people to develop their skills and capabilities and fulfilling and challenging work in a supportive culture which recognises, celebrates and rewards the contribution made by both teams and individuals.

We understand that having a diverse workforce enhances our performance, fostering innovation and creativity and helping us better understand how to serve the needs of our customers. Our equal opportunity policy seeks to ensure that all our current employees and potential employees are treated with respect. We welcome job applications from all parts of the community. It is our intention that all job applicants and employees are treated equally, regardless of their age, ability, marital or partnership status, race, religion or belief, sex or sexual orientation. We monitor our workforce profile against census and sector data and aim to be recognised as an employer of choice within the diverse communities we serve, ensuring we take full advantage of the wide range of backgrounds and abilities of current and potential employees.

Engagement
Actively involving and engaging our people is a fundamental building block to delivering strong results and improving our performance. Every other year we seek their views through an annual employee engagement survey and this year's survey had the largest response rate ever with 78% of people taking part. In alternate years we participate in the Sunday Times Best Companies survey. One of the key measures in our survey is the Employee Satisfaction Index (ESI). Our target is to achieve and sustain an ESI of 81% and, although we missed the target in 2011/12, we did achieve our highest ever annual score of 78% and are confident that we will achieve this medium term goal by 2015.

Overall, 83% of respondents told us they are proud to work for the Company, 85% would recommend working for the Company and 80% believe that NWL is a great organisation to work for. This commitment is borne out by low employee turnover which, at 4.56% last year, was well below the UK average of 16%.

To recognise the contribution of our people, who bring our values to life every day in the way they do their jobs, we have launched our Vision and Values awards, known as the ViVa Awards. In the first year over 240 people and teams have been nominated by colleagues in the business to celebrate great ViVa performance against one or more of our five values.

Our constructive employee relations have been further enhanced through collaborative working, establishing a change management framework which was developed jointly with our trade union representatives, describing how we involve and engage people affected by change. This has enabled early involvement of trade union and employee representatives in shaping proposals and communication plans, even where formal collective consultation is not a requirement.

Supporting wellbeing
It is clear to us that when people are feeling at their best they will give of their best to customers and colleagues. In 2011, we signed up to the Public Health Responsibility Deal and have further developed our Wellbeing strategy to promote all aspects of working well.

We actively encourage our people to take care of their health and wellbeing by providing a wide range of health services, support and resources. The Group's medical advisor provides comprehensive occupational health services, general health promotion and stress management. Our people have access to specialist advice and treatment to support recovery from musculoskeletal disorders and, in 2010, we introduced NWL Support which gives our people access to face to face or telephone counselling on a range of personal concerns. We continue to promote healthy eating, hydration and exercise alongside excellent health screening and medical insurance schemes. Our current level of sickness absence is 3.0%, continuing on a downward trend from 3.2% in 2010 and 3.1% in 2011.

Where employees develop a disability which affects their work we support them to remain in employment, wherever practicable, by providing appropriate adjustments to their roles and/or effective redeployment. Occupational health physicians assist this process with professional medical advice.

Encouraging personal growth
Our aim is to build and maintain a culture which values, encourages and recognises outstanding performance, where we share a commitment to our objectives and to delivering our personal best. From corporate induction days and induction planning, to individual coaching, accreditation of skills through national vocational qualifications, and management and leadership programmes, we provide the resources needed to help employees reach their full potential.

Annual appraisals are given high priority, along with the identification of training needs, recognising how important technical and personal skills are in seeking to achieve the Company's vision and values.

Currently, 75% of our line managers are qualified to at least NQF Level 3. Overall, around 2,600 of our people, 90% of the workforce, are qualified to at least NQF Level 2, the equivalent of five GCSEs at grades A to C. Our commitment to skills is delivered through a series of NVQ programmes, working in partnership with leading providers.

Growing new talent is key to our continued success and, last year, four people were participating in our graduate development programme, with 18 in our apprentice programme, and plans are being formulated to increase our development programmes for 2012.

A fair deal
We aim for our terms and conditions to both attract and retain the best people in the areas we serve. In addition to competitive pay and benefits we also offer a scheme providing a wide range of lifestyle benefits through salary sacrifice, such as childcare vouchers, water services, cars for personal use and discounted store vouchers. Around 80% of our people chose to take advantage of the scheme during the year, up from 73% last year.

Communication
We use a wide range of communication methods including magazines, brochures, leaflets, newsletters, intranet, notice boards and regular team meetings. We issue all employees with a series of information booklets clearly explaining areas such as the Company's vision and values, terms, conditions and benefits of employment, and occupational health and wellbeing programmes.

We fully recognise the importance of an inclusive and engaging leadership and management style. In 2011 we engaged with our people through over 120 departmental workshops facilitated by senior managers and over 50 participative roadshows facilitated by the CEO and directors. Throughout the year we share key information through TeamTalk, the CEO's bi-monthly briefing which is cascaded through the business, with a wide range of newsletters and briefings also keeping people informed of more local news.

Disclosure (Whistleblowing)
We encourage open feedback and are committed to protecting employees who wish to voice concerns about behaviour or decisions that they believe to be illegal or unethical. The Audit

Committee regularly reviews the disclosure policy. There were no concerns raised by the Audit Committee during the year.

Health and safety
We place great emphasis on health and safety and a safe working environment. Employees are actively encouraged to be involved in identifying and eliminating hazards in the workplace. This has resulted in a significant reduction in accidents over recent years and, this year, there were only eight lost time reportable accidents, which continues the improving trend.

We have established a medium term plan for taking health and safety forward in the Company to 2015. We aim to further reduce the number of accidents by 10% each year and to maintain and improve the safety culture in the Company.

Safety information, communication and awareness are critical to creating a positive safety culture. In 2010 we reviewed the consultation process and, this year, introduced a new health and safety committee structure and a new health and safety forum chaired by the CEO. We are already seeing the benefits from involving the safety representatives in reviewing and consulting on safety policies and procedures and in championing the importance of health and safety in the workplace.

Employee Share Incentive Plan (SIP)
Prior to the change of control, we operated a Share Incentive Plan that provided one free matching share for every three shares purchased by an employee. This plan closed in October 2011 following the change of control of NWG.

Environment

Water resources
We continue to make excellent progress with the Abberton Scheme. This increases the capacity of Abberton reservoir by 58% and also includes the construction of two pipelines and a pumping station, all of which remain on programme. Once this scheme is operating, in 2014, we do not expect to have to develop further major resources in Essex for the next 25 years.

In addition to improving the supply of water, we believe it is important to manage the demand for water so that it does not exceed levels that can be supplied in a sustainable way. Metering has an important role to play in this regard. For several years we have been installing water meters upon change of occupier in properties in Essex. This is in addition to the optional metering scheme available to all customers.

Water efficiency targets were introduced in 2010/11 to reduce consumption of water by the Company's customers by one litre per property per day. These targets apply in all areas served and the award-winning work previously carried out in Essex and Suffolk was extended to the rest of the Company. We have consistently met our water efficiency targets year on year.

The reporting year was very dry in Essex and Suffolk, where only 83% of the long term average rainfall was recorded. However, through careful abstraction management, we were on track to fill our reservoirs to target levels by the end of April and avoided the need to impose a Temporary Use Ban (previously known as a hosepipe ban). In the north east, for the majority of the year, our storage position was at or above average. There are no plans for restrictions during 2012/13, although the Company will continue to encourage customers to use water wisely and control demand in dry periods.

By March 2011, we had recovered from the previous year's extremely severe winter which caused our northern operating area to miss its annual leakage target. Changes were made to leakage operations management and our response to any increase in leakage was quick and thorough to ensure that we achieved the 2011/12 leakage target regardless of the weather. Throughout 2011/12, distribution input and leakage levels have been at their lowest ever. Our final reported leakage figure has met our target comfortably.

Waste water

Our exceptional performance for sewage treatment works continued for a fourth year. All numerically consented works remained compliant for the year on the basis of routine ‘operator self monitoring’ samples. One works, Bowburn, was non-compliant based on an additional sample taken following the self reporting of a process issue to the EA.

The AAD plant at Bran Sands has performed well over the last 12 months. Further enhancements to the site are planned in 2012/13 to increase energy production further. Construction of a second AAD plant at Howdon, on Tyneside, to process the remainder of NWL’s sludge has gone well and started commissioning in June 2012.

The number of properties experiencing internal flooding due to hydraulic overloading reduced significantly for the second year in 2011/12. This can be attributed to a combination of less frequent and intense summer storms in 2011 and the cumulative effect of our sewer flooding investment programme. Enhanced resolution rain radar has now been in place in the north east since 2009, allowing us to identify severe weather across the region.

During 2011/12, we invested over £22.0m in conventional sewer flood relief projects, resulting in the removal of 224 properties from our flooding registers. Planning to identify schemes for coming years forms a key part of our investment programme and is well advanced, with a further 137 properties to be addressed in 2012/13. Additionally, in line with our serviceability action plan for sewer flooding, we have embarked on a programme of increased mitigation.

The number of properties flooded due to other causes has increased in 2011/12. A serviceability action plan has been put in place to reduce this number which includes new and additional programmes of sewer cleansing, sewer inspection, and sewer rehabilitation. These programmes form part of our long term policy to prevent unmanaged escapes from the sewer network.

The total number of pollution incidents showed a slight reduction from 2010, however, there was a significant increase in those classified as serious (categories 1 & 2). While there was no single cause for these serious events, the programme of installing overflow and sewer level monitoring (Hawkeye) is continuing. Furthermore, the monitoring has been brought in-house for quicker detection and a rapid response to warning level alarms, to solve problems before any overflow occurs.

All of the 34 bathing waters in the north east passed the required mandatory standard and 31 met the more demanding guideline standard.

Carbon management plan

The water industry is one of the largest users of energy in the UK and we aim to play a full part in support of the Government’s plans to reduce emissions. We have been working hard over recent years to reduce our carbon footprint while preparing ourselves for the future challenges of a change in climate and the weather events we may face as a consequence.

We have published our carbon management plan to meet the target of a 35% reduction in operational emissions by 2020, from a 2008 base.

The carbon management plan includes energy efficiency, renewable energy generation and water efficiency and supports our activities to help us adapt to a changing climate. It represents a sustainable and responsible way forward for the business, our customers and the environment. The projects which will help us to achieve our carbon reduction target include: our investment in AAD at Bran Sands and Howdon on Tyneside; hydroelectric installations at five reservoirs; improved metering of electricity to enable us to improve our energy efficiency through site energy management plans; limiting tertiary ultraviolet disinfection outside the bathing water season at five major works; and encouraging customers to avoid wastage through our 'using water wisely' campaign.

Through these projects, and by reviewing the efficiency of our pumps across the business, we have progressively reduced the amount of energy used over recent years despite upward pressures as a consequence of tighter environmental standards.

We have been awarded, for the second time, the Carbon Trust Standard for our efforts in reducing greenhouse gas emissions. The standard provides an objective benchmark against which our commitment and success in addressing our climate change impact was assessed and is significant as it demonstrates progress against our ambitious carbon management plan.

Changing weather patterns
The water cycle and the changing weather have a direct influence on the provision of water and waste water services. Our employees are experienced in managing the effects of too much or too little rainfall, but changing weather patterns will present a growing challenge for the business.

In past years, we have carried out research into the likely impact of climate change on all our assets and water resources and this has been incorporated in our climate change policy as part of our corporate responsibility work. This work is continuing, based on the latest UKCP09 projections published in 2009 by the UK Climate Impacts Programme.

Last year, we incorporated this work into our response to the new adaptation reporting power granted to the Government by the 2008 Climate Change Act, assessing the risk that climate change presents to our business. This work has highlighted that increasing rainfall intensity is the most significant short term threat that we will face as a result of the changing climate, which will increase the risk of sewer flooding. More positively, we have found that the anticipated drier summers of the future are less of a concern for NWL than for many other companies in our industry as a result of our investment to increase the capacity of Abberton reservoir for our Essex operating area and the presence of Kielder Water for the north east region.

Quality
We have maintained our certification to the international standards for quality (ISO 9001:2008), environment (ISO 14001:2004) and occupational health and safety (OHSAS 18001:2007) across all areas of the business, including operational sites and office based teams.

Communities

We support the communities we serve in a number of different ways and have been widely recognised as leaders in our support for projects that make the areas we serve better places in which to live, work or invest. This year, the Company has been re-accredited by FTSE4Good though, following our de-listing in the autumn, we will not be eligible for this index in future years. We have also received re-accreditation as a Platinum Plus company by Business in the Community and our Queen's Award for Industry is still in place as it was awarded in 2009 for a five year period. For the second year running, the company was also recognised by Ethisphere, an American-based international think-tank, as one of the most ethical companies in the world and was one of only seven UK only based companies and the only water utility worldwide to make the list of 145 companies.

This year, the Group made charitable donations totalling £155,000. In addition, and in line with previous years, we have contributed resources with a value equivalent to at least 1% of our annual pre-tax profits (through cash, employee time and expertise, or use of our facilities) to projects which benefit the communities we serve. Our employees raised £43,667 for charities this year. In addition, our 'Care for safety' scheme, which encourages employees to reduce accidents and associated lost time, triggered payments of over £28,190 for charities nominated by employees.

The support we give to our communities focuses on five broad areas.

Investment in our communities
Community Foundations covering our areas of supply hold endowment funds totalling nearly £1.0m contributed by NWL over the last 20 years. These are long term investments with the income from the funds used to support community and environmental initiatives. Community groups are chosen by committees of our own employees.

In addition to cash donations, we seek to support many projects through in-kind giving and support. Through 'Good Moves' we aim to put NWL estates into productive community use. Working in partnership with artists' groups CoExist and Metal, we have developed a temporary art project at our vacant Southend site to provide space for a temporary gallery, studio and small creative business complex. We have also focused on developing affordable rural housing to contribute to the sustainability and vitality of those communities, including support of the Prince of Wales' Affordable Rural Housing Initiative since it was launched in 2003.

This is the first full operating year for the newly formed Kielder Water & Forest Park (KW&FP) Development Trust, a registered charity which formalised the original Kielder Partnership founded in 1994. This year, activity has focused on refining the vision, mission and goals of the Trust as well as ensuring the appropriate governance and financial systems are in place, but this has not stopped the continued delivery of the 25 year investment plan for the area.

A £10.0m development scheme for the Calvert Trust Kielder site has gained planning permission which will increase the activity provision and accommodation within the Park. Encouraging and enabling sustainable development has been a high priority and the development of the local business forum has been a key facet. We helped the Kielder Observatory secure funding leading to a significant uplift in observing sessions and visitors. Events and activities have also grown with the successful delivery of the second Kielder marathon and the Kielder 100 mile mountain bike race using the new trails across Kielder Forest.

Participation in our communities
As part of NWL's in-kind giving, we encourage employees to volunteer their time, skills and expertise through our 'Just an hour' volunteering scheme. We support our people to participate in their local communities by giving them work time to volunteer in projects of their choice.

During the year, our people have helped hundreds of community projects and employees have volunteered 15,204 hours in their communities. In 2011/12, 48% of our employees participated in the 'Just an hour' volunteering scheme (up from 27% in the previous year) and 1,417 different organisations were given financial and in-kind support.

We have continued our support for Castle View Enterprise Academy, in Sunderland, for which NWL is lead sponsor. The school has now completed its second year of operations after opening its doors in 2009 and has seen considerable improvements in pass rates for students in GCSEs including English and Maths.

Educating our communities about their environment
Key partnerships have been developed by NWL to help the conservation of biodiversity on our sites, to facilitate public access and to develop conservation education. Our contribution includes funding project officers and providing expertise to the organisations. Our current partnerships include:

- Northumberland Wildlife Trust (Kielder and Bakethin);
- Durham Wildlife Trust;
- Essex Wildlife Trust (Hanningfield);
- Broads Authority (Lound and Trinity Broads); and
- Davy Down Trust (North Stifford, Essex).

A wide range of targeted educational materials is available on our websites for children and teachers. We promote the use of these materials and celebrate innovative approaches to environment and health education via our support of the Northumbrian Water Schools Awards in the north east and Cash for Schools Awards in Essex.

Supporting healthy communities
We continue to promote the health benefits of drinking tap water and our 'Water for health' campaign aims to encourage people to lead a healthy lifestyle. To date, almost £376,000 has been provided to fund free mains-fed water coolers in schools and around 800 have been supplied in nearly 465 schools and community groups. We also donated 143,200 bottles of tap water to community sporting events in order to promote the importance of rehydration during exercise. Working with a wide and diverse range of sporting partners is a natural extension of our 'Water for health' campaign and we work with them to support grassroots sporting activities to get people active as well as educating them on healthy eating and good hydration.

We have linked our 'Good moves' initiative and our 'Water for health' campaign to develop Healthworks. This is a unique project utilising one of our redundant buildings to help tackle the poor long term health of residents in Easington, County Durham, by granting a 99 year lease to County Durham Primary Care Trust and working in partnership to develop services for the local community in an area where census records show one of the worst health records in the country.

The centre received 27,500 visits during the year and now provides over 70 health and community support services including a GP led walk-in health centre open from 8am to 8pm 365 days a year. It acts as a community focal point where service providers and community groups can come together to address issues that affect the quality of life in their local community.

Supporting developing communities through WaterAid
We continue to raise funds and awareness for the work of WaterAid which brings sustainable water and sanitation solutions, as well as hygiene education, to the poorest parts of Africa and Asia, as it has since the charity was formed by the water industry in 1981.

The employee fundraising committee has raised more than £5.0m, since 1997, with the help of the Company and last year focused its fundraising support on specific projects in Ghana and Tanzania. We support our employees to become ambassadors for the charity and encourage annual supporter trips to see WaterAid projects.

Corporate governance

Since de-listing from the London Stock Exchange on 14 October 2011, the Company is no longer obliged to take account of The UK Corporate Governance Code (the Code). However, the Board maintains its belief that best practice in corporate governance helps it discharge its duties in the best interests of the Company. In accordance with the 'comply or explain' approach, the Board continues to comply with the main principles of the Code to the extent considered applicable. The areas where the Company departs from the main principles of the Code are explained below:

- the Company's immediate parent company, UKW, is a company indirectly wholly owned by a consortium comprising Cheung Kong Infrastructure Holdings Limited, Cheung Kong (Holdings) Limited and Li Ka Shing Foundation Limited (together the 'Ultimate Shareholders'). As a privately owned Company, the procedure for the appointment of new directors is less formal, rigorous and transparent than those considered appropriate for listed companies. In addition, the provisions concerning annual evaluation and re-election of directors are considered less relevant since the change in legal status; and

- dialogue with the Company's ultimate shareholders is maintained through member-nominated director representation on not only the Company's Board but that of several of its subsidiaries. Annual General Meetings are no longer required since becoming a privately owned company and the Company's amended Articles of Associations reflect this position.

The board of NWL also maintains high standards of corporate governance and endeavours to comply with the main principles of the Code, wherever practicable.

The group has a code of ethics, 'Our Code of Conduct', covering its relationships with customers, employees, suppliers, local communities, shareholders, other investors and regulators.

Board responsibilities and processes
The Board sets and implements the Company's vision, values and strategy and ensures compliance with group policies and legal and regulatory obligations.

The Company has adopted terms of reference which set out the matters reserved to the Board for approval and matters which are, or can be, delegated to the committees and management. The Company has also adopted financial approval rules which set out the authorisation processes and financial limits to be applied to financial transactions within the Company. NWL has adopted its own version of these guidelines. Standing or Executive Committees can take decisions not delegated to specific committees between Board meetings. All directors receive notice of Standing Committee meetings and may participate if they wish. Decisions taken by the Standing or Executive Committees are reported at the next Board meeting. The NWG Board meets at least every two months.

Authorisation of directors' conflicts of interest
Directors have a statutory duty, under s175 of the Companies Act 2006, to avoid a situation in which they have, or could have, a conflict of interest with the Company's interests. However, there is no breach of this duty if the Board has authorised the matter in question. The Articles permit directors (other than the director having the interest in question) to authorise any situation giving rise to a known or potential conflict. A register of the interests which have been authorised is maintained by the Company Secretary and is available at every Board meeting. The Company will follow emerging best practice in line with the General Counsel 100's guidance paper.

Board balance and independence
The Chairman and CEO have clearly defined roles and responsibilities. The Chairman leads the Board and creates the conditions for overall Board and individual director effectiveness, both inside

and outside the boardroom. The CEO is responsible for running the Company's business on a day to day basis.

The non-executive directors bring to the Board many years of business experience as well as financial expertise and the ability and willingness to constructively challenge and help develop proposals on strategy.

The General Counsel and Company Secretary, Martin Parker, assists the Board to ensure that good corporate governance compliance is achieved, to the extent considered applicable. He is also Company Secretary of NWL and is secretary to all Board committees.

Board committees
The Board has Audit and Remuneration Committees to assist it in the performance of its duties. The Board sets the terms of reference of the committees and receives regular reports from their chairmen at Board meetings.

Remuneration Committee
The work of the Remuneration Committee primarily comprises the adoption of principles and standards for executive remuneration and benefits.

Audit Committee
The purpose of the Audit Committee is to assist both executive and non-executive directors of NWG to discharge their individual and collective responsibilities in relation to:

- ensuring the financial and accounting systems of NWG and its subsidiaries are providing accurate and up to date information on their current position;
- ensuring NWG's published financial statements represent a true and fair reflection of this position; and
- assessing the scope and effectiveness of the Group's risk management systems and the integrity of its internal financial controls.

The Committee has now assumed responsibility for the practical work being done to ensure that the Group's procedures designed to prevent bribery are adequate (having regard to the provisions of the Bribery Act 2010 and the official guidance published in relation to that Act). This builds on significant work done by the NWG Board, with advice from the Company Secretary and Internal Audit Manager, to assess the bribery risk faced by the Group, clarify policies and map the procedures to be put in place.

The Audit Committee Chairman reports to the Board following each meeting of the Committee and Committee minutes are circulated to the Board.

Organisational structure
The trading subsidiaries have their own boards of directors (the subsidiary Boards) which are responsible for the operational and financial control of their own businesses. The subsidiary Boards report to the executive directors and to the Company's Board on matters including major strategic, financial, organisational, compliance and regulatory issues.

The Board is able to monitor the impact of environmental, social and governance matters on the Group's business, to assess the impact of significant risks on the business and to evaluate methods of managing these risks through reports it receives from the subsidiary Boards and the Audit Committee

Risks and uncertainties

The NWG Board requires all subsidiaries within the Group to identify and assess the impact of risks to their business using a standard risk model. For each risk identified, the model records the uncontrolled magnitude and likelihood of the risks occurring as well as the controls in place to mitigate those risks before assessing the controlled magnitude. The Board's view of acceptable risk is based on a balanced view of all of the risks in the operating environment. It aims to ensure an appropriate balance between risk aversion and opportunities.

The Board sets the tone for risk management within the Group and determines the appropriate risk appetite. The Board monitors the management of fundamental risks and approves major decisions affecting the Group's risk profile. Senior management implement policies on risk management and internal control.

For NWL, the management team reviews the approach to risk management in detail every year and the Audit Committee considers the outcome. The management team reviews the significant risks every month and a full review of the model for emerging significant risks is carried out quarterly. Any issues that arise from these management team reviews are reported by the CEO to the board.

Apart from NWL, none of the subsidiaries has risks considered to be significant to the Group's short and long term value.

The system of internal control incorporates risk management. It encompasses a number of elements that together facilitate an effective and efficient operation, enabling the company to respond to a variety of risks. These elements include:

- Policies and procedures
  Attached to fundamental risks are a series of policies that underpin the internal control process. Written procedures support the policies where appropriate.

- Business planning and budgeting
  The business planning and budgeting process is used to set objectives, agree action plans and allocate resources. Progress against meeting business plan and budget objectives is monitored regularly.

- Risk register
  The risk register identifies key risks, each with a risk owner who is responsible for evaluating the risk on a regular basis. As a way of ensuring that risk management is embedded into the business, the risk owners have the management of these risks as a personal KPI.

- Strategic risk model
  Risks that are known but not yet well defined enough for the likelihood and consequence to be reasonably foreseen are included in a strategic risk model.

- Audit Committee
  The Audit Committee reports to the Board on internal controls and alerts the Board to any emerging issues. In addition, the Audit Committee oversees internal audit, external audit and management, as required, in its review of internal controls.

An assurance map forms a permanent part of the process and, for each risk, highlights who provides assurance that the control activities are in place and operating effectively.

Risk description	Mitigation measures
Funding and liquidity risk	The financial ratios, financial results, liquidity position and credit ratings are described in the financial performance section on pages 9 to 12. In addition, note 20 to the financial statements, on pages 58 to 63, includes details on the Group's strategy and treasury operations for managing its capital; its exposures to liquidity risk, interest rate risk, foreign currency risk and counterparty risk; and details of its financial instruments. The Board reviews the treasury strategy periodically and approves specific proposals.
Unfavourable changes to the regulatory structure, as a result of the Water White Paper	We play a leading role in the policy debate, through Water UK, direct lobbying and forging positive relationships with relevant parties. We respond positively to consultation papers.
Unfavourable changes to the regulatory structure or price setting mechanism by Ofwat	We play a leading role in consultation groups with Ofwat and other stakeholders. We respond positively to consultation papers.
Impact of the transfer of private drains and sewers is greater than anticipated	An internal project team was established to understand and prepare the business for the transfer. We maintain sound financial documentation to support a possible future claim for tariff increases in order to recover additional costs borne. We maintain close liaison with the rest of the industry and have had constructive dialogue with Ofwat regarding the process.
Unexpected shift in climate change impact	We have processes in place to anticipate and plan for the impact of climate change. While these have long time horizons, they are reviewed regularly to ensure that any changes are identified early.
Loss of supply due to failure of strategic water main. This covers catastrophic failure that is greater than the response capability of the company	In most cases, duplicate mains and diversion of supplies would limit supply consequences. Comprehensive plans exist to provide a minimum emergency service to customers until repairs are completed, including mutual aid arrangements with other water companies. A proactive inspection regime is in place along with longer term reviews of network resilience.
Sewer flooding failures	A sewer flooding group, comprising stakeholders from various teams, is responsible for managing the process, flood reporting, network capacity studies and prioritisation of investment to reduce risk. Significant additional capital expenditure has been invested to address affected properties. The recently constructed rain radar station for the region is now operational and provides improved data. However, controls are not yet sophisticated enough to predict or prevent consequences of severe rainfall.
Pesticides lead to prescribed concentration or value failure and possible enforcement action	Undertakings have been agreed with the DWI to carry out certain actions to mitigate pesticide issues (metaldehyde and clopyralid). While specific treatment processes, such as carbon filters, are undertaken at treatment works, proactive catchment management is also being carried out. This involves working with farmers, regulators and other stakeholders to advise on improved storage and application techniques for such pesticides. This is a more sustainable solution than the alternative of constructing major new treatment processes.
Loss of income through closure of large customers or lower industrial volumes	It is not possible to directly influence industrial volumes, however, our account managers liaise closely with significant customers to provide support where possible.
Incident at Bran Sands waste water treatment works causes business interruption	We have a number of contracts to treat industrial waste streams at our Bran Sands works. The liability under each contract is capped except, in certain cases, where NWL is in wilful breach. A site-specific management regime is in place incorporating additional monitoring and a greater amount of standby assets.
Risk of increasing pension contributions resulting from increasing longevity and the impact	The defined benefit scheme was closed to new entrants, benefits restructured and employee contributions increased in 2008. Advance contributions have been made to the scheme, including deficit funding

of economic conditions on investment returns	allowed in the last price review. The scheme Trustee determines investment policy and monitors performance of investment managers. Triennial actuarial valuations of the scheme are carried out, with the latest being as at 31 December 2010.
Health and safety prosecution	Our health and safety policy and safety management system define clear arrangements and responsibilities for implementation and management throughout the Group. This is audited as part of our quality and environmental management system. Visible high level support for health and safety is provided by the Board and management team. Long term plans and targets are set to promote continuous improvement.

Statutory disclosures

Political

During the year, the Group has worked with politicians of all major parties, officials and opinion formers. This work has included making representations on issues which NWL feels are important to our customers and communities such as competition, the review of regulators, the Water White Paper, adoption of private sewers, 'Water for health', climate change, the Water Framework Directive and other legislative issues which could affect our customers.

We do not support any political party and we do not, directly or through any subsidiary, make what are commonly regarded as donations to any political party or other political organisation. However, the wide definition of donations in the Political Parties, Elections and Referendums Act 2000 covers activities which form part of the necessary relationship between the Group and political parties and political organisations. These activities include attending party conferences, as these provide the best opportunity to meet a range of stakeholders, both national and local, to explain our activities, as well as local meetings with MPs, MEPs and their agents. The costs associated with these activities during 2011/12 were as follows:

Name of political party	£
Conservative	7,500
Labour	13,062
Liberal Democrats	3,720
Total	**24,282**

Creditors

The Company's policy is to agree payment terms with suppliers and to pay on time according to those agreed terms. The Company's policy is to make payment not more than 30 days after receipt of a valid invoice, except as otherwise agreed. The ratio, expressed in days, between the amount invoiced by its suppliers during the year and the amount owed to its trade creditors at 31 March 2012, was 19 days (2011: 30 days).

Directors' remuneration and interests

Information about directors' remuneration is contained in note 5 to the financial statements.

Indemnification of directors

UKW has in place directors' and officers' insurance. On 28 November 2005, the Company entered into a deed of indemnity to grant the directors further protection against liability to third parties, subject to the conditions set out in the Companies Act. Such qualifying third party indemnity provision remains in force as at the date of approving the directors' report.

Auditors
Deloitte LLP was appointed as auditor in the current year following the resignation of Ernst & Young LLP. Deloitte LLP has indicated its willingness to continue in office for the ensuing year.

Directors' declaration
As required under s418 of the Companies Act 2006, so far as each current director is aware, there is no relevant audit information of which the Company's auditors are unaware and each director has taken all the steps that he or she ought to have taken as a director in order to make himself or herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Going concern
The Group has sufficient funding and facilities in place to meet its requirements for the foreseeable future. The directors believe that the Group is well placed to manage its business risks successfully and, accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

By order of the Board

Martin Parker
General Counsel and Company Secretary
4 October 2012

Northumbrian Water Group Limited
Registered office: Northumbria House, Abbey Road, Pity Me, Durham, DH1 5FJ
Registered in England and Wales No. 4760441

Appendix to the directors' report

Definition of KPIs

Balanced scorecard KPIs

Measure	Definition of measure
Customer	
Customer satisfaction – SIM quantitative score	SIM quantitative measure, based on customer contacts. Contacts are normalised per thousand connected properties and multiplied by a weighting factor for each 'unwanted' category. Categories include unwanted customer calls, abandoned calls, first stage written complaints, second stage written complaints and CCWater investigations. The lower the score the higher the customer satisfaction.
Customer satisfaction – SIM qualitative score	SIM qualitative measure, assessing satisfaction of consumers across their experience from first correspondence to final resolution, through independent surveys. Surveys are carried out four times a year for water, waste water and billing contacts and the average score taken. A score of 5 indicates maximum satisfaction.
Unplanned interruptions >6 hours	A weighted scoring of the number of properties affected by interruptions to supply of more than six hours duration which are unplanned or unwarned (excluding overruns of planned and warned interruptions) except for those caused directly by third parties. It includes interruptions for which customers are notified less than 48 hours in advance. The scoring weights interruptions which exceed 12 hours, and heavily weights those which exceed 24 hours.
Coliform incidents	Total number of coliform failures in regulatory samples at water treatment works and service reservoirs. One coliform or more is a failing sample.
Competition	
Profit before tax	Actual profit before tax compared to the budget approved by the Board, adjusted for the impact of variances related to indexation on index linked bonds, which depends on the July RPI. Profit before tax has been chosen because it is a primary financial measure for the Group for which the executive directors are accountable.
Capital efficiency	An assessment of the efficiency of the NWL capital investment programme undertaken annually by the Board.
Earnings before interest and tax	Actual earnings before interest and tax (EBIT), in the UKW consolidated accounts, compared to the budget approved by the Board. EBIT has been chosen because it is a primary financial measure for which the executive directors are accountable.
Cash available for distribution	Cash available for distributions in the period at UKW, compared to the budget approved by the Board.
People	
Engagement and satisfaction index (%)	The Engagement and Satisfaction Index is calculated from scores for 13 items selected from the annual employee survey. These items align to the Sunday Times Best Companies survey and give a measure of employee satisfaction.
Employee engagement score	The employee engagement score is derived from the Sunday Times Best Companies survey and gives a measure of employee satisfaction.

Lost time reportable accidents (no.)	Accidents reportable to the Health and Safety Executive resulting in more than three days lost from work.
Environment	
Leakage (Mld)	Water network leakage for the financial year, as reported to Ofwat.
Sewage treatment works compliance (%)	Percentage of population equivalent served by sewage treatment works compliant with Environment Agency (EA) look-up table consents.
Pollution incidents (categories 1 & 2)	Number of category 1 and 2 pollution incidents in the calendar year, as defined by the EA. Category 1 is a major water pollution incident and category 2 is a significant water pollution incident.
Communities	
FTSE4Good accreditation	Accreditation by FTSE4Good index series, which has been designed to objectively measure the performance of companies that meet globally recognised corporate responsibility standards.
BITC Platinum Plus accreditation	Accreditation by BITC at Platinum Plus level, the highest level in their corporate responsibility index. BITC is a national business-led charity which advises, challenges and supports its members to create a sustainable future for people and the planet and to improve business performance.
Just an Hour participation	The percentage of NWL employees actively volunteering in their communities.

Financial KPIs

Measure	Definition of measure
Gearing to RCV	The ratio of net debt, excluding fair value adjustments, to NWL's RCV. The RCV represents the total capital value of the appointed water and sewerage business on which Ofwat allows a rate of return at price reviews. The RCV generates most of the revenue stream of the Group and gearing is an important factor in credit ratings. The RCV is calculated by Ofwat and published each year. Net debt is calculated from the balance sheet in the audited financial statements, adjusted for the fair value of loans owed by subsidiaries acquired in 2003.
Cash interest cover	The ratio of cash generated from operations less tax divided by net interest paid. This measures the ability of the Company to service its debt. Cash interest cover is calculated from the audited financial statements.
Cash flow to net debt	The ratio of cash generated from operations less tax paid divided by net debt. This indicates the Company's ability to reduce debt in the absence of need for additional investment, without resorting to asset disposal. Cash flow to net debt is calculated from the audited financial statements.

Statement of directors' responsibilities in relation to the Group financial statements

The directors are responsible for preparing the annual report and the Group financial statements in accordance with applicable United Kingdom law and those International Financial Reporting Standards (IFRSs) as adopted by the European Union.

The directors are required to prepare Group financial statements for each financial year. Under Company Law, the directors must not approve the financial statements unless they are satisfied that they present fairly the financial position of the Group and the financial performance and cash flows of the Group for that period. In preparing those Group financial statements the directors are required to:

- select suitable accounting policies in accordance with IAS 8: Accounting Policies, Changes in Accounting Estimates and Errors and then apply them consistently;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's financial position and financial performance;
- state that the Group has complied with IFRSs, subject to any material departures disclosed and explained in the financial statements; and
- make judgements and estimates that are reasonable and prudent.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy at any time the financial position of the Group and enable them to ensure that the Group financial statements comply with the Companies Act 2006 and Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Group and, hence, for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Responsibility statements

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with IFRSs as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Company and the undertakings included in the consolidation taken as a whole; and
- the directors' report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

By order of the Board

Heidi Mottram
Chief Executive Officer

Independent auditor's report to the members of Northumbrian Water Group Limited

We have audited the financial statements of Northumbrian Water Group Limited for the year ended 31 March 2012 which comprise the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity, consolidated balance sheet, consolidated cash flow and related notes 1 to 29, and the parent Company balance sheet and related notes 1 to 10. The financial reporting framework that has been applied in the preparation of the group financial statements is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. 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 auditor's 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 auditor

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

Scope of the audit of the financial statements

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

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 March 2012 and of the group's profit for the year then ended;
- the group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Separate opinion in relation to IFRSs as issued by the IASB
As explained in Note 1 to the group financial statements, the group in addition to applying IFRSs as adopted by the European Union, has also applied IFRSs as issued by the International Accounting Standards Board (IASB).

In our opinion the group financial statements comply with IFRSs as issued by the IASB.

Opinion on other matter prescribed by the Companies Act 2006
In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception
We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

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

Paul Feechan (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditor
Newcastle upon Tyne
5 October 2012

Consolidated income statement

For the year ended 31 March 2012

	Notes	Year to 31.3.2012 £m	Year to 31.3.2011 £m
Continuing operations			
Revenue	2	**789.5**	738.1
Operating costs	3	**(458.5)**	(433.9)
Profit on ordinary activities before interest	2	**331.0**	304.2
Finance costs payable	7	**(189.2)**	(178.8)
Finance income receivable	7	**51.3**	54.9
Share of profit after tax of jointly controlled entities		**0.8**	0.7
Profit on ordinary activities before taxation	2	**193.9**	181.0
– current taxation	8	**(30.8)**	(33.1)
– deferred taxation	8	**23.3**	30.5
Profit for the year		**186.4**	178.4
Attributable to:			
Equity shareholders of the parent Company		**185.9**	178.3
Non-controlling interests		**0.5**	0.1
		186.4	178.4

Consolidated statement of comprehensive income

For the year ended 31 March 2012

	Notes	Year to 31.3.2012 £m	Year to 31.3.2011 restated £m
Profit for the year		**186.4**	178.4
Other comprehensive income			
Actuarial (losses)/gains	25	**(83.5)**	74.0
Losses on cash flow hedges taken to equity		**(22.5)**	(4.0)
Translation differences		**-**	0.2
Tax on items charged or credited to equity		**18.8**	(22.2)
Total other comprehensive (loss)/gain		**(87.2)**	48.0
Total comprehensive income for the year		**99.2**	226.4
Attributable to:			
Equity shareholders of the parent Company		**98.7**	226.3
Non-controlling interests		**0.5**	0.1
		99.2	226.4

Consolidated statement of changes in equity

For the year ended 31 March 2012

	Equity share capital £m	Share premium reserve £m	Cash flow hedge reserve £m	Treasury shares £m	Currency translation £m	Retained earnings £m	Total equity £m	Non-controlling interests £m	Total £m
At 1 April 2010 restated	51.9	446.5	(38.7)	(2.0)	0.7	(177.8)	280.6	2.8	283.4
Profit for the year	-	-	-	-	-	178.3	178.3	0.1	178.4
Other comprehensive income	-	-	(4.1)	-	0.2	51.9	48.0	-	48.0
Total comprehensive income and expense for the year	-	-	(4.1)	-	0.2	230.2	226.3	0.1	226.4
Share-based payment	-	-	-	-	-	0.1	0.1	-	0.1
Exercise of LTIP awards	-	-	-	0.3	-	(0.3)	-	-	-
Deferred tax related to share-based payment	-	-	-	-	-	0.1	0.1	-	0.1
Acquisition of non-controlling interest in subsidiaries	-	-	-	-	-	0.6	0.6	(0.6)	-
Equity dividends paid	-	-	-	-	-	(70.3)	(70.3)	-	(70.3)
At 1 April 2011 restated	51.9	446.5	(42.8)	(1.7)	0.9	(17.4)	437.4	2.3	439.7
Profit for the year	-	-	-	-	-	185.9	185.9	0.5	186.4
Other comprehensive income	-	-	(22.4)	-	-	(64.8)	(87.2)	-	(87.2)
Total comprehensive income and expense for the year	-	-	(22.4)	-	-	121.1	98.7	0.5	99.2
Share-based payment	-	-	-	-	-	1.1	1.1	-	1.1
Exercise of LTIP awards	-	-	-	1.7	-	(1.7)	-	-	-
Equity dividends paid	-	-	-	-	-	(281.6)	(281.6)	(0.3)	(281.9)
At 31 March 2012	**51.9**	**446.5**	**(65.2)**	**-**	**0.9**	**(178.5)**	**255.6**	**2.5**	**258.1**

Consolidated balance sheet

As at 31 March 2012

	Notes	**Year to 31.3.2012 £m**	Year to 31.3.2011 restated[1] £m	Year to 31.3.2010 restated[1] £m
Non-current assets				
Goodwill	10	**3.6**	3.6	3.6
Other intangible assets	10	**64.2**	64.2	64.2
Property, plant and equipment	11	**3,822.9**	3,626.8	3,518.9
Investments in jointly controlled entities	12	**4.3**	4.0	4.1
Financial assets		**11.5**	12.0	12.9
Amounts receivable relating to consortium relief		**1.7**	1.7	1.7
		3,908.2	3,712.3	3,605.4
Current assets				
Inventories	13	**3.2**	3.3	3.3
Trade and other receivables	14	**167.3**	153.9	136.4
Short term cash deposits	15	**4.3**	1.4	15.8
Cash and cash equivalents	15	**168.5**	141.7	174.8
		343.3	300.3	330.3
Total assets		**4,251.5**	4,012.6	3,935.7
Non-current liabilities				
Interest bearing loans and borrowings	17	**2,746.9**	2,295.8	2,433.9
Provisions	19	**2.2**	2.4	2.2
Deferred income tax liabilities	8	**543.9**	586.0	594.3
Hedging instruments	20	**59.1**	53.7	48.4
Pension liability	25	**84.1**	46.0	133.1
Other payables		**5.1**	6.8	7.8
Grants and deferred income		**281.9**	255.1	233.5
		3,723.2	3,245.8	3,453.2
Current liabilities				
Interest bearing loans and borrowings	17	**89.4**	163.7	33.1
Provisions	19	**0.2**	0.2	0.2
Trade and other payables	16	**175.9**	155.6	151.2
Hedging instruments	20	**4.7**	5.0	6.4
Income tax payable		**-**	2.6	8.2
		270.2	327.1	199.1
Total liabilities		**3,993.4**	3,572.9	3,652.3
Net assets		**258.1**	439.7	283.4
Capital and reserves				
Issued capital	21	**51.9**	51.9	51.9
Share premium reserve		**446.5**	446.5	446.5
Cash flow hedge reserve		**(65.2)**	(42.8)	(38.7)
Treasury shares		**-**	(1.7)	(2.0)
Currency translation		**0.9**	0.9	0.7
Retained earnings		**(178.5)**	(17.4)	(177.8)
Equity shareholders' funds		**255.6**	437.4	280.6
Non-controlling interests		**2.5**	2.3	2.8
Total capital and reserves		**258.1**	439.7	283.4

1. The prior year balance sheets have been restated to reflect the recognition of an inflation hedge (see note 22).

Approved by the Board on 4 October 2012 and signed on its behalf by:

Heidi Mottram
Chief Executive Officer

Consolidated cash flow statement
For the year ended 31 March 2012

	Notes	**Year to 31.3.2012 £m**	Year to 31.3.2011 £m
Operating activities			
Reconciliation of profit before interest to net cash flows from operating activities			
Profit on ordinary activities before interest		**331.0**	304.2
Depreciation		**113.8**	111.6
Other non-cash charges and credits		**(5.6)**	(8.9)
Net credit for provisions, less payments		**(0.2)**	0.2
Difference between pension contributions paid and amounts recognised in the income statement		**9.7**	11.5
Decrease in inventories		**0.1**	-
Increase in trade and other receivables		**(11.5)**	(14.7)
Increase in trade and other payables		**5.8**	5.2
Cash generated from operations		**443.1**	409.1
Advanced contributions in respect of retirement benefits		**(47.1)**	(22.4)
Interest paid		**(123.2)**	(116.1)
Income taxes paid		**(37.2)**	(38.7)
Net cash flows from operating activities		**235.6**	231.9
Investing activities			
Interest received		**2.1**	4.7
Capital grants received		**9.9**	13.2
Proceeds on disposal of property, plant and equipment		**1.0**	1.3
Dividends received from jointly controlled entities		**0.5**	0.8
Short term cash deposits		**(2.9)**	14.4
Maturity of investments		**0.9**	1.1
Purchase of property, plant and equipment		**(273.3)**	(202.9)
Net cash flows from investing activities		**(261.8)**	(167.4)
Financing activities			
New borrowings		**510.2**	-
Settled hedge instrument		**(17.5)**	-
Dividends paid to minority interests		**(0.3)**	-
Dividends paid to equity shareholders		**(281.6)**	(70.3)
Repayment of borrowings		**(150.6)**	(19.5)
Payment of principal under hire purchase contracts and finance leases		**(7.2)**	(7.3)
Acquisition of externally held loan stock issued by a subsidiary		**-**	(0.4)
Net cash flows from financing activities		**53.0**	(97.5)
Increase/(decrease) in cash and cash equivalents		**26.8**	(33.0)
Cash and cash equivalents at start of year	15	**140.3**	173.3
Cash and cash equivalents at end of year	15	**167.1**	140.3
Cash and cash equivalents at end of year	15	**167.1**	140.3
Short term cash deposits	15	**4.3**	1.4
Total cash, cash equivalents and short term cash deposits		**171.4**	141.7

Notes to the consolidated financial statements

1. Accounting policies
(a) Statement of compliance
The consolidated financial statements have been prepared in accordance with IFRS as adopted by the European Union as it applies to the financial statements of the Group for the year ended 31 March 2012 and in accordance with the Companies Act 2006.

The financial statements have been prepared on a going concern basis which assumes that the Group will have adequate funding to meet its liabilities as they fall due in the foreseeable future. As at 31 March 2012 the Group had net current assets of £73.1 million (2011 restated: net current liabilities of £26.8 million). The directors have reviewed cash flow requirements, including reasonably possible changes in trading performance, and are confident that they will be able to meet these from funds available and existing financing facilities. Accordingly, the directors believe it is appropriate to prepare the financial statements on a going concern basis.

The Group is party to an inflation hedge which commenced in May 2004 as part of the issue of the Eurobonds due in January 2034. The Group has not previously accounted for the fair value of this hedge instrument. However, the directors have determined that the fair value should be recognised in the consolidated balance sheet in accordance with IAS 39 Financial Instruments: Recognition and Measurement. The impact of this change is explained in note 22.

The directors consider the following accounting policies to be relevant in relation to the Group's financial statements. The financial statements of the Group for the year ended 31 March 2012 were authorised for issue by the Board of directors on 4 October 2012 and the balance sheet was signed on the Board's behalf by Heidi Mottram (Chief Executive Officer).

The Group has adopted the following standards and interpretations during the year:
- IAS 24 (revised), 'Related party disclosures'
- Amendment to IFRS 1, 'First time adoption'
- IFRIC 19, 'Extinguishing financial liabilities with equity investments'
- Amendment to IFRIC 14, 'Prepayments of a minimum funding requirement'
- Annual improvements to IFRSs 2010

The adoption of the standards and interpretations listed above does not have a material impact on the Group.

Northumbrian Water Group Limited is a limited company incorporated and domiciled in England and Wales.

The Group financial statements are presented in sterling and all values are rounded to the nearest one hundred thousand pounds (£0.1 million) except where otherwise indicated.

(b) Basis of consolidation
The consolidated financial statements include the Company and its subsidiary undertakings. The results of subsidiaries acquired during the period are included from the date of their acquisition. The results of subsidiaries disposed of during the period are included to the date of their disposal. Inter-segment sales and profits are eliminated fully on consolidation. Where, for commercial reasons, the accounting reference date of a subsidiary is a date other than that of the Company, management accounts made up to the Company's accounting reference date have been used. In accordance with SIC 12 'Consolidation – Special Purpose Entities', the financial statements of two companies are consolidated as special purpose entities, with effect from 12 May 2004, the date of the transaction which utilised these entities.

Where necessary, adjustments are made to bring the accounting policies used under relevant local GAAP in the individual financial statements of the Company, subsidiaries and jointly controlled entities into line with those used by the Group under IFRS.

Non-controlling interests represent the portion of profit or loss and net assets in subsidiaries that is not held by the Group and is presented within equity in the consolidated balance sheet, separately from parent shareholders' equity.

(c) Associates and jointly controlled entities
Investments in associates and jointly controlled entities in the Group financial statements are accounted for using the equity method of accounting where the Group exercises significant influence over the associate. Significant influence is generally presumed to exist where the Group's effective ownership is 20% or more. The Group's share of the post tax profits less losses of associates and jointly controlled entities is included in the consolidated income statement and the carrying value in the balance sheet comprises the Group's share of their net assets/liabilities less distributions received and any impairment losses. Goodwill arising on the acquisition of associates and jointly controlled entities, representing the excess of the cost of investment compared to the Group's share of net fair value of the associate's identifiable assets, liabilities and contingent liabilities, is included in the carrying amount of the associate and is not amortised. Financial

statements of jointly controlled entities and associates are prepared for the same reporting period as the Group. Where necessary, adjustments are made to bring the accounting policies used into line with those of the Group to take into account fair values assigned at the date of acquisition and to reflect impairment losses where appropriate. Adjustments are also made to the Group's financial statements to eliminate the Group's share of unrealised gains and losses on transactions between the Group and its jointly controlled entities and associates.

(d) Goodwill
Goodwill arising on the acquisition of subsidiary undertakings and businesses represents the excess of the fair value of the consideration given over the fair value of the identifiable assets and liabilities acquired. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Prior to 1 April 2004, goodwill was amortised over its estimated useful life; such amortisation ceased on 31 March 2004. Goodwill relating to acquisitions since 1 April 2004 is not amortised. Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. For the purposes of impairment testing, goodwill is allocated to the related cash-generating units monitored by management. Where the recoverable amount of the cash-generating unit is less than its carrying amount, including goodwill, an impairment loss is recognised in the income statement. The carrying amount of goodwill allocated to a cash-generating unit is taken into account when determining the gain or loss on disposal of the unit, or of an operation within it.

(e) Intangible assets other than goodwill
Other intangible fixed assets represent the right to receive income under the operating agreement with the Environment Agency in respect of the Kielder Water transfer scheme. The value of this intangible asset has been assessed with reference to the net monies raised in accordance with the Kielder securitisation on 12 May 2004. The term of the operating agreement is in perpetuity and, accordingly, no amortisation is provided. The value of this intangible is assessed for impairment on an annual basis in accordance with IAS 36 'Impairment of Assets'.

Expenditure on internally developed intangible assets, excluding development costs, is taken to the income statement in the year in which it is incurred. Intangible assets acquired separately from a business are carried initially at cost. An intangible asset acquired as part of a business combination is recognised outside goodwill if the asset is separable or arises from contractual or other legal rights and its fair value can be measured reliably. Development expenditure is recognised as an intangible asset only after its technical feasibility and commercial viability can be demonstrated, the availability of adequate technical and financial resources and an intention to complete the project have been confirmed and the correlation between development costs and future revenues has been established.

(f) Property, plant and equipment
Property, plant and equipment and depreciation
Property, plant and equipment, including assets in the course of construction, comprise infrastructure assets (being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls) and other assets (including properties, overground plant and equipment).

Property, plant and equipment are included at cost less accumulated depreciation and any provision for impairment. Cost comprises the aggregate amount paid and the fair value of any other consideration given to acquire the asset and includes costs directly attributable to making the asset capable of operating as intended.

Freehold land is not depreciated. Other assets are depreciated evenly over their estimated economic lives, which are principally as follows: freehold buildings, 30-60 years; operational structures, plant and machinery, 4-92 years; infrastructure assets 13-200 years (see below); and fixtures, fittings, tools and equipment, 4-10 years.

The carrying values of property, plant and equipment are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable and are written down immediately to their recoverable amount. Useful lives and residual values are reviewed annually and, where adjustments are required, these are made prospectively.

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

Infrastructure assets
In the regulated water services business, infrastructure assets comprise a network of systems being mains and sewers, reservoirs, dams and sea outfalls.

Infrastructure assets were measured at a date prior to transition to IFRS (23 May 2003) at their fair value, which was adopted as deemed historical cost on transition to IFRS. The assets and liabilities were measured at fair value as a result of the acquisition on 23 May 2003.

Expenditure on infrastructure assets which enhances the asset base is treated as fixed asset additions while maintenance expenditure which does not enhance the asset base is charged as an operating cost.

Infrastructure assets are depreciated evenly to their estimated residual values over their estimated economic lives, which are principally as follows:

Dams and impounding reservoirs	150 years
Water mains	100 years
Sea outfalls	60 years
Sewers	200 years
Dedicated pipelines	4-20 years

(g) Financial assets
Financial assets comprise loans to third parties recoverable in more than one year and include cash held on long term deposit as a guaranteed investment contract relating to the Kielder securitisation. These assets are recognised at cost and are measured annually based on the ability of the borrower to repay. Any impairment is taken to the income statement in the period in which it arises. Loans and receivables are measured at amortised cost using the effective interest rate method. The Group assesses at each balance sheet date whether a financial asset or group of financial assets is impaired.

(h) Foreign currencies and foreign currency transactions
Transactions in foreign currencies are initially recorded in the functional currency by applying the spot exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are re-translated at the functional currency rate of exchange ruling at the balance sheet date. The functional and presentational currency of Northumbrian Water Group Limited is United Kingdom sterling (£). Assets and liabilities of subsidiaries and jointly controlled entities in foreign currencies are translated into sterling at rates of exchange ruling at the end of the financial period and the results of foreign subsidiaries are translated at the average rate of exchange for the period. Differences on exchange arising from the re-translation of the opening net investment in subsidiary companies and jointly controlled entities, and from the translation of the results of those companies at average rate, are taken to equity. All other foreign exchange differences are taken to the income statement in the period in which they arise.

Unrealised gains and losses arising from changes in foreign currency exchange rates are not cash flows. However, the effect of exchange rate changes on cash and cash equivalents held or due in a foreign currency is reported in the cash flow statement in order to reconcile cash and cash equivalents at the beginning and the end of the period. This amount is presented separately from cash flows from operating, investing and financing activities, where material, and includes the differences, if any, had those cash flows been reported at end of period exchange rates.

(i) Inventories
Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and, where applicable, direct labour costs, as well as an element of overheads that have been incurred in bringing the inventories to their present locations and condition.

(j) Revenues
Provision of services
Revenue, which excludes value added tax, represents the fair value of the income receivable in the ordinary course of business for services provided. Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured.

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

(k) Dividends
Dividends payable and receivable are recognised when the shareholders' right to receive the revenue is established.

(l) Grants and contributions
Grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. Revenue grants are credited to the income statement in the period to which they relate. Capital grants and contributions relating to property, plant and equipment are treated as deferred income and amortised to the income statement over the expected useful economic lives of the related assets. Deferred income relating to assets adopted from customers, recognised in accordance with IFRIC 18, is amortised to the income statement over the expected useful economic lives of the related assets.

(m) Leases
Where assets are financed by leasing arrangements which transfer substantially all the risks and rewards of ownership to the Group, the assets are treated as if they had been purchased at their fair value or, if lower, at the present value of the minimum lease payments. Rentals or leasing payments are treated as consisting of a capital element and finance charges, the capital element reducing the outstanding liability and the finance charges being charged to the income statement over the period of the leasing contract at a constant rate on the reducing outstanding liability.

Rentals under operating leases (where the lessor retains a significant proportion of the risks and rewards of ownership) are expensed in the income statement on a straight line basis over the lease term.

(n) Pensions and other post-employment benefits
Defined benefit scheme
The cost of providing benefits under the defined benefit scheme is determined using the projected unit credit method, which attributes entitlement to benefits to the current period (to determine current service cost) and to the current and prior periods (to determine the present value of defined benefit obligation) and is based on actuarial advice. Past service costs are recognised in the income statement on a straight line basis over the vesting period or immediately if the benefits have vested. When a settlement (eliminating all obligations for benefits already accrued) or a curtailment (reducing future obligations as a result of a material reduction in the scheme membership or a reduction in future entitlement) occurs, the obligation and related plan assets are re-measured using current actuarial assumptions and the resultant gain or loss recognised in the income statement during the period in which the settlement or curtailment occurs.

The interest element of the defined benefit cost represents the change in present value of scheme obligations resulting from the passage of time, and is determined by applying the discount rate to the opening present value of the benefit obligation, taking into account material changes in the obligation during the year. The expected return on plan assets is based on an assessment made at the beginning of the year of long term market returns on scheme assets, adjusted for the effect on the fair value of plan assets of contributions received and benefits paid during the year.

The service cost is disclosed in employment costs and the expected interest income and interest cost on obligations are disclosed within finance costs payable/(income receivable).

Actuarial gains and losses on experience adjustments and changes in actuarial assumptions are recognised in full in the period in which they occur in the consolidated statement of comprehensive income.

Defined contribution scheme
The Group also operates a defined contribution scheme. Obligations for contributions to the scheme are recognised as an expense in the income statement in the period in which they arise.

(o) Share-based payments
The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted and is recognised as an expense over the vesting period, which ends on the date on which the relevant employees become fully entitled to the award. Fair value is determined by an external valuer using the Monte-Carlo simulation model. In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the Company (market conditions) or those not related to performance or service (non-vesting conditions).

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market or non-vesting condition, which are treated as vesting irrespective of whether or not the market or non-vesting condition is satisfied, provided that all other performance conditions are satisfied.

At each balance sheet date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired, management's best estimate of the achievement or otherwise of vesting conditions and the number of equity instruments that will ultimately vest or, in the case of an instrument subject to a market or non-vesting condition, be treated as vesting as described above. This includes any award where non-vesting conditions within the control of the Group or the employee are not met. The movement in cumulative expense since the previous balance sheet date is recognised in the income statement, with a corresponding entry in equity.

Where the terms of an equity-settled award are modified or a new award is designated as replacing a cancelled or settled award, the cost based on the original award terms continues to be recognised over the original vesting period. In addition, an expense is recognised over the remainder of the new vesting period for the incremental fair value of any modification, based on the difference between the fair value of the original award and the fair value of the modified award, both as measured on the date of the modification. No reduction is recognised if this difference is negative.

(p) Taxes
Current tax
Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from, or paid to, the taxation authorities. The tax rates and tax laws used to compute the amounts are those that are enacted or substantively enacted by the balance sheet date.

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

Deferred tax liabilities are recognised for all taxable temporary differences except:
- where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in jointly controlled entities, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised except:
- where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in jointly controlled entities, deferred tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

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

Deferred tax is recognised in the income statement unless it relates to items accounted for outside profit or loss, in which case it is recognised in correlation with the underlying transaction either in other comprehensive income or directly in equity.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Value added tax
Revenues, expenses and assets are recognised net of the amount of value added tax except:
- where the value added tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case the value added tax is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables. The net amount of value added tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the balance sheet.

(q) Derivative financial instruments
The Group utilises interest rate swaps, forward rate agreements and forward exchange contracts as derivative financial instruments.

A derivative instrument is considered to be used for hedging purposes when it alters the risk profile of an underlying exposure of the Group in line with the Group's risk management policies. Interest rate swap agreements are used to manage interest rate exposures. Derivative financial instruments are stated at their fair value.

Under IAS 39, derivative financial instruments are always measured at fair value, with hedge accounting employed in respect of those derivatives fulfilling the stringent requirements for hedge accounting as prescribed under IAS 39. In summary, these criteria relate to initial designation and documentation of the hedge relationship, prospective testing of the relationship to demonstrate the expectation that the hedge will be highly effective throughout its life and subsequent retrospective testing of the hedge to verify effectiveness.

The fair value of forward exchange contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles. The fair value of interest rate swaps is determined by reference to market values for similar instruments.

Hedging transactions undertaken by the Company are classified as either fair value hedges when they hedge the exposure to changes in the fair value of a recognised asset or liability; or cash flow hedges where they hedge exposure to variability in currency cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a forecast transaction.

In relation to fair value hedges, which meet the conditions for hedge accounting, any gain or loss from re-measuring the hedging instrument at fair value is recognised immediately in profit or loss. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the income statement. Where the adjustment is to the carrying amount of a hedged interest bearing financial instrument, the adjustment is amortised to the net profit and loss such that it is fully amortised by maturity.

In relation to cash flow hedges to hedge firm currency commitments which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in equity and the ineffective portion is recognised in the income statement.

When the hedged firm commitment results in the recognition of a non-financial asset or a non-financial liability then, at the time the asset or liability is recognised, the associated gains or losses that had previously been recognised in equity are included in the initial measurement of the acquisition cost or other carrying amount of the asset or liability. For all other cash flow hedges, the gains or losses that are recognised in equity are transferred to the income statement in the same periods in which the hedged firm commitment affects the net profit and loss.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the income statement.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that point in time, any cumulative gain or loss on the hedging instrument recognised in equity is kept in equity until the forecast transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the income statement.

(r) Interest bearing loans and borrowings

All loans and borrowings are initially stated at the amount of the net proceeds, being fair value of the consideration received net of issue costs associated with the borrowing. Finance costs (including issue costs) are taken to the income statement over the term of the debt at a constant rate on the balance sheet carrying amount. The carrying amount is increased by the finance charges amortised and reduced by payments made in respect of the accounting period. The carrying amount of index linked borrowings increases annually in line with the July RPI, with the accretion being charged to the income statement as finance costs payable. Other borrowing costs are recognised as an expense when incurred.

Loans and borrowings acquired at acquisition are restated to fair value. The adjustment arising on acquisition is amortised to the income statement on the basis of the maturity profile of each instrument. Realised gains and losses that occur from the early termination of loans and borrowings are taken to the income statement in that period.

Net debt is the sum of all current and non-current liabilities less cash and cash equivalents, short term cash deposits, financial investments and loans receivable.

(s) Borrowing costs

Borrowing costs are generally expensed as incurred. Borrowing costs that are directly attributable to the acquisition or construction of an asset that necessarily takes a substantial time to prepare for its intended use are capitalised while the asset is being constructed as part of the cost of that asset.

Capitalisation ceases when the asset is substantially ready for its intended use or sale. If active development is interrupted for an extended period, capitalisation is suspended. When construction occurs piecemeal, and use of each part ceases upon substantial completion of that part, a weighted average cost of borrowings is used.

The Group capitalises borrowing costs for all eligible assets when construction commenced on or after 1 April 2009 and continues to expense borrowing costs relating to construction projects that commenced prior to that date.

(t) Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, do not qualify as trading assets and have not been designated as either fair value through profit and loss or available for sale. Gains and losses are recognised in income when the investments are de-recognised or impaired, as well as through the amortisation process.

(u) Cash and cash equivalents and short term cash deposits
Cash and cash equivalents disclosed in the balance sheet comprise cash at bank and in hand and short term deposits with a maturity on acquisition of three months or less, which are held for the purpose of meeting short term cash commitments rather than for investment or other purposes. Cash equivalents are readily convertible to a known amount of cash and subject to an insignificant risk of changes in value.

Short term cash deposits disclosed in the balance sheet comprise cash deposited with a maturity of greater than three months on acquisition, a fixed interest rate and which do not constitute cash equivalents under IAS 7 'Statement of Cash Flows'.

For the purpose of the consolidated cash flow statement, cash and cash equivalents are as defined above, net of outstanding bank overdrafts.

(v) Trade and other receivables
Trade receivables are recognised and carried at original invoice amount less an allowance for any uncollectable amounts. Invoices for unmeasured water and waste water charges are due on fixed dates; other receivables generally have 30 day payment terms. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified. Trade and other receivables do not carry any interest.

(w) Investments
Investments are initially recorded at the fair value of the consideration given including the acquisition charges associated with the investment. Subsequent to initial recognition, they are valued at original cost less any impairment.

(x) Provisions
Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources will be required and a reliable estimate can be made of the amount of the obligation.

(y) Impairment of assets
The Group assesses at each reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses on continuing operations are recognised in the income statement in those expense categories consistent with the function of the impaired asset.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the income statement unless the asset is carried at revalued amount, in which case the reversal is treated as a revaluation increase. After such a reversal the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

(z) De-recognition of financial assets and liabilities
A financial asset or liability is generally de-recognised when the contract that gives rise to it is settled, sold, cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a de-recognition of the original liability and the recognition of a new liability, such that the difference in the respective carrying amounts together with any costs or fees incurred are recognised in the income statement.

(aa) Accounting standards
The International Accounting Standards Board and International Financial Reporting Interpretation Committee (IFRIC) have issued the following standards and interpretations with an effective date after the date of these financial statements:

International Accounting Standards (IAS/IFRS)	Effective for accounting periods beginning on or after:
IFRS 1: Amendment to IFRS 1 - First time adoption	1.7.2011; 1.1.2013
IFRS 7: Amendment to IFRS 7 - Financial instruments: Disclosures	1.7.2011; 1.1.2013
IFRS 9: Financial instruments: classification and measurement	1.1.2015
IFRS10: Consolidated financial statements	1.1.2013
IFRS11: Joint arrangements	1.1.2013
IFRS12: Disclosures of interests in other entities	1.1.2013
IFRS13: Fair value measurement	1.1.2013
IAS 1: Amendment to IAS 1 - Financial statement presentation	1.7.2012
IAS 12: Amendment to IAS 12 - Income taxes	1.1.2012
IAS 19: Amendment to IAS 19 - Employee benefits	1.7.2012
IAS 27 (revised 2011): Separate financial statements	1.1.2013
IAS 28 (revised 2011): Associates and joint ventures	1.1.2013
IAS 32: Amendment to IAS 32 - Financial instruments: Presentation	1.1.2013

IFRIC	Effective for accounting periods beginning on or after:
IFRIC 20: Stripping costs in the production phase of a surface mine	1.1.2013

(ab) Key assumptions
The directors consider that the key assumptions applied at the balance sheet date, which may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are:

- those assumptions used in arriving at the pension asset/liability under IAS 19. These key assumptions and their possible impact are disclosed in note 25, ‘Pensions and other post-retirement benefits’;
- the bad debt provision which is calculated by applying a range of percentages to debt of different ages. These percentages also vary between different categories of debt. Higher percentages are applied to those categories of debt which are considered to be of greater risk and also to debt of greater age. The value of the bad debt provision is sensitive to the specific percentages applied; and
- the asset lives assigned to property, plant and equipment, details of which can be found in note 1(f).

2. Segmental analysis
For management purposes, the Group is organised into business units according to the nature of its products and services and has three reportable operating segments. The trading of the business is principally carried out within the UK. Profit is measured at profit on ordinary activities before interest.

Northumbrian Water Limited
NWL is one of the ten regulated water and sewerage businesses in England and Wales. NWL operates in the north east of England, where it trades as Northumbrian Water, and in the south east of England, where it trades as Essex & Suffolk Water. NWL also has non-regulated activities closely related to its principal regulated activity.

Water and waste water contracts
NWG owns a number of special purpose companies for specific water and waste water contracts in Scotland, Ireland and Gibraltar.

Other
Agrer provides overseas aid funded project work in developing countries through a number of funding agencies. Central unallocated costs and provisions are also included in this segment.

Transfer prices between business segments are set on an arm’s length basis in a manner similar to transactions with third parties. Segment revenue, segment expense and segment result include transfers between business segments. Those transfers are eliminated on consolidation.

Revenue

	Northumbrian Water Limited £m	Water and waste water contracts £m	Other £m	Total £m
Year ended 31 March 2012				
Segment revenue	**737.4**	**42.1**	**16.1**	**795.6**
Inter-segment revenue	**-**	**-**	**(6.1)**	**(6.1)**
Revenue from external customers	**737.4**	**42.1**	**10.0**	**789.5**
Year ended 31 March 2011				
Segment revenue	689.4	40.0	14.1	743.5
Inter-segment revenue	-	-	(5.4)	(5.4)
Revenue from external customers	689.4	40.0	8.7	738.1

Profit on ordinary activities before interest

	Northumbrian Water Limited £m	Water and waste water contracts £m	Other £m	Total £m
Year ended 31 March 2012				
Segment profit on ordinary activities before interest	**338.8**	**10.0**	**(17.8)**	**331.0**
Net finance costs				**(137.9)**
Share of profit from jointly controlled entities				**0.8**
Profit on ordinary activities before taxation				**193.9**
Taxation				**(7.5)**
Profit for the year from continuing operations				**186.4**
Year ended 31 March 2011				
Segment profit on ordinary activities before interest	297.6	9.5	(2.9)	304.2
Net finance costs				(123.9)
Share of profit from jointly controlled entities				0.7
Profit on ordinary activities before taxation				181.0
Taxation				(2.6)
Profit for the year from continuing operations				178.4

Assets and liabilities

	Northumbrian Water Limited		Water and waste water contracts		Other		Total	
	31.3.2012	31.3.2011	**31.3.2012**	31.3.2011	**31.3.2012**	31.3.2011	**31.3.2012**	31.3.2011
	£m	£m	**£m**	£m	**£m**	£m	**£m**	£m
Segment assets	**3,929.5**	3,709.6	**109.9**	123.6	**212.1**	179.4	**4,251.5**	4,012.6
Segment liabilities	**495.3**	422.3	**15.9**	18.0	**3,427.8**	3,096.4	**3,939.0**	3,536.7

Other comprises taxation, interest and net debt.

	Northumbrian Water Limited		Water and waste water contracts		Total	
	31.3.2012	31.3.2011	**31.3.2012**	31.3.2011	**31.3.2012**	31.3.2011
	£m	£m	**£m**	£m	**£m**	£m
Property, plant and equipment additions	**308.2**	219.6	**2.0**	0.3	**310.2**	219.9
Depreciation	**107.1**	105.8	**6.7**	5.8	**113.8**	111.6

Geographical information

Revenue from external customers from the UK was £762.9 million (2011: £714.8 million). Revenue from other countries was £26.6 million (2011: £23.3 million).

Non-current assets for operations in the UK were £3,896.5 million (2011: £3,700.7 million). Non-current assets for operations in other countries were £11.7 million (2011: £11.6 million).

3. Operating costs

	Year to 31.3.2012 £m	Year to 31.3.2011 £m
Materials and consumables	**24.8**	25.6
Manpower costs (see note 6)	**115.6**	110.6
Own work capitalised	**(28.3)**	(28.7)
Depreciation of property, plant and equipment	**113.8**	111.6
Profit on disposal of property, plant and equipment	**(0.7)**	(0.9)
Amortisation of capital grants	**(4.8)**	(4.6)
Costs of research and development	**1.1**	2.3
Operating lease payments	**1.1**	1.2
Bad debt charge	**6.4**	17.8
Other operating costs	**229.5**	199.0
Operating costs	**458.5**	433.9

4. Auditor's remuneration

	Year to 31.3.2012 £m	Year to 31.3.2011 £m
Audit of the financial statements[1]	**0.2**	0.3
Other fees to auditors:		
Other services	**0.2**	0.1

Note:
1. £8,000 of this relates to the Company (2011: £97,000).

5. Directors' Emoluments

(a) Directors' remuneration

The remuneration of the directors of the Company was as follows:

	Year to 31.3.2012 £000	Year to 31.3.2011 £000
Emoluments (including benefits in kind)	**1,470**	1,292

One of the directors at 31 March 2012 was a member of a defined benefit pension scheme where the Company makes contributions towards the cost (2011: 1).

One of the directors at 31 March 2012 was a member of a defined contribution scheme where the Company makes contributions towards the cost (2011: 1).

Long Term Incentive Plan (LTIP)
Prior to the change of control and de-listing, the company operated a share based Long Term Incentive Plan. Awards under the LTIP had three year pre-vesting performance conditions. Before the change of control, the Remuneration Committee determined the extent to which the performance conditions had been met and the proportion of the performance period that had elapsed in deciding upon how many shares of the remaining three awards would vest. These shares were transferred to individuals, at market value, on 11 October 2011. The Company was de-listed on 14 October 2011.

The directors who held office as at 31 March 2012 held the following conditional interests in the ordinary 10p shares of the company, awarded in accordance with the terms of its LTIP:

	Award date		Awards held at the start of the year	Awarded during the year	Awards lapsed during the year	Awards vested during the year	**Awards held as at 31.3.2012**
Heidi Mottram	8.12.2010	3	96,212	-	11,844	84,368	**-**
Totals			96,212	-	11,844	84,368	**-**
Chris Green	15.12.2008	1	78,650	-	39,325	39,325	**-**
	4.1.2010	2	83,240	-	18,904	64,336	**-**
	8.12.2010	3	68,551	-	8,439	60,112	**-**
Totals			230,441	-	66,668	163,773	**-**

Notes:

1. The market value of the shares on the date of the award was 251.50 pence per share. Due to the change of control, the performance period ran from 1 October 2008 to 23 September 2011.
2. The market value of the shares on the date of the award was 272.50 pence per share. Due to the change of control, the performance period ran from 1 October 2009 to 23 September 2011.
3. The market value of the shares on the date of the award was 328.70 pence per share. Due to the change of control, the performance period ran from 1 October 2010 to 23 September 2011.
4. The cost of conditional awards is charged to the profit and loss account over the performance period to which they relate after taking account of the probability of performance criteria being met. In the year, £1.1 million was charged to the income statement (2011: £0.1 million).
5. The market price of the shares on 11 October 2011 was 464.40 pence per share.
6. Aggregate gross gains made by directors on exercise of awards at date of vesting was £1,152,367 (2011: £99,915).
7. Details of the performance conditions are shown below.

Details of awards and performance conditions are shown below:

LTIP award made 15 December 2008

Maximum award	100% of salary permitted and actual grants to executive directors related to shares worth 100% of salary.
Performance conditions	(1) 50% of award depends on NWL's return on capital employed (ROCE) relative to that of the other water and sewerage companies of England and Wales. (2) 50% of award depends on the Company's TSR performance against the FTSE 250 Index, excluding investment trusts.
Vesting schedules	(1) 30% vests at median performance. At upper quartile or above, all of this element of the award will vest. Between median and upper quartile, straight line pro-rating will apply. Where the return on capital employed performance is below the median, none of this element of the award will vest. (2) 30% vests at median performance with straight line pro-rating of TSR performance against the members of the FTSE 250 Index, excluding investment trusts, to 100% for upper quartile performance. Where the Company's TSR performance is below the median, none of this element of the award will vest.

LTIP awards made 4 January 2010 and 8 December 2010

Maximum award	100% of salary permitted and actual grants to executive directors related to shares worth 100% of salary.
Performance conditions	(1) 50% of award depends on the Company's relative TSR against the FTSE 250 excluding investment trusts and companies in the following sectors: banks, financial services, life insurance, non-life insurance, real estate investment and services and real estate investment trusts, oil and gas producers and oil equipment and services. In addition, awards will only vest if the Committee is satisfied that the Company's TSR performance is consistent with the underlying business performance of the Company. (2) 20% of award depends on NWL's average ROCE over the three financial years starting from 1 April immediately preceding grant date.

LTIP awards made 4 January 2010 and 8 December 2010 (continued)	
Performance conditions (continued)	(3) 20% of the award depends on performance against Ofwat serviceability targets for the four asset classes (i.e. water non-infrastructure, water infrastructure, sewerage non-infrastructure and sewerage infrastructure) in the final year of the relevant three year performance period. Serviceability is measured by Ofwat based on a number of indicators which include asset performance indicators, water quality compliance, environmental compliance and consumer service. (4) 10% of award depends on the results of NWL's independently run customer satisfaction index, measured as the average score for the surveys carried out during the relevant three year performance period.
Vesting schedules	(1) 30% vests for median performance increasing on a straight line so that 100% vests for upper quartile performance. (2) 30% vests for average three year ROCE of 6.3%, increasing on a straight line so that 50% will vest for average three year ROCE of 6.45% and 100% will vest for an average ROCE of 6.75%. (3) 50% vest for 'stable' assessments in three out of the four asset classes. 100% of this will vest for 'stable' assessments in all four asset classes. No awards would vest under this part of an award for less than three 'stable' assessments. (4) 30% will vest for a customer satisfaction index of 83%, increasing on a straight line so that 100% will vest for a customer satisfaction index of 93% or above.

New LTIP

After the change of control, a new cash-based LTIP was introduced with effect from 1 January 2012. The new LTIP targets relate to financial performance, SIM (customer services performance) and serviceability (asset performance). Payments which are approved by the Remuneration Committee will be paid three years after the start of the performance period.

Share Incentive Plan (SIP)

Prior to the change of control and de-listing, the company operated a SIP that provided one free matching share for every three shares purchased by an employee. The SIP closed in October 2011 following the change of control of NWG and the participants received cash consideration for both purchased and matching shares.

The directors who held office as at 31 March 2012 had the following interests in the ordinary 10 pence shares of the Company, purchased and held in accordance with the terms of the SIP:

	Number of SIP shares held at the start of the year [1]	**Number of SIP shares held as at 31.3.2012[1]**
Heidi Mottram	606	**-**
Chris Green	6,372	**-**

Notes:

1. These figures include the shares paid for by the participant and the free shares granted by the Company.

(b) Highest paid director

The amounts for remuneration shown in note 5(a) include the following in respect of the highest paid director:

	Year to 31.3.12 £000	Year to 31.3.11 £000
Emoluments (including benefits in kind)	**595**	526

In 2011/12, the highest paid director was a member of the defined contribution scheme. During the year the company made payments to that scheme of £64,099 (2011: £43,600).

6. Employee information

The total employment costs of all employees (including directors) of the Group were:

	Year to 31.3.2012 £m	Year to 31.3.2011 £m
Wages and salaries	**93.0**	87.6
Social security costs	**7.9**	7.3
Defined benefit pension service cost (see note 25)	**12.8**	13.9
Other pension costs	**1.9**	1.8
Total employment costs	**115.6**	110.6
Total employment costs were charged as follows:		
Capital schemes and infrastructure renewals	**28.3**	25.4
Manpower costs	**87.3**	85.2
	115.6	110.6

Included in wages and salaries is a total expense of share-based payments of £0.4 million (2011: £0.4 million) which arises from transactions accounted for as equity-settled share-based payments.

The average monthly number of employees of the Group during the year was:

	Year to 31.3.2012 Number	Year to 31.3.2011 Number
Northumbrian Water Limited	**2,894**	2,875
Water and waste water contracts	**156**	132
Other	**26**	24
	3,076	3,031

7. Finance costs payable/(income receivable)

	Year to 31.3.2012 £m	Year to 31.3.2011 £m
Finance costs payable on debentures, bank and other loans and overdrafts	**124.9**	112.9
Amortisation of discount, fees, loan issue costs and other financing items	**(2.8)**	(2.5)
Capitalisation of interest	**(3.2)**	(1.9)
Accretion on index linked bonds	**23.8**	21.9
Interest cost on pension plan obligations	**41.3**	43.3
Finance costs payable on hire purchase contracts and finance leases	**5.2**	5.1
Total finance costs payable	**189.2**	178.8
Expected return on pension plan assets	**(49.3)**	(45.5)
Finance income receivable	**(2.0)**	(1.9)
Acquisition of CES loan stock	**-**	(4.6)
Finance lease termination discount	**-**	(2.9)
Net finance costs payable	**137.9**	123.9

During the prior year, the Group acquired the subordinated loan stock issued by CES from an external party. This was acquired at below book value leading to a gain of £4.6 million. In addition, the Group transferred a finance lease to a new counterparty with a termination discount valued at £2.9 million.

8. Taxation

(a) Tax on profit on ordinary activities

	Year to 31.3.2012 £m	Year to 31.3.2011 £m
Current tax:		
Current income tax charge at 26% (2011: 28%)	**31.2**	42.3
Income tax recycled from equity on cash flow hedges	**-**	0.1
Adjustment in respect of prior periods	**(0.6)**	(9.5)
UK corporation tax	**30.6**	32.9
Overseas tax	**0.2**	0.2
Total current tax	**30.8**	33.1
Deferred tax:		
Origination and reversal of temporary differences in the year at 24% (2011: 26%)	**19.5**	9.0
Effect of changes in tax rates and laws:		
– Impact of reduction in rate of UK corporation tax	**(47.5)**	(46.3)
Adjustment in respect of prior periods	**4.7**	6.8
Total deferred tax (credit)/charge	**(23.3)**	(30.5)
Tax charge in the income statement	**7.5**	2.6

The rate of UK corporation tax was reduced from 26% to 25% by the Finance Act 2011 with effect from 1 April 2012. The rate was further reduced to 24%, with effect from the same date, on the passing of a resolution under the Provisional Collection of Taxes Act 1968 on 26 March 2012 at which point the new rate was substantively enacted. As a result, deferred tax was re-measured at the rate at which timing differences are expected to reverse. Adjustments in respect of prior periods arise from revisions to UK tax returns.

(b) Tax relating to items charged or credited outside of profit or loss

	Year to 31.3.2012 £m	Year to 31.3.2011 restated £m
Current tax:		
Current tax recycled to income statement on cash flow hedges	**-**	(0.1)
Deferred tax:		
Actuarial gains and losses on pension schemes	**(20.0)**	19.4
Hedging instruments	**(1.3)**	(1.0)
Impact of reduction in rate of UK corporation tax	**2.4**	3.9
Tax charge in the statement of comprehensive income	**(18.9)**	22.2
Deferred tax:		
Share-based payment	**0.1**	(0.1)
Tax credit in the statement of changes in equity	**0.1**	(0.1)

(c) Reconciliation of the total tax charge

	Year to 31.3.2012 £m	Year to 31.3.2011 £m
Accounting profit before tax	**193.9**	181.0
Accounting profit multiplied by standard rate of corporation tax (26%; 2011: 28%)	**50.4**	50.7
Effects of:		
Expenses not deductible for tax purposes	**2.6**	2.1
Depreciation in respect of non-qualifying items	**1.8**	1.1
Non-taxable income and enhanced tax reliefs	**(1.0)**	-
Non-taxable amortisation of financing items	**(1.3)**	(1.4)
Adjustment to tax charge in respect of prior periods	**4.1**	(2.7)
Other	**-**	(0.2)
	56.6	49.6
Effect of changes in tax rates and laws:		
– Impact of rate reduction on opening deferred tax	**(47.5)**	(46.3)
– Impact of rate reduction on movement in deferred tax	**(1.6)**	(0.7)
Total tax expense reported in the income statement	**7.5**	2.6

The effective tax rate for the year to 31 March 2012 was 3.9% (2011: 1.4%). The increase of 2.5% is mainly due to prior year items. In the absence of the rate change and prior year items, the effective rate would have been 26%.

(d) Deferred tax

The movements in deferred tax liabilities/(assets) are as follows:

	Accelerated tax depreciation £m	Deferred income £m	Tax losses £m	Retirement benefit obligations £m	Fair value hedging instruments £m	Business combinations £m	Other £m	Total £m
At 1 April 2010 restated	686.9	(60.2)	(5.7)	(38.1)	(15.3)	10.9	15.8	594.3
Charge/(credit) in the income statement	(43.5)	13.8	0.2	(0.4)	-	(1.0)	0.4	(30.5)
Charge/(credit) in other comprehensive income	-	-	-	22.1	0.1	-	0.1	22.3
Reported in equity on cash flow hedges	-	-	-	-	-	-	(0.1)	(0.1)
At 1 April 2011 restated	643.4	(46.4)	(5.5)	(16.4)	(15.2)	9.9	16.2	586.0
Charge/(credit) in the income statement	(42.4)	3.2	3.6	12.1	-	(0.9)	1.1	(23.3)
Charge in other comprehensive income	-	-	-	(18.8)	(0.1)	-	-	(18.9)
Reported in equity on share-based payment	-	-	-	-	-	-	0.1	0.1
At 31 March 2012	**601.0**	**(43.2)**	**(1.9)**	**(23.1)**	**(15.3)**	**9.0**	**17.4**	**543.9**

The Group has tax losses of £5.3 million (2011: £7.0 million) which have arisen in its Gibraltar subsidiary for which a deferred tax asset has not been recognised as they may not be used to offset taxable profits elsewhere in the Group and it is not expected that the subsidiary will utilise significant amounts in the foreseeable future. The losses are, however, available for offset against future taxable profits arising in the subsidiary without time limit.

The rate of UK corporation tax was reduced to 23% with effect from 1 April 2013 by Finance Act 2012. Had that rate applied in 2011/12 the closing deferred tax liability would have been reduced by £22.7 million to £521.2 million.

(e) Factors that may affect future tax charges

The Government has stated its intention to reduce the UK rate of corporation tax to 22% by 1 April 2014. Had that rate applied in 2011/12 the closing deferred tax liability would have been reduced by £45.3 million to £498.6 million and the current year's corporation tax charge would have been reduced by £4.8 million to £26.4 million.

The Group expects to continue to incur high levels of capital expenditure during NWL's 2010-15 regulatory period and be able to claim tax reliefs in excess of depreciation. However, capital allowances will be claimed at a slower rate in future following the reduction in rates from 20% to 18% (general plant pool) and from 10% to 8% (special rate pool) with effect from 1 April 2012.

9. Dividends paid and proposed

	Year to 31.3.2012 £m	Year to 31.3.2011 £m
Declared and paid during the year:		
Equity dividends on ordinary shares:		
Final dividend for 2010/11: 9.57 pence (2009/10: 8.85 pence)	**49.6**	45.8
Interim dividend for 2011/12: nil (2010/11: 4.72 pence)	**-**	24.5
Special dividend for 2011/12: 44.73 pence (2010/11: nil)	**232.0**	-
Dividends paid	**281.6**	70.3
Proposed for approval by shareholders at the AGM:		
Final dividend for 2011/12: nil (2010/11: 9.57 pence)	**-**	49.6

10. Intangible assets

	Goodwill £m	Other £m	Total £m
Cost:			
At 1 April 2010, 1 April 2011 and 31 March 2012	**3.8**	**64.2**	**68.0**
Impairment:			
At 1 April 2010, 1 April 2011 and 31 March 2012	**(0.2)**	**-**	**(0.2)**
Net book value at 31 March 2012	**3.6**	**64.2**	**67.8**
Net book value at 1 April 2010 and 31 March 2011	3.6	64.2	67.8

As from 1 April 2004, the date of transition to IFRS, goodwill is no longer amortised but is now subject to an annual impairment review.

Goodwill has been allocated to the water and waste water cash-generating unit and the other intangible asset has been allocated to the Northumbrian Water Limited cash-generating unit, which are also the operating segments.

The other intangible asset represents the right in perpetuity to receive income under the operating agreement with the Environment Agency in respect of the Kielder Water transfer scheme and, therefore, the directors consider the asset has an indefinite life. Accordingly, future cash flows, which increase in line with inflation, have been discounted at a rate of 5.36% in perpetuity. This represents a long term nominal gilt yield and an assumed credit spread. This calculation satisfied the Group that the carrying value at 31 March 2012 had not been impaired. Furthermore, it is improbable that the discount rate would increase to such a level that the carrying value would be impaired.

11. Property, plant and equipment

	Freehold land and buildings £m	Infrastructure assets £m	Operational structures, plant and machinery £m	Fixtures, fittings, tools and equipment £m	Assets in the course of construction £m	Total £m
Cost:						
At 1 April 2010	115.6	1,811.7	2,254.3	208.1	111.4	4,501.1
Additions	-	14.5	1.2	0.4	203.8	219.9
Schemes commissioned	3.7	76.3	73.7	13.1	(166.8)	-
Reclassifications	2.8	-	(2.5)	(0.3)	-	-
Disposals	(0.5)	(6.8)	(2.4)	-	-	(9.7)
At 1 April 2011	121.6	1,895.7	2,324.3	221.3	148.4	4,711.3
Additions	0.1	13.2	3.5	0.6	292.8	310.2
Schemes commissioned	0.5	119.8	92.9	11.6	(224.8)	-
Reclassifications	-	(0.1)	0.1	-	-	-
Disposals	-	(7.5)	(2.4)	-	-	(9.9)
At 31 March 2012	**122.2**	**2,021.1**	**2,418.4**	**233.5**	**216.4**	**5,011.6**
Depreciation:						
At 1 April 2010	36.0	99.9	709.4	136.9	-	982.2
Charge for the year	2.2	25.2	72.8	11.4	-	111.6
Reclassifications	-	-	(0.3)	0.3	-	-
Disposals	-	(6.8)	(2.5)	-	-	(9.3)
At 1 April 2011	38.2	118.3	779.4	148.6	-	1,084.5
Charge for the year	2.3	24.3	75.8	11.4	-	113.8
Disposals	-	(7.5)	(2.1)	-	-	(9.6)
At 31 March 2012	**40.5**	**135.1**	**853.1**	**160.0**	**-**	**1,188.7**
Net book value at 31 March 2012	**81.7**	**1,886.0**	**1,565.3**	**73.5**	**216.4**	**3,822.9**
Net book value at 31 March 2011	83.4	1,777.4	1,544.9	72.7	148.4	3,626.8
Net book value at 1 April 2010	79.6	1,711.8	1,544.9	71.2	111.4	3,518.9

Operational structures, plant and machinery include an element of land and buildings dedicated to those assets. The Group has applied IAS 23 Borrowing Costs (Revised) in the year and has capitalised £3.2 million for the year to 31 March 2012 (2011: £1.9 million). The capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation was 5.96% (2011: 5.96%).

It is not possible to separately identify the value of all land assets.

The net book value of property, plant and equipment held under hire purchase contracts and finance leases was as follows:

	31.3.2012 £m	31.3.2011 £m
Infrastructure assets	**46.8**	47.3
Operational structures, plant and machinery	**21.8**	22.0
	68.6	69.3

12. Investments

	31.3.2012 £m	31.3.2011 £m
Investments in jointly controlled entities	**4.3**	4.0

(a) Investments in jointly controlled entities
The Group, through Northumbrian Services Limited, holds 50% of the nominal value of issued ordinary £1 shares in Vehicle Lease and Service Limited (VLS), the Group's principal jointly controlled entity. VLS was incorporated in England and Wales and undertakes the business of hiring, leasing and servicing of vehicles and plant.

The Group, through Agrer, also holds a 50% interest in Agreco, a jointly controlled entity incorporated in Belgium.

	VLS 31.3.2012 £m	Agreco 31.3.2012 £m	VLS 31.3.2011 £m	Agreco 31.3.2011 £m
Revenue	**6.9**	**3.3**	6.7	3.2
Operating costs	**(5.9)**	**(2.9)**	(5.7)	(2.9)
Profit on ordinary activities before interest	**1.0**	**0.4**	1.0	0.3
Finance costs payable	**(0.5)**	**-**	(0.5)	-
Profit on ordinary activities before taxation	**0.5**	**0.4**	0.5	0.3
Current taxation	**-**	**-**	(0.1)	-
Profit for the year	**0.5**	**0.4**	0.4	0.3
Non-current assets	**8.5**	**-**	8.4	-
Current assets	**7.2**	**3.2**	7.7	1.4
Share of gross assets	**15.7**	**3.2**	16.1	1.4
Current liabilities	**(5.8)**	**(2.3)**	(4.9)	(0.8)
Non-current liabilities	**(6.5)**	**-**	(7.8)	-
Share of gross liabilities	**(12.3)**	**(2.3)**	(12.7)	(0.8)
Share of net assets	**3.4**	**0.9**	3.4	0.6

(b) The Group's interests in principal subsidiaries at 31 March 2012 were as follows:

Name of undertaking	Country of incorporation or registration and operation	Description of shares held	Proportion of nominal value of issued shares held by Group (%)	Business activity
Northumbrian Services Limited	England and Wales	Ordinary shares of £1	100	Holding of investments and loans
Northumbrian Water Limited	England and Wales	Ordinary shares of £1	100	Water and sewerage services
Northumbrian Water Finance plc	England and Wales	Ordinary shares of £1	100	Holding of finance instruments
Caledonian Environmental Services plc	Scotland	Ordinary shares of £1	100	Waste water services
Caledonian Environmental Levenmouth Treatment Services Limited	Scotland	Ordinary shares of £1	100	Waste water services
Ayr Environmental Services Limited	Scotland	Ordinary shares of £1	75	Waste water services
Ayr Environmental Services Operations Limited	Scotland	Ordinary shares of £1	100	Waste water services
AquaGib Limited	Gibraltar	Ordinary shares of £1	67	Water and sewerage services
Northumbrian Water Projects Limited	England and Wales	Ordinary shares of £1	100	Waste water services
SA Agrer NV	Belgium	Ordinary shares of £1	100	Aid funded project work

All subsidiaries listed above are indirectly held. The directors consider that to give full particulars of all subsidiary and associated undertakings would lead to a statement of excessive length. The above information relates to those subsidiary and associated undertakings or groups of undertakings whose results or financial position, in the opinion of the directors, principally affect the figures of the Group. A full list of the Company's subsidiaries is attached to the Company's latest annual return filed at Companies House.

13. Inventories

	31.3.2012 £m	31.3.2011 £m
Stores	**3.2**	3.3

14. Trade and other receivables

	31.3.2012 £m	31.3.2011 £m
Trade receivables	**84.4**	78.2
Amounts owed by jointly controlled entities	**0.6**	0.6
Prepayments and accrued income	**67.9**	60.3
Financial assets	**2.0**	3.8
Other receivables	**12.4**	11.0
	167.3	153.9

As at 31 March 2012, trade receivables at nominal value of £50.8 million (2011: £44.5 million) were impaired. Movements in the provision for impairment of trade receivables were as follows:

	£m
At 1 April 2010	37.1
Charge for the year	17.8
Utilised	(10.4)
At 1 April 2011	44.5
Charge for the year	17.8
Utilised	(11.5)
At 31 March 2012	**50.8**

At 31 March, the analysis of trade receivables overdue but not impaired is as follows:

	0-3 months £m	3-12 months £m	12-24 months £m	24-36 months £m	36-48 months £m	>48 months £m	Total £m
2012	**0.3**	**29.7**	**13.8**	**7.1**	**3.0**	**-**	**53.9**
2011	0.6	26.8	12.4	6.4	2.5	-	48.7

15. Cash and cash equivalents and short term deposits

For the purposes of the consolidated cash flow statement, cash and cash equivalents comprise the following at 31 March:

	31.3.2012 £m	31.3.2011 £m
Cash at bank and in hand	**75.3**	76.7
Cash equivalent deposits	**93.2**	65.0
	168.5	141.7
Bank overdrafts	**(1.4)**	(1.4)
Cash and cash equivalents	**167.1**	140.3

	31.3.2012 £m	31.3.2011 £m
Short term cash deposits >3 months	**4.3**	1.4

16. Trade and other payables

	31.3.2012 £m	31.3.2011 £m
Trade payables	**13.6**	16.5
Other payables	**23.3**	17.8
Interest payable	**46.0**	39.1
Accruals and deferred income	**93.0**	82.2
	175.9	155.6

17. Interest bearing loans and borrowings

	31.3.2012	31.3.2011
	£m	£m
Current:		
Bank overdrafts	**1.4**	1.4
Current instalments due on borrowings (principal £76.2million, 2011: £150.4 million)	**80.7**	155.1
Current obligations under finance leases and hire purchase contracts (see note 18)	**7.3**	7.2
	89.4	163.7
Non-current:		
Non-current obligations under finance leases and hire purchase contracts (principal £105.0million, 2011: £103.5 million) (see note 18)	**105.0**	103.5
Non-current instalments on borrowings (principal £2,624.1 million, 2011: £2,166.9 million)	**2,641.9**	2,192.3
	2,746.9	2,295.8
Borrowings comprise the following:		
Loans (principal £427.0 million, 2011: £527.1 million)	**429.1**	530.0
Subordinated loan stock (principal £1.9 million, 2011: £1.9 million)	**1.9**	1.9
Eurobonds – due 11 October 2017 bearing interest rate of 6.0% (principal £300.0 million, 2011: £300.0 million)	**306.3**	307.5
Eurobonds – due 6 February 2023 bearing interest rate of 6.875% (principal £350.0 million, 2011: £350.0 million)	**381.1**	384.0
Eurobonds – due 29 April 2033 bearing interest rate of 5.625% (principal £350.0 million, 2011: £350.0 million)	**346.5**	346.4
Eurobonds – due 23 January 2042 bearing interest rate of 5.125% (principal £360.0 million, 2011: £nil)	**356.4**	-
Eurobonds – due 23 January 2034 bearing interest rate of 5.87526% (principal £248.0 million, 2011: £248.0 million)	**241.7**	241.4
Eurobonds – due 31 March 2037 bearing interest rate of 6.627% (principal £61.5 million, 2011: £61.5 million)	**58.6**	58.9
USPP Notes – due 14 April 2021 bearing interest rate of 5.82% (principal £100.0 million, 2011: £nil)	**100.0**	-
Index linked Eurobonds – due 15 July 2036 bearing interest rate of 2.033% (principal £186.3 million, 2011: £177.6 million)	**185.4**	176.6
Index linked Eurobonds – due 30 January 2041 bearing interest rate of 1.6274% (principal £73.0 million, 2011: £69.8 million)	**73.2**	69.7
Index linked Eurobonds – due 16 July 2049 bearing interest rate of 1.7118% (principal £121.3 million, 2011: £115.7 million)	**121.2**	115.5
Index linked Eurobonds – due 16 July 2053 bearing interest rate of 1.7484% (principal £121.3 million, 2011: £115.7 million)	**121.2**	115.5
	2,722.6	2,347.4
Less current instalments due on bank loans (principal £76.2 million, 2011: £150.4 million)	**(80.7)**	(155.1)
	2,641.9	2,192.3

The difference between the principal value of £2,624.1 million (2011: £2,166.9 million) and the carrying value of £2,641.9 million (2011: £2,192.3 million) are unamortised issue costs of £17.2 million (2011: £14.1 million) and a credit of £35.0 million (2011: £39.5 million) in excess of the original loan proceeds to reflect the fair value of loans owed by subsidiaries acquired in 2003.

The Eurobonds – due 23 January 2034 are secured on the income receivable under the Kielder Water transfer scheme for the period to 23 January 2034.

The value of the capital and interest elements of the index linked Eurobonds are linked to movements in the UK RPI (see note 1(r)).

18. Obligations under hire purchase contracts and finance leases

	31.3.2012	31.3.2011
	£m	£m
Amounts due:		
Not later than one year	**7.3**	7.2
After one year but not more than five years	**25.0**	23.5
Later than five years	**147.5**	151.6
	179.8	182.3
Less finance charges allocated to future periods	**(67.5)**	(71.6)
Present value of minimum lease payments	**112.3**	110.7
Disclosed as due:		
Not later than one year	**7.3**	7.2
After more than one year	**105.0**	103.5
	112.3	110.7

Lease commitments
The Group has entered into non-cancellable operating leases in respect of land and buildings, plant, machinery and motor vehicles. The future minimum rentals payable under non-cancellable operating leases are as follows:

	31.3.2012	31.3.2011
	£m	£m
Not later than one year	**0.8**	0.7
After one year but not more than five years	**2.3**	2.4
After five years	**31.9**	26.6
	35.0	29.7

19. Provisions

	£m
At 1 April 2011	
Current	0.2
Non-current	2.4
At 1 April 2011	2.6
Utilised	(0.2)
At 31 March 2012	**2.4**
Analysed as:	
Current	0.2
Non-current	2.2
	2.4

The provision represents outstanding discretionary pension liabilities. The discretionary pension liabilities have been calculated by an independent actuary, using the same actuarial assumptions as applied to the defined benefit pension scheme (see note 25), and are expected to be paid over the remaining lives, which is approximately 10 years.

20. Financial instruments
(a) Group strategy
The level of capital expenditure which the Group is obliged to incur is such that it cannot be wholly financed by internally generated sources. As a result, the Group must rely upon raising additional finance on a regular basis, to be principally used to fund the long term assets required in its regulated business. The Group's strategy is to finance such investment by raising medium to long term debt, to provide a balance sheet match with long term assets and to fix a major proportion of interest rates.

(b) Treasury operations
The main purpose of the Group's treasury function is to assess the Group's ongoing capital requirement and to raise funding on a timely basis, taking advantage of any favourable market opportunities. It also invests any surplus funds the Group may have, based upon its forecast requirements and in accordance with the Group's treasury policy. On occasions, derivatives are used as part of this process but the Group's policies prohibit their use for speculation.

(c) Risks arising from the Group's financial instruments
The main risks arising from the Group's financial instruments are liquidity risk, interest rate risk and foreign currency risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below. All treasury activities are conducted in accordance with these policies.

(d) Liquidity risk
As regards day to day liquidity, the Group's policy is to have available standby committed bank borrowing facilities with a value of no less than £50.0 million and with a bank agreement availability period of no less than three months. At 31 March 2012, the Group had £450.0 million of undrawn committed bank facilities (2011: £35.0 million).

(e) Interest rate risk
The Group finances its operations through a mixture of retained profits and bank borrowings. It borrows at both fixed and floating rates of interest and, accordingly, uses interest rate swaps to generate the desired interest profile and to manage the Group's exposure to interest rate fluctuations. The Group's policy is to keep a minimum 60% of its borrowings at fixed rates of interest. At 31 March 2012, 75% (2011: 74%) of the Group's borrowings were at fixed rates of interest. Index linked borrowings are treated as variable rate debt.

(f) Foreign currency risk
The Group's policy is that any foreign currency exposure in excess of £100,000 sterling equivalent of a transactional nature, or £3.0 million sterling equivalent of a translation nature, should be covered immediately on identification. Any exposures are covered through the use of forward foreign exchange contracts.

(g) Market price risk
The Group's exposure to market price risk principally comprises interest rate exposures. The Group's policy is to accept a degree of interest rate risk. The following table shows the impact on profit and equity of an increase in the variable cost of borrowing. The range is considered reasonable based on the forecast variable rates of borrowing and all other elements being consistent for the next 12 months and highlights this is not material to the Group:

Increase in basis points	Effect on profit/equity £m
2012	
+50	**1.2**
+100	**2.5**
+150	**3.7**
2011	
+50	1.3
+100	2.5
+150	3.8

(h) Credit risk
There are no significant concentrations of credit risk within the Group. Management's assessment of the maximum credit risk exposure relating to financial assets is represented by their carrying value as at the balance sheet date (see (o)). A significant proportion of the trade debtor balances are with domestic customers who are unlikely to have a published credit rating.

(i) Counterparty risk
The treasury strategy, which is approved by the Board, requires that investments are limited to certain money market and treasury instruments, and that the Group's exposure to any single bank, building society or market is controlled, with maximum deposits allowed with any single counterparty. The investment criteria cover credit rating and asset size, including sovereign and political risk. Current market conditions have resulted in closer monitoring of counterparties and cancellation or suspension of deposits.

(j) Capital risk
The primary objective of the Group's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios in order to support its business and maximise shareholder value.

The Group monitors capital using gearing ratios for the Group and NWL. For NWL, this is net debt divided by the RCV as determined and published by Ofwat, and for the Group, RCV plus a pro forma RCV for the Kielder securitisation and the PFI contracts (at the level of associated debt included in the Group's net debt relating to those assets). The Group's policy is to keep the gearing ratio less than 75% and 70% for the Group and NWL, respectively.

For the Group, the pro forma RCV at 31 March 2012 was £3,871.4 million. For NWL, the RCV at 31 March 2012 was £3,550.0 million. On this basis, the gearing ratios were 68% for the Group and 64% for NWL.

(k) Contractual maturity of financial liabilities (principal and future interest payments)
The table below summarises the maturity profile of the Group's financial liabilities at 31 March based on contractual undiscounted payments, including the impact of interest rate swaps:

Year ended 31 March 2012

	On demand	Less than 3 months	3-12 months	1-5 years	More than 5 years	Total
	£m	£m	£m	£m	£m	£m
Interest bearing loans and borrowings	1.4	77.9	159.6	773.2	5,084.1	6,096.2
Trade and other payables	-	101.5	51.8	-	-	153.3
	1.4	**179.4**	**211.4**	**773.2**	**5,084.1**	**6,249.5**

Year ended 31 March 2011

	On demand	Less than 3 months	3-12 months	1-5 years	More than 5 years	Total
	£m	£m	£m	£m	£m	£m
Interest bearing loans and borrowings	1.4	162.4	124.6	704.5	4,381.8	5,374.7
Trade and other payables	-	82.3	48.7	-	-	131.0
	1.4	244.7	173.3	704.5	4,381.8	**5,505.7**

(l) Maturity profile of financial assets and liabilities (carrying value)
Year ended 31 March 2012

	Within 1 year	1-2 years	2-3 years	3-4 years	4-5 years	More than 5 years	Total
	£m	£m	£m	£m	£m	£m	£m
Fixed rate:							
Eurobonds	(4.0)	(4.2)	(4.3)	(4.2)	(5.0)	(1,668.9)	(1,690.6)
USPP notes	-	-	-	-	-	(100.0)	(100.0)
Subordinated loan stock	-	-	-	-	-	(1.9)	(1.9)
Bank loans	(20.9)	(21.3)	(21.3)	(22.1)	(22.0)	(124.0)	(231.6)
Obligations under finance leases and hire purchase contracts	(2.8)	(2.1)	(1.9)	(1.3)	(0.9)	(0.4)	(9.4)
Other loans	(0.3)	(0.3)	(0.4)	(0.3)	(0.3)	(0.4)	(2.0)
Fixed rate at 31 March 2012	**(28.0)**	**(27.9)**	**(27.9)**	**(27.9)**	**(28.2)**	**(1,895.6)**	**(2,035.5)**
Variable rate:							
Cash and cash equivalents	172.8	-	-	-	-	-	172.8
Financial investments	0.5	0.2	-	-	-	11.3	12.0
Eurobonds	-	-	-	-	-	(501.0)	(501.0)
Bank loans	(55.5)	(10.0)	(11.7)	(13.5)	(13.4)	(91.4)	(195.5)
Overdrafts	(1.4)	-	-	-	-	-	(1.4)
Obligations under finance leases and hire purchase contracts	(4.5)	(4.6)	(4.8)	(4.8)	(4.8)	(79.4)	(102.9)
Variable rate at 31 March 2012	**111.9**	**(14.4)**	**(16.5)**	**(18.3)**	**(18.2)**	**(660.5)**	**(616.0)**
Net borrowings at 31 March 2012							**(2,651.5)**

Year ended 31 March 2011

	Within 1 year £m	1-2 years £m	2-3 years £m	3-4 years £m	4-5 years £m	More than 5 years £m	Total £m
Fixed rate:							
Eurobonds	(4.2)	(4.1)	(4.2)	(4.2)	(4.3)	(1,317.2)	(1,338.2)
Subordinated loan stock	-	-	-	-	-	(1.9)	(1.9)
Bank loans	(24.3)	(21.2)	(21.1)	(21.3)	(22.1)	(145.9)	(255.9)
Obligations under finance leases and hire purchase contracts	(2.8)	(2.0)	(1.5)	(1.0)	(0.5)	(0.4)	(8.2)
Other loans	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)	(0.9)	(2.4)
Fixed rate at 31 March 2011	(31.6)	(27.6)	(27.1)	(26.8)	(27.2)	(1,466.3)	(1,606.6)
Variable rate:							
Cash and cash equivalents	143.1	-	-	-	-	-	143.1
Financial investments	0.9	0.5	0.2	-	-	11.3	12.9
Eurobonds	-	-	-	-	-	(477.3)	(477.3)
Bank loans	(126.3)	(55.4)	(10.0)	(10.0)	(10.0)	(60.0)	(271.7)
Overdrafts	(1.4)	-	-	-	-	-	(1.4)
Obligations under finance leases and hire purchase contracts	(4.4)	(4.4)	(4.5)	(4.5)	(4.5)	(80.2)	(102.5)
Variable rate at 31 March 2011	11.9	(59.3)	(14.3)	(14.5)	(14.5)	(606.2)	(696.9)
Net borrowings at 31 March 2011							(2,303.5)

The variable rate net borrowings comprise sterling denominated bank borrowings and deposits that bear interest at rates based upon up to 12 months LIBOR.

(m) Currency exposures
At 31 March 2012, after taking into account the effects of forward foreign exchange contracts, the Group had no currency exposures (2011: £nil).

(n) Borrowing facilities
The Group has various undrawn committed borrowing facilities. The facilities available at 31 March, in respect of which all conditions precedent have been met, are as follows:

	31.3.2012 £m	31.3.2011 £m
Expiring in less than one year	**-**	35.0
Expiring in more than two years but not more than five years	**450.0**	-

(o) Fair values of financial assets and financial liabilities
A comparison by category of book values, which are all recognised at amortised cost except for interest rate swaps which are recognised at fair value, and fair values of the Group's financial assets and liabilities as at 31 March is set out below:

	Book value		Fair value	
	31.3.2012	31.3.2011 restated	**31.3.2012**	31.3.2011 restated
	£m	£m	**£m**	£m
Financial assets:				
Cash and cash equivalents	**172.8**	143.1	**172.8**	143.1
Financial investments	**12.0**	12.9	**12.0**	12.9
Trade and other receivables	**167.3**	153.9	**167.3**	153.9
Financial liabilities:				
Overdraft	**(1.4)**	(1.4)	**(1.4)**	(1.4)
Bank loans (principal of £427.0 million, 2011: £527.1million)	**(429.1)**	(530.0)	**(445.7)**	(541.3)
Subordinated loan stock (principal of £1.9 million, 2011: £1.9 million)	**(1.9)**	(1.9)	**(1.9)**	(1.9)
Eurobonds (principal of £2,171.4 million, 2011: £1,788.3 million)	**(2,191.6)**	(1,815.5)	**(2,474.0)**	(1,899.2)
USPP notes (principal of £100.0 million, 2011: nil)	**(100.0)**	-	**(111.8)**	-
Obligations under finance leases and hire purchase contracts (principal of £112.3 million, 2011: £110.7 million)	**(112.3)**	(110.7)	**(112.3)**	(110.7)
Cash flow hedges	**(63.8)**	(58.7)	**(63.8)**	(58.7)
Trade and other payables	**(175.9)**	(155.5)	**(175.9)**	(155.5)
	(2,723.9)	(2,363.8)	**(3,034.7)**	(2,458.8)

The fair values of the cash flow hedges and sterling denominated long term fixed rate and index linked debt with a book value of £2,191.6 million (2011: £1,815.5 million), have been determined by reference to prices available from the markets on which the instruments involved are traded. All the other fair values shown above have been calculated by discounting cash flows at prevailing interest rates.

In the absence of an openly traded market value for the index linked bonds with a book value of £501.0 million (2011: £477.3 million), the fair value at the balance sheet date has been calculated by considering the remaining debt maturity, the relevant UK index linked gilt rate and an appropriate credit spread by reference to market evidence for conventional bonds.

The difference between the principal value of £2,812.6 million (2011: £2,428.0 million) and the carrying value of £2,834.9 million (2011: £2,458.1 million) are unamortised issue costs of £17.2 million (2011: £14.3 million) and a credit of £39.5 million (2011: £44.4 million) in excess of the original loan proceeds to reflect the fair value of loans owed by subsidiaries acquired in 2003.

(p) Hedges
Cash flow hedges – currency forward contracts
At 31 March 2012, the Group held no forward exchange contracts (2011: nil).

Cash flow hedges – interest rate swap
At 31 March 2012, the Group held one interest rate swap, designated as a hedge of future interest cash flows, for which the Group has firm commitments. The swap was used to convert variable rate interest payments to a fixed rate basis. The terms of this swap were as follows:

Notional amount	Start date	Termination date	Fixed rate%
GBP 100.0 million	**15.9.2008**	**15.3.2022**	**4.79**

The swap was designated as highly effective.

At 31 March 2011, the Group held three interest rate swaps, designated as a hedge of future interest cash flows, for which the Group had firm commitments. The swaps were used to convert variable rate interest payments to a fixed rate basis. The terms of these swaps were as follows:

Notional amount	Start date	Termination date	Fixed rate%
GBP 100.0 million	15.9.2008	15.3.2022	4.79
GBP 62.5 million	29.1.2009	31.5.2011	2.345
GBP 62.5 million	29.1.2009	31.5.2011	2.435

The £100.0 million swap was designated as highly effective. The two £62.5 million swaps were not effective.

Cash flow hedges – inflation swap
As at 31 March 2012, 2011 and 2010, the Group held an inflation swap, designated as a hedge of future inflation-linked cash flows. The swap was used to convert variable inflation-linked revenues on a contract with the Environment Agency, to fixed.

The cash flow hedge was designated as highly effective. In consequence, the inflation-linked revenues are fixed and are accounted for in the consolidated income statement on an accruals basis. The inflation swap and the inflation-linked cash flows occur simultaneously and the amount accumulated in equity is reclassified to profit or loss over the period during which the inflation-linked cash flows affect profit or loss.

The terms of the swap, including its maturity and the cash value of the annual outflow under the inflation swap based on current rates, are as follows:

Notional amount	Annual swap cash flow paid	Start date	Termination date	Fixed rate%
GBP 2.9 million	**0.9 million**	**12.5.2004**	**9.1.2034**	**2.62**

(q) Fair value hierarchy
The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

Liabilities measured at fair value

Year ended 31 March 2012

	31.3.2012	**Level 1**	**Level 2**	**Level 3**
	£m	**£m**	**£m**	**£m**
Interest rate swap	**(15.1)**	**-**	**(15.1)**	**-**
Inflation swap	**(48.7)**	**-**	**(48.7)**	**-**

Year ended 31 March 2011 restated

	31.3.2011	**Level 1**	**Level 2**	**Level 3**
	£m	**£m**	**£m**	**£m**
Interest rate swaps	(9.8)	-	(9.8)	-
Inflation swap	(48.9)	-	(48.9)	-

Year ended 31 March 2010 restated

	31.3.2010	**Level 1**	**Level 2**	**Level 3**
	£m	**£m**	**£m**	**£m**
Interest rate swaps	(12.5)	-	(12.5)	-
Inflation swap	(42.3)	-	(42.3)	-

During the year to 31 March 2012, there were no transfers between level 1 and level 2 fair value measurements, and no transfers into and out of level 3 fair value measurements. All other financial assets and liabilities are carried at amortised cost.

21. Authorised and issued share capital

	31.3.2012 £m	31.3.2011 £m
Authorised:		
700 million ordinary shares of 10 pence each	**70.0**	70.0
Allotted, called up and fully paid:		
518.6 million ordinary shares of 10 pence each	**51.9**	51.9

22. Prior period adjustment

The Group is party to an inflation hedge which commenced in May 2004 as part of the issue of the Eurobonds due in January 2034. The Group has not previously accounted for the fair value of this hedge instrument. However, the directors have determined that the fair value should be recognised in the consolidated balance sheet in accordance with IAS 39 Financial Instruments: Recognition and Measurement.

Comparative information has been restated in the consolidated balance sheet, consolidated statement of comprehensive income and consolidated statement of changes in equity and in notes 7 and 20, in accordance with IAS 1 Presentation of Financial Statements.

The impact of the restatement on the consolidated balance sheet is as follows:

	31.3.2011 £m	change £m	31.3.2011 restated £m	31.3.2010 £m	change £m	31.3.2010 restated £m
Non-current liabilities						
Deferred income tax liabilities	(598.7)	12.7	(586.0)	(606.1)	11.8	(594.3)
Hedging instruments	-	(53.7)	(53.7)	-	(48.4)	(48.4)
Non-current liabilities	(3,204.8)	(41.0)	(3,245.8)	(3,416.6)	(36.6)	(3,453.2)
Current liabilities						
Hedging instruments	(9.8)	4.8	(5.0)	(12.5)	6.1	(6.4)
Current liabilities	(331.9)	4.8	(327.1)	(205.2)	6.1	(199.1)
Total liabilities	(3,536.7)	(36.2)	(3,572.9)	(3,621.8)	(30.5)	(3,652.3)
Net assets	475.9	(36.2)	439.7	313.9	(30.5)	283.4
Cash flow hedge reserve	(6.6)	(36.2)	(42.8)	(8.2)	(30.5)	(38.7)
Equity shareholder' funds	473.6	(36.2)	437.4	311.1	(30.5)	280.6
Total capital and reserves	475.9	(36.2)	439.7	313.9	(30.5)	283.4

23. Additional cash flow information

Analysis of net debt as at 31 March 2012

	As at 1.4.2011 £m	Cash flow £m	Other non-cash movements £m	As at 31.3.2012 £m
Cash and cash equivalents	140.3	26.8	-	**167.1**
Short term cash deposits	1.4	2.9	-	**4.3**
Financial investments	12.9	(0.9)	-	**12.0**
Loans (principal of £2,700.3 million, 2011: £2,317.3 million)	(2,347.4)	(355.6)	(19.6)	**(2,722.6)**
Finance leases (principal of £112.3 million, 2011: £110.7 million)	(110.7)	3.2	(4.8)	**(112.3)**
	(2,303.5)	(323.6)	(24.4)	**(2,651.5)**

The difference between the principal value of £2,812.6 million (2011: £2,428.0 million) and the carrying value of £2,834.9 million (2011: £2,458.1 million) are unamortised issue costs of £17.2 million (2011: £14.3 million) and a credit of £39.5 million (2011: £44.4 million) in excess of the original loan proceeds to reflect the fair value of loans owed by subsidiaries acquired in 2003.

Non-cash movements on loans relate to the principal uplift on index linked borrowings and amortisation of loan issue costs offset by the amortisation of debt fair value for the year. Non-cash movements on finance leases relate to the inception of new finance leases on the acquisition of plant and machinery during the year.

Analysis of net debt as at 31 March 2011

	As at 1.4.2010	Cash flow	Other non-cash movements	As at 31.3.2011
	£m	£m	£m	£m
Cash and cash equivalents	173.3	(33.0)	-	140.3
Short term cash deposits	15.8	(14.4)	-	1.4
Financial investments	14.0	(1.1)	-	12.9
Loans (principal of £2,317.3 million, 2010: £2,319.8 million)	(2,354.4)	19.9	(12.9)	(2,347.4)
Finance leases (principal of £110.7 million, 2010: £111.1 million)	(111.1)	7.3	(6.9)	(110.7)
	(2,262.4)	(21.3)	(19.8)	(2,303.5)

The difference between the principal value of £2,428.0 million (2010: £2,430.9 million) and the carrying value of £2,458.1 million (2010: £2,465.5 million) are unamortised issue costs of £14.3 million (2010: £14.7 million) and a credit of £44.4 million (2010: £49.3 million) in excess of the original loan proceeds to reflect the fair value of loans owed by subsidiaries acquired in 2003.

Non-cash movements on loans relate to the principal uplift on index linked borrowings and amortisation of loan issue costs offset by the amortisation of debt fair value for the year. Non-cash movements on finance leases relate to the inception of new finance leases on the acquisition of plant and machinery during the year.

24. Financial commitments

	31.3.2012	31.3.2011
	£m	£m
Expenditure contracted for	**172.8**	222.3

In addition to these commitments, the Group has longer term expenditure plans, which include investment to meet shortfalls in performance and condition, and to provide for new demand and growth within the water and sewerage business.

25. Pensions and other post-retirement benefits

The Group operates a defined benefit pension scheme, Northumbrian Water Pension Scheme (NWPS or the scheme), providing benefits based on final pensionable remuneration to 1,830 active members at 31 March 2012 (2011: 1,908).

The assets of the NWPS are held separately from those of the Group in independently administered funds.

The most recent actuarial valuation of the scheme was at 31 December 2010. At that date the value of assets amounted to £680.1 million and the funding level was 84.7%.

The future service contribution rate jointly payable by members and the employers from 31 December 2010 was 24.2% of pensionable salaries. Members' contributions are 7.3% on average with the employers paying 16.9%.

The employer contribution rate was assessed using the projected unit method and the following actuarial assumptions:

	%
Pre-retirement discount rate	5.80
Post-retirement discount rate	4.90
Pay increases	3.85
Price inflation (RPI)	3.60
Price inflation (CPI)	2.90
Pension increases linked to RPI	3.60
Price inflation linked to CPI	2.90

With the agreement of the NWPS Trustee, the employers have made capital contributions of £70.0m to cover the period 1 January 2011 to 31 March 2015. These payments comprise employers' contributions, the deficit recovery funding assumed in the final determination and employees contributions under a salary sacrifice arrangement. Amounts totalling £22.9m were paid prior to 31 March 2011 with the remaining £47.1m paid in the current period. Further payments of £3.1m relating to early retirements were paid in the period bringing total contributions to £50.2m. Contributions for the next financial period, to 31 December 2012, are expected to be £0.4m, relating to early retirements.

The scheme also has a defined contribution section which had 542 active members at 31 March 2012 (2011: 460). Members can choose to contribute either 3%, 4% or 5% of salary, with employers contributing at either 6%, 7% or 8% depending on the member contribution rate. The contributions paid to the defined contribution section by the Company in the year totalled £0.9m (2011: £0.8m).

The additional disclosures regarding the defined benefit scheme as required under IAS 19 Employee benefits and the relevant impact on the financial statements are set out below.

A qualified actuary, using revised assumptions that are consistent with the requirements of IAS 19, has updated the actuarial valuation described above as at 31 March 2012. Investments have been valued, for this purpose, at fair value.

	31.3.2012	31.3.2011
Pay increases[1]	**3.85%**	4.50%
RPI inflation	**3.20%**	3.50%
CPI inflation	**2.50%**	2.80%
Pension increases linked to RPI	**3.20%**	3.50%
Pension increases linked to CPI	**2.50%**	2.80%
Discount rate	**4.80%**	5.50%
Mortality assumptions[2]	**PCMA/PCFA00**	PCMA/PCFA00
- Life expectancy for a member aged 65 – female (years)	**24.3**	23.0
- Life expectancy for a member aged 65 – male (years)	**22.0**	20.7

Notes:

1. Including promotional salary scale.
2. 115% of PCMA00/PCFA00 (year of birth with medium cohort improvements).

The fair value of the assets in the NWPS, the present value of the liabilities in the scheme and the long term expected rate of return at 31 March were:

	Long term expected rate of return 31.3.2012 %	**31.3.2012 £m**	Long term expected rate of return 31.3.2011 %	31.3.2011 £m
Equities	**6.3**	**441.8**	7.3	511.8
Corporate bonds	**4.8**	**128.1**	5.5	62.1
Government bonds	**3.3**	**80.4**	4.3	63.9
Property	**4.8**	**76.0**	5.8	71.6
Cash	**2.5**	**12.0**	3.8	3.9
Total fair value of assets		**738.3**		713.3
Present value of liabilities		**(822.4)**		(759.3)
Deficit		**(84.1)**		(46.0)

The discount rate at 31 March 2012 has been set by reference to the yield on AA corporate bonds at that date, extrapolated forward to a duration of 18 years which reflect the duration of the expected benefit payments. The expected rate of return on equities represents a 3.0% premium of the yield on long term Government bonds at 31 March 2012. The gross redemption yield on index linked UK Government stocks was 3.3%. The long term inflation rate implied by these yields is 3.3% which has been reduced by 0.1% to allow for an inflation risk premium. Post-retirement mortality assumptions use a base table of 115% of PCMA00/PCFA00 with an allowance for future improvements in line with the medium cohort projections, lagged to apply 10 years later, based on each individual's year of birth. This is subject to a minimum improvement of 1.0% per annum.

The amounts recognised in the income statement and in the statement of comprehensive income for the year are analysed as follows:

	31.3.2012 £m	31.3.2011 £m
Recognised in the income statement:		
Current service cost	**12.5**	13.5
Past service cost	**0.3**	0.4
Recognised in operating costs in arriving at profit on ordinary activities before interest	**12.8**	13.9
Interest cost on plan obligations	**41.3**	43.3
Expected return on plan assets	**(49.3)**	(45.5)
Recognised in (income receivable)/finance costs payable	**(8.0)**	(2.2)
Recognised in the statement of comprehensive income:		
Actual return on scheme assets	**7.1**	56.2
Less expected return on scheme assets	**(49.3)**	(45.5)
	(42.2)	10.7
Other actuarial gains and losses	**(41.3)**	63.3
Net actuarial (losses)/gains	**(83.5)**	74.0
Cumulative amounts recognised since adopting the standard	**(90.0)**	(6.5)

History of experience gains and losses:

	31.3.2012 £m	31.3.2011 £m	31.3.2010 £m	31.3.2009 £m	31.3.2008 £m
Fair value of assets	**738.3**	713.3	663.4	478.6	666.7
Present value of defined benefit obligation	**(822.4)**	(759.3)	(796.5)	(598.0)	(576.2)
(Deficit)/surplus	**(84.1)**	(46.0)	(133.1)	(119.4)	90.5
Experience adjustments arising on plan assets	**(42.2)**	10.7	177.4	(205.3)	(93.4)
Experience adjustments arising on plan liabilities	**31.0**	-	-	18.7	0.6

Changes in the present value of the defined benefit pension obligations are analysed as follows:

	31.3.2012 £m	31.3.2011 £m
At 1 April	**759.3**	796.5
Current service cost	**12.5**	13.5
Past service cost	**0.3**	0.4
Interest cost on plan obligations	**41.3**	43.3
Contributions by plan participants	**0.1**	0.1
Actuarial loss/(gain) on obligations	**41.3**	(63.3)
Benefits paid	**(32.4)**	(31.2)
At 31 March	**822.4**	759.3
Present value of funded defined benefit obligations	**822.4**	759.3

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

	31.3.2012 £m	31.3.2011 £m
At 1 April	**713.3**	663.4
Expected return on plan assets	**49.3**	45.5
Actuarial (loss)/gain on plan assets	**(42.2)**	10.7
Contributions by employer	**50.2**	24.8
Contributions by plan participants	**0.1**	0.1
Benefits paid	**(32.4)**	(31.2)
At 31 March	**738.3**	713.3

The Group through its subsidiary, AquaGib, also operates a non-contributory defined benefit scheme. The deficit at 31 March 2012, under local GAAP, was £3.6 million (2011: £2.1 million). The Group made contributions amounting to £0.9 million (2011: £1.0 million) to the defined benefit pension scheme.

Sensitivity to key assumptions

IAS 1 requires disclosure of the sensitivity of the results to the methods and assumptions used.

The costs of a pension arrangement require estimates regarding future experience. The financial assumptions used for IAS 19 reporting are the responsibility of the directors of the Company. These assumptions reflect market conditions at the balance sheet date. Changes in market conditions which result in changes in the net discount rate (essentially the difference between the discount rate and the assumed rates of increases of salaries, deferred pension revaluation or pensions in payment), can have a significant effect on the value of the liabilities reported.

A reduction in the net discount rate will increase the assessed value of liabilities, as a higher value is placed on benefits paid in the future. A rise in the net discount rate will have an opposite effect of similar magnitude. The overall effect of a change in the net discount rate of 0.1% would change the liabilities by around £14 million.

There is also uncertainty around life expectancy for the UK population. The value of current and future pension benefits will depend on how long they are assumed to be in payment.

The disclosures have been prepared using the mortality assumptions used in the 2010 formal valuation. Specifically, the post-retirement mortality assumptions use a base table of 115% of PCMA00/PCFA00 with an allowance for future improvements in line with the medium cohort projections, lagged to apply 10 years later, based on each individual's year of birth. This is subject to a minimum improvement of 1.0% per annum. These assumptions imply an assumed life expectancy for a member aged 65 at 31 March 2012 of 22.0 years (2011: 20.7 years) for males and 24.3 years (2011: 23.0 years) for females.

The effect of increasing the assumed life expectancies by one year would be to increase the value of liabilities by around 3%.

26. Long Term Incentive Plan

Prior to the change of control and delisting on 14 October 2011, the Company operated a share based LTIP. Accordingly, the accounting treatment is only relevant up to this date and was not in place at the balance sheet date.

Under the LTIP, executive directors and senior managers may receive, at the discretion of the Remuneration Committee, annual conditional awards of shares in the Company. Further details of the LTIP can be found in note 5.

The following table illustrates the movements in conditional share awards during the year.

	31.3.2012 Number	31.3.2011 Number
Outstanding at 1 April	**1,120,941**	1,242,293
Granted during the year	**-**	378,503
Forfeited/lapsed during the year	**(340,222)**	(351,299)
Exercised	**(780,719)**	(148,556)
Outstanding at 31 March	**-**	1,120,941
Exercisable at 31 March	**-**	4,649

The weighted average exercise price throughout the year was £nil (2011: £nil). The fair value of conditional share awards granted during the year was £nil (2011: £nil million).

The weighted average share price at the date of exercise for the conditional share awards was 465.00 pence (2011: 324.79 pence).

No conditional awards were outstanding as at 31 March 2012. The weighted average remaining contractual life as at 31 March 2011, was 1.7 years.

The fair value of conditional share awards granted was estimated using the Monte-Carlo model. The significant inputs to the model were as follows:

	31.3.2012	31.3.2011
Dividend yield	**-**	4.0%
Expected share price volatility	**-**	28%
Expected FTSE 250 Index volatility	**-**	21%
Risk free interest rate	**-**	1.5%
Expected life of option (years)	**-**	3

The expected life of these options was based on historical data and was not necessarily indicative of exercise patterns that may have occurred. The expected volatility reflects the assumption that the historical volatility was indicative of future trends, which was not necessarily the actual outcome.

Share Incentive Plan

Prior to the change of control and delisting on 14 October 2011 the Company operated a SIP. Accordingly, the accounting treatment is only relevant up to this date and was not in place at the balance sheet date.

The SIP scheme provided one free matching share for every three shares purchased by an employee. Shares for the SIP were purchased at market price by the Trustee and dividends were paid in cash directly to participants.

The following table illustrates the movements in conditional share awards during the year.

	31.3.2012 Number	31.3.2011 Number
Outstanding at 1 April	**160,182**	143,201
Granted during the year	**150,596**	115,519
Forfeited during the year	**(1,497)**	(3,383)
Exercised	**(309,281)**	(95,155)
Outstanding at 31 March	**-**	160,182

27. Special purpose entities

As noted under accounting policy 1(b), under SIC 12, two companies are consolidated as special purpose entities. The principal special purpose entity is Bakethin Holdings Limited, the shares in which are owned by Bakethin Charitable Trust. The other special purpose entity is Bakethin Finance plc, which is a wholly owned subsidiary of Bakethin Holdings Limited.

Bakethin Finance plc was established for the purpose of issuing guaranteed secured Eurobonds. On 12 May 2004, Bakethin Finance plc issued £248.0 million of guaranteed secured bonds maturing January 2034. Bakethin Finance plc used the proceeds of the bond issue to make a loan to Reiver Finance Limited to fund the consideration given by that company to Northumbrian Water Limited for the securitisation of the cash flows receivable from the EA under the Water Resources Operating Agreement relating to Kielder Water transfer scheme. The assignment is for a period of 30 years.

The summarised combined financial statements of the special purpose entities are as follows:

	31.3.2012 £m	31.3.2011 £m
Income statement:		
Finance costs receivable	**14.9**	14.9
Finance costs payable	**(14.9)**	(14.9)
Balance sheet:		
Investments	**241.7**	241.4
Current assets	**4.8**	4.7
Non-current liabilities	**(243.6)**	(243.2)
Current liabilities	**(2.7)**	(2.7)
Net assets	**0.2**	0.2

28. Related parties

During the year, the Group entered into transactions, in the ordinary course of business, with other related parties. Transactions entered into and trading balances outstanding at 31 March between the Group and its associates and joint ventures, are as follows:

Trading transactions

	Sales to related party £m	Purchases from related party £m	Amounts owed by related party £m	Amounts owed to related party £m
Related party:				
Jointly controlled entities				
2012	**0.1**	**11.2**	**0.6**	**8.7**
2011	0.1	9.6	0.6	8.2

Purchases from jointly controlled entities include £3.6 million (2011: £2.5 million) in respect of capital purchases under finance leases, £0.1 million (2011: £0.1 million) in respect of operating leases, £6.7 million (2011: £6.3 million) in respect of costs payable under finance leases and £0.8 million (2011: £0.7 million) in respect of other purchases.

Outstanding balances due from related parties are expected to be settled within 60 days and amounts due to related parties are in respect of leasing arrangements, where the amounts owed will relate specifically to the terms of the lease.

Remuneration of key management personnel

The remuneration of the directors is included within the amounts disclosed below. Further information about the remuneration of directors is provided in note 5.

	31.3.2012 £m	31.3.2011 £m
Short term employee benefits	**1.6**	1.4
Post employment benefits	**0.2**	0.2
Other long-term employee benefits	**0.6**	-
Termination benefits	**0.1**	-
Share based payments	**-**	0.5
	2.5	2.1

29. Ultimate parent company

The Company's immediate parent undertaking is UKW, which is incorporated in England and Wales.

In the directors' opinion, UKW is the Company's ultimate parent undertaking and controlling party. UKW acquired Northumbrian Water Group plc on 14 October 2011. UKW is indirectly wholly owned by a consortium comprising Cheung Kong Infrastructure Holdings Limited, Cheung Kong (Holdings) Limited and Li Ka Shing Foundation Limited.

Copies of UKW's group financial statements, which include the Company, will be available in due course from Northumbria House, Abbey Road, Pity Me, Durham, DH1 5FJ.

Statement of directors' responsibilities in relation to the parent Company financial statements

The directors are responsible for preparing the annual report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under Company Law, the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing 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 United Kingdom Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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

Company balance sheet
As at 31 March 2012

	Notes	31.3.2012 £m	31.3.2011 £m
Fixed assets			
Investments in subsidiary undertakings	4	**1,101.4**	1,101.4
		1,101.4	1,101.4
Current assets			
Debtors: receivable within one year	5	**7.1**	3.5
Debtors: receivable in greater than one year	5	**100.0**	-
Cash at bank		**13.4**	59.1
		120.5	62.6
Creditors: amounts falling due within one year	6	**(8.3)**	(93.2)
Net current assets/(liabilities)		**112.2**	(30.6)
Total assets less current liabilities		**1,213.6**	1,070.8
Creditors: amounts falling due after more than one year	7	**(660.0)**	(490.0)
Net assets		**553.6**	580.8
Capital and reserves			
Called up share capital	8	**51.9**	51.9
Share premium account	9	**446.5**	446.5
Treasury shares	9	**-**	(1.7)
Profit and loss account	9	**55.2**	84.1
Equity shareholders' funds		**553.6**	580.8

Approved by the Board on 4 October 2012 and signed on its behalf by:

Heidi Mottram
Chief Executive Officer

Chris Green
Finance Director

Notes to the Company financial statements

1. Accounting policies
(a) Basis of accounting
The financial statements have been prepared in accordance with applicable United Kingdom law and accounting standards. The accounting policies have been reviewed in accordance with the requirements of FRS 18: Accounting Policies. The directors consider the following accounting policies to be relevant in relation to the Company's financial statements. The Company's financial statements are included in the consolidated financial statements of Northumbrian Water Group Limited. Accordingly, the Company has taken advantage of the exemption from publishing a profit and loss account and cash flow statement and from disclosing related party transactions with its wholly-owned subsidiaries. The Company is also exempt from disclosing the information otherwise required by FRS 29 Financial Instruments: Disclosures, as the consolidated financial statements, in which the Company is included, provide equivalent disclosures for the Group under IFRS 7 Financial Instruments: Disclosures.

The financial statements have been prepared on a going concern basis which assumes that the Company will have adequate funding to meet its liabilities as they fall due in the foreseeable future. As at 31 March 2012 the Company had net current assets of £112.3 million (2011: net current liabilities of £30.6 million). The directors have reviewed cash flow requirements and believe it is appropriate to prepare the financial statements on a going concern basis.

(b) Fixed asset investments
Fixed asset investments are stated at their purchase cost, less any provision for impairment.

(c) Taxation
Corporation tax is based on the profit for the year as adjusted for taxation purposes using the rates of tax enacted at the balance sheet date. Provision is made for deferred tax in respect of all timing differences that have originated but not reversed at the balance sheet date that will result in an obligation to pay more, or a right to pay less, tax in future periods. Deferred tax is calculated at the tax rates that are expected to apply in the periods in which timing differences are expected to reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date. Deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

(d) Interest bearing loans and borrowings
All loans and borrowings are initially stated at the amount of the net proceeds, being fair value of the consideration received net of issue costs associated with the borrowing. Finance costs (including issue costs) are taken to the income statement over the term of the debt at a constant rate on the balance sheet carrying amount. The carrying amount is increased by the finance charges amortised and reduced by payments made in respect of the accounting period.

2. Auditors' remuneration
Auditors' remuneration for the year ended 31 March 2012 was £8,000 (2011: £97,000).

Fees paid to Deloitte LLP for non-audit services to the Company itself are not disclosed in the individual financial statements of the Company because Group financial statements are prepared which are required to disclose such fees on a consolidated basis.

3. Profit attributable to members of the parent Company
The profit dealt with in the financial statements of the parent Company is £253.4 million (2011: £106.9 million).

4. Investments in subsidiary undertakings

	£m
At 1 April 2011	1,101.4
At 31 March 2012	**1,101.4**

Name of undertaking	Country of incorporation or registration and operation	Description of shares held	Proportion of nominal value of issued shares held by Group (%)	Business activity
Northumbrian Services Limited	England and Wales	Ordinary shares of £1	100	Holding of investments and loans
Northumbrian Water Limited	England and Wales	Ordinary shares of £1	100	Water and sewerage services
Northumbrian Water Finance plc	England and Wales	Ordinary shares of £1	100	Holding of finance instruments
Caledonian Environmental Services plc	Scotland	Ordinary shares of £1	100	Waste water services
Caledonian Environmental Levenmouth Treatment Services Limited	Scotland	Ordinary shares of £1	100	Waste water services
Ayr Environmental Services Limited	Scotland	Ordinary shares of £1	75	Waste water services
Ayr Environmental Services Operations Limited	Scotland	Ordinary shares of £1	100	Waste water services
AquaGib Limited	Gibraltar	Ordinary shares of £1	67	Water and sewerage services
Northumbrian Water Projects Limited	England and Wales	Ordinary shares of £1	100	Waste water services
SA Agrer NV	Belgium	Ordinary shares of £1	100	Aid funded project work

All subsidiaries listed above are indirectly held. The directors consider that to give full particulars of all subsidiary and associated undertakings would lead to a statement of excessive length. A full list of the Company's subsidiaries is attached to the Company's latest annual return filed at Companies House.

5. Debtors

	31.3.2012	31.3.2011
	£m	£m
Amounts falling due within one year:		
Amounts owed by subsidiary undertakings	**7.0**	3.3
Other	**0.1**	0.2
	7.1	3.5
Amounts falling due after one year:		
Amounts owed by subsidiary undertakings	**100.0**	-
	100.0	-

Amounts owed by subsidiary undertakings include amounts receivable for the provisional surrender of tax losses amounting to £2.8 million (2011: £1.6 million).

6. Creditors: amounts falling due within one year

	31.3.2012	31.3.2011
	£m	£m
Trade creditors	**0.1**	0.1
Amounts owed to subsidiary undertakings	**5.5**	93.0
Interest payable	**2.7**	-
Accruals and deferred income	**-**	0.1
	8.3	93.2

7. Creditors: amounts falling due after more than one year

	31.3.2012	31.3.2011
	£m	£m
Loans	**100.0**	-
Amounts owed to subsidiary undertakings	**560.0**	490.0
	660.0	490.0

	31.3.2012	31.3.2011
	£m	£m
Loans are repayable as follows:		
Repayable after more than five years	**660.0**	490.0

In April 2011 the company issued £100 million USPP notes, maturing April 2021, with an annual coupon of 5.82%.

Amounts owed to subsidiary undertakings bear rates of interest linked to LIBOR. The loans will continue until such time as terminated by mutual agreement.

8. Authorised and issued share capital

	31.3.2012	31.3.2011
	£m	£m
Authorised:		
700 million ordinary shares of 10 pence	**70.0**	70.0
Allotted, called up and fully paid:		
518.6 million ordinary shares of 10 pence	**51.9**	51.9

9. Reserves

	Treasury shares	Share premium account	Profit and loss account
	£m	£m	£m
At 1 April 2010	(2.0)	446.5	47.8
Profit for the year	-	-	106.9
Exercise of LTIP awards	0.3	-	(0.3)
Dividends paid	-	-	(70.3)
At 31 March 2011	(1.7)	446.5	84.1
Profit for the year	-	-	253.3
Share-based payment	-	-	1.1
Exercise of LTIP awards	1.7	-	(1.7)
Dividends paid	-	-	(281.6)
At 31 March 2012	**-**	**446.5**	**55.2**

10. Commitments

The Company has issued letters of continuing support to subsidiary companies with net liabilities amounting to £16.0 million (2011: £11.9 million) and net current liabilities of £nil (2011: £nil). These subsidiary companies are expected to meet their working capital requirements from operating cash flows.

The Company is guarantor to the EIB in respect of borrowings by Northumbrian Water Limited. The loan principal outstanding at 31 March 2012 amounted to £371.7 million (2011: £344.7 million).

The Company is party to a cross guarantee arrangement with other Group companies in respect of bank facilities. Overdrafts outstanding at 31 March 2012 in respect of the arrangement amounted to £1.0 million (2011: £27.2 million). The directors do not expect any loss to arise as a result of this arrangement.