REGULATORY ACCOUNTS 2010

CONTENTS

OUR BUSINESS

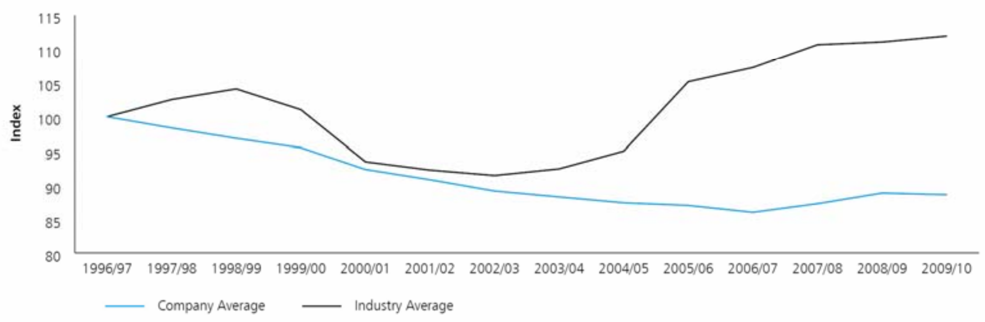
Portsmouth Water provides water to 303,000 homes and businesses in an area covering 868 square kilometres from the River Meon in Hampshire to the River Arun in West Sussex. The Company serves the cities and towns of Portsmouth, Chichester, Fareham, Gosport, Havant and Bognor Regis. On average, each day it supplies approximately 180 million litres of water through a network of over 3,266 kilometres of underground mains. Water supplied is derived from the chalk of the South Downs and is abstracted from wells, boreholes, springs and the River Itchen. The table below shows the major sources used by the Company during the year. The springs at Havant and Bedhampton, which provide nearly 26% of the total supply, are thought to be the largest group of springs used for public supplies in Europe.

Source	**Actual 2009/10 Abstraction (Million Litres)**	**% of Supply 2009/10**	**% of Supply 2008/09**
Springs at Havant & Bedhampton	17,186	26	29
River Itchen	8,880	13	10
Boreholes, Wells & Adits	40,270	61	61
Totals	**66,336**	**100**	**100**

Water from the springs at Havant and Bedhampton is treated at the Farlington treatment works and there are also treatment works at the River Itchen, Lovedean, Soberton and Fishbourne. The last three works accounted for approximately 6% of supplies in 2009/10. Water from the remaining sources requires less sophisticated treatment.

Portsmouth Water's charges are the lowest in England and Wales, the average annual bill for water being £89 per household, the equivalent of 24p per day. In real terms, the price of water for household customers has fallen by 11.4% over the last 13 years. This compares with a real increase of 12% for the industry as a whole, as illustrated in the chart below, where the 1996/97 prices are indexed at 100:

Comparison of Average Household Bills with Average Industry Tariffs



The water industry is subject to a range of UK and EU legislation. Standards, particularly those relating to the environment, are being tightened on a regular basis and require increasing levels of investment. The standards of service provided by Portsmouth Water are monitored by three main regulators - the Water Services Regulation Authority (Ofwat) for setting prices and to ensure value for customers, the Environment Agency (EA) for environmental protection and the Drinking Water Inspectorate (DWI) for drinking water quality. Customers are represented by the Consumer Council for Water (CCW), which monitors the quality of service provided by the Company. Portsmouth Water works closely with these and other organisations interested in the services it provides.

Ofwat is the water industry's economic regulator, and its principal duties are exercised through the price-setting process. Ofwat sets price limits for Portsmouth Water every five years. The last determination of prices was in November 2009 for the period 2010 to 2015. The price setting process is known as the Periodic Review and involves a series of consultations between water companies, Ofwat and the other regulators over a two year period. The review examines all aspects of the business and requires the Company to submit a detailed Business Plan to Ofwat. Water companies are allowed to increase prices to customers annually by inflation (RPI) plus or minus the price limit set by Ofwat. The price limits reflect the revenue, which the regulator believes an efficient company needs in order to finance its operations and capital programme, after making an assessment of potential future efficiency gains.

Portsmouth Water is recognised as one of the most efficient water companies in England and Wales (Source - Water and Sewerage Service Unit Costs and Relative Efficiency 2008/09 Report - published by Ofwat), and this has benefited customers through lower bills over many years, as shown above.

Over the last twenty years, the Company has experienced falling demand for water, particularly from commercial customers. The future, however, is expected to see rising demand from domestic customers, with a significant house building programme planned in the Company's area of supply. A twenty five year Water Resources Plan is also produced at each Periodic Review which now has to be approved by the Secretary of State before it can be published. The plan is reviewed annually and enables the Company to balance supplies with forecast demand even at times of dry conditions. A Draft Water Resources Management Plan looking at required resources through to 2035 was published for consultation in April 2008. Representations on the Plan were received from a number of interested parties and, in January 2009, the Company published its response to these representations. In August 2009 the Secretary of State decided that the Plan needed to be subject to a Public Hearing. After reviewing the evidence the Planning Inspector decided that a Public Inquiry was required.

The Company is committed to sustainable development. It must balance the provision of water supply with the needs of the environment and play a part in ensuring that the UK complies with European and National environmental legislation.

BUSINESS STRATEGY

Mission Statement
'We aim to supply drinking water of the highest quality, providing high levels of customer service and excellent value for money'

The Company has a well developed, focused strategy which will meet the demands of all its stakeholders. In 2007 the Company Strategy was made available to customers in our Strategic Direction Statement titled "Sustainable Water Supplies for the future". This document formed the basis of the Company Business Plan, submitted to Ofwat as part of the Periodic Review. The key objectives are:

– To maintain services to customers at the highest level
– To balance the provision of water supply with the needs of the environment
– To maintain the health and welfare of employees
– To ensure that customers continue to enjoy secure and reliable water supplies
– To meet present and future water quality obligations
– To maintain its leadership position at the water industry efficiency frontier
– To maintain the ability to finance its function

The strategy will be achieved by focusing on four key issues:

– Having a well developed and frequently updated long term water resources plan, which will meet the needs of the customer, through secure water supplies, whilst respecting the environment
– Putting customers at the heart of everything we do, and ensuring that they continue to receive excellent value for money
– Setting goals for efficiency which outperform regulatory targets
– Maintaining a motivated workforce, whilst ensuring that the health and safety of employees is given the highest priority

The progress of the Company is measured by a number of key performance indicators (KPI) and these are highlighted in the following section of the Review.

CURRENT DEVELOPMENT AND PERFORMANCE

Financial Performance

The commentary below relates to the historic cost accounts and includes the non-appointed business.

Profit before tax

Turnover for the year increased by 5.5% to £37.3m. This reflected the 4.0% overall tariff increase implemented in July 2009 and £0.5m of income for undertaking a mains diversion. As a result of this historic cost operating profit increased by 19.2% to £8.2m as analysed below:

	2009/10 £m	2008/09 £m
Operating profit before depreciation and FRS17	17.5	16.3
Depreciation (including renewals)	7.9	7.7
FRS17 Pension Charge	1.4	1.7
Total Operating Profit	**8.2**	**6.9**

Operating costs, excluding depreciation and the FRS17 pension charge rose by £0.7m (3.7%), including an increase in electricity costs of £0.3m which reflected the full year effect from an increase in price as a result of the new electricity contract which took effect from November 2008. The current service cost for the pension scheme reduced by £0.3m to £1.4m following a review by the Actuaries in accordance with FRS 17. The Company did not make any contributions to the scheme.

Interest receivable at £1.4m (2009 - £4.5m) relates mainly to interest received from group companies and is based on Libor plus 1%. A reduction in other finance income of £1.0m represents a fall in the expected return on Pension Fund assets following a review by the actuaries in accordance with FRS 17.

Interest payable at £1.9m (2009 - £7.3m) includes £1.2m negative indexation of the loan provided by Artesian Finance plc (2009 - positive £4.0m). The indexation of the loan for 2010 was based on a fall in RPI for July 2009 of 0.4%, whereas, RPI for July 2008 was +5.0%. Interest on the capital sum amounted to £2.9m (2009 - £3.0m).

As a result of the higher turnover and lower interest costs, profit before tax increased to £8.5m (2009 - £5.8m).

Taxation

The taxation charge at £3.0m was £1.3m higher than last year as result of the higher profit and higher deferred tax, together with the effect of a refund received in the previous year.

Dividends

The dividends paid during the year amounted to £4.663m (2009 - £4.664m). Dividends are paid up to the parent company and largely used to service debt held by the group.

Cashflow and Balance Sheet

Net cashflow from operations at £16.6m (2009 - £16.7m) was unchanged from the previous year despite the increase in operating profit, largely as a result of the mains diversion work undertaken but not billed by the year end. Net cash outlay on fixed assets at £12.4m (2009 - £10.6m) reflected further progress on the mains renewal programme (£7.0m) and completion of the AMP 4 Quality programme. The mains renewal expenditure included replacement of a large raw water main at £0.9m.

Net debt at £84.5m (2009 - £82.9m) increased during the year as a result of the relatively large capital programme. At the year end, net debt to regulatory capital value (RCV) was 77.0% (2009 – 77.4%). The ratio for 2010 reflects the RCV arising from the 2009 final determination.

Interest Rate, Liquidity, Capital and Credit Risk

The major financial risks faced by the Company are interest rate, liquidity, capital and credit risks. The Company assesses these risks on an ongoing basis and its policies for managing them remain unchanged from previous periods.

The Company’s exposure to interest rate fluctuations is now limited by the fixed interest rate applicable to the index-linked loan drawn in 2002, with inflation risks on the cost of the loan being effectively hedged against regulated revenues which are also linked to the RPI. Interest is charged at a fixed rate of 3.635% on the indexed amount of the loan. The indexed value of the loan at 31 March 2010 was £81.4m (2009 - £82.6m).

The Company seeks to manage financial risk, to ensure sufficient liquidity is available to meet foreseeable needs through an appropriate borrowing structure and to invest cash assets safely and profitably on the short term market. In 2009/10 all of the short term cash was deposited with the Company’s Bankers, RBS. Short term liquidity is achieved through a £15m working capital facility and an overdraft arrangement. At the end of the year, £6.0m of this facility had been drawn (2009 - £4.0m), while the overdraft arrangement remained unutilised. The £15m facility terminates in March 2011 but the Company has had approval from its Bankers for a three year £10m facility to take effect from April 2011.

The Company’s objectives when managing capital are to safeguard the entity’s ability to continue as a going concern, so it can provide returns for shareholders and benefit to customers.

The capital structure is set at a level which provides an appropriate risk profile to ensure the Company can obtain finance at competitive levels. As is common in the water industry the Company monitors capital in the ratio of debt to Regulatory Capital Value (RCV). RCV is a measure of the Company's asset value used in the setting of prices in the water industry. The level of RCV is published by the regulator (Ofwat) on an annual basis. The ratio achieved for 2009/10 is shown below, and the details of the calculation are shown on page 43.

The Company's exposure to credit risk results from the continuing impact of bad debt on its ability to collect water revenues. It seeks to minimise this risk by utilising all available means, including the use of a dedicated debt recovery section, agencies for collecting outstanding debt and the following of best practice guidelines.

Accounting Policies

The accounts have been prepared in accordance with the accounting policies described in note 1 to the accounts on pages 16 to 18 and with UK GAAP.

Under its licence of appointment, Portsmouth Water Limited, a private company, is required to publish information about its annual results as if it were a company covered by the Listing Rules of the Financial Services Authority. From April 2005, listed groups are required to prepare accounts in accordance with International Financial Reporting Standards (IFRS). It is the Company's view that these standards are not appropriate for a regulated water business and it has been granted exemption, by Ofwat, such that it need only adopt IFRS when non-listed companies are required by statute to do so.

Pensions

The Company accounts for the Brockhampton Pension Scheme in which it is the principal employer, in accordance with FRS17. The latest actuarial valuation carried out for the purposes of FRS17 showed a surplus after deferred tax of £9.8m (2009 - £12.2m).

Key Financial Performance Indicators

Gearing (net debt/regulatory capital value) and cash interest cover are recognised as key indicators for the Company. Performance in 2010 against the target ratios is shown in the table below.

KPI - 1[1]	**Target**	**Performance 2009/10**	**Performance 2008/09**
Gearing - Debt/RCV[2]	<83%	77.0%	77.4%
Cash interest cover[2]	>1.5	1.72	1.66

[1] Each KPI is defined in the Appendix on pages 43 to 44
[2] Definition of terms is contained in the Appendix on pages 43 to 44

Customer Service

The Company measures its services to customers in three key areas:

– The Overall Performance Assessment provided by Ofwat
– The DG indicators provided by Ofwat
– Drinking Water Quality

KPI - 2 The Overall Performance Assessment

Target	**Performance 2008/09**	**Performance 2007/08**
To be in the upper quartile of performance for all water companies	Placed equal 5th out of 22 companies	Placed 11th out of 22 companies

The Overall Performance Assessment for 2009/10 will be published by Ofwat after the Report and Accounts have been completed and therefore the performance shown above is for 2008/09.

KPI - 3 DG Service Indicators

The DG service indicators data shown below is as recorded by the Company for 2009/10 and will be reported to Ofwat in the annual regulatory June Return.

DG Service Indicator	**Target**	**Performance 2009/10**	**Performance 2008/09**
DG2 No. of properties at risk of inadequate pressure	≤ 120	66	66
DG3 Unplanned interruptions to supply	≤ 0.3	0.02	0.05
DG4 Population subject to hosepipe bans	Nil	Nil	Nil
DG6 Billing contacts - answered within 5 days	100%	100%	100%
DG7 Written complaints - answered within 10 days	100%	100%	99%
DG8 Bills for metered customers - no. receiving bill based on meter reading	100%	100%	100%
DG9 Telephone contact - no. of calls abandoned	≤ 2.5%	2.9%	2.8%
- all lines busy	≤ 0.7%	0.1%	0.4%

The Ofwat assessments for 2009/10 will not be published until September, but the results recorded by the Company meet the criteria for being assessed as good.

KPI - 4 Water Quality

The Company carries out an exhaustive programme of testing to ensure that water of the highest quality is supplied to customers. The table below shows the percentage number of samples which pass the strict standards set out in the Water Supply (Water Quality) Regulations.

Water Quality	**Target**	**Performance 2009**	**Performance 2008**
Compliance samples passing standards	99.95%	99.98%	99.97%

The water quality performance indicator relates to the calendar year.

Operating Efficiency

Ofwat publishes a report each year which includes its assessment of the comparative operating efficiency of all water companies in England and Wales using econometric modelling. Companies are put in bands A to E according to their performance for operating efficiency, A being the top band. The latest report published is for the financial year 2008/09, which showed that Portsmouth Water was assessed as the second highest performing company. In the medium term this benefits customers through relatively lower prices and the Company intends to maintain its position in the efficiency rankings.

KPI - 5 Efficiency

Target	**Performance 2008/09**
To be ranked in Band A for Operating Efficiency	Operating Efficiency Band A

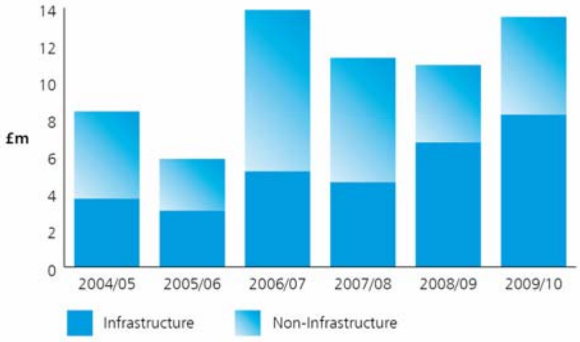
Capital Investment

The Company made good progress with the five year capital programme agreed with the Regulator for the period 2005 to 2010. Details of progress are shown in the table below:

Capital Programme Agreed	**Outcome**
Infrastructure Assets	
– Renewal of 25km of mains each year	Since April 2005, the Company has renewed an average of 24.5km per year
Water Quality	
Installation of membrane filtration plants to minimise the risk of cryptosporidium at	
– River Itchen	Completed Summer 2007
– Soberton	Completed 2008
– Fishbourne	Completed 2008
Remedial work on trunk mains in the Company's largest supply area to reduce the risk of discoloured water incidents	Completed Spring 2009
The installation of blending facilities at sources at risk from increasing nitrate levels	Completed 2010
Optional Water Meters	
It was anticipated that 2,200 domestic customers would wish to switch from an unmeasured to a measured supply	In the 5 years to March 2010, over 23,000 customers had opted to switch, an average of 4,700 per year

Gross capital investment during the year was £14.1m (2009 - £11.8m) and included £7.0m (2009 - £5.2m) on infrastructure renewals. After receiving capital contributions and infrastructure charges of £0.6m, net capital expenditure was £13.5m (2009 - £10.9m). The chart below shows the level of net capital investment over a six year period in outturn prices.

Net Capital Expenditure



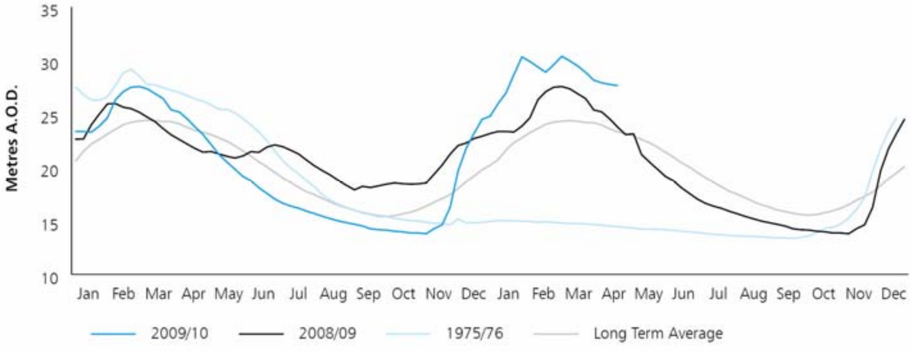
The major elements of expenditure in the year related to:

- Mains renewed – 23.7km (2009 – 24.9km) were renewed at a cost of £6.1m. In addition a large raw water main was renewed at a cost of £0.9m.
- Membrane plants - now in service. Limited expenditure during the year
- Nitrate Blending Schemes - was completed in 2010, expenditure in 2009/10 of £1.8m
- Havant Thicket Winter Storage Reservoir – the Company has made good progress with the preparatory work for a winter storage reservoir at Havant Thicket, which should help ensure security of water supplies well into the future. A stakeholder group consisting of interested local bodies and interested parties is well established and we believe that there is strong local support. In order to obtain planning permission for this scheme, considerable environmental studies and Public Consultation has to be undertaken, which requires a range of design options and impact assessments. In 2009/10 this work resulted in expenditure of £0.5m.

Water Resources - Outlook for 2010

As detailed on page 1, 87% of water supplied to customers is from groundwater springs, boreholes and wells which abstract from the underground chalk of the South Downs. Groundwater levels are therefore critical to maintaining supplies to customers. The Company has for many years monitored the groundwater level at Idsworth Well, Rowlands Castle, which is unaffected by abstraction and is representative of groundwater conditions in the South Downs chalk.
At the end of April 2010, groundwater levels were above the long term average as outlined on the two year graph below, which includes the thirty year long term average and the drought year of 1976, when the Company last imposed a hosepipe ban.

Idsworth Well



Water resources are therefore expected to be sufficient to meet peak demands in the summer of 2010 and a hosepipe ban is not expected in our area of supply. However, the Company has used its newsletter, website and press releases to stress to customers the need to be conservative in their use of water.

Long Term Resource Planning

In April 2008, the Company published its Draft Water Resources Management Plan (DWRMP) for Public Consultation. The plan examined the likely key influences on the demand for water from customers and on the Company's ability to meet that demand. The plan also identified the actions required to ensure that the supply/demand balance is met, which included the construction of a winter storage reservoir at Havant Thicket, close to the Company's head office, which would be scheduled to come into service in 2022. As noted above preliminary work on the reservoir including environmental assessments has already begun. Following representation from stakeholders, the Company has revised its plans and informed the Secretary of State of its proposed actions. In August 2009 the Secretary of State announced that certain issues raised in the plan should be subject to a Public Hearing under the auspices of the Planning Inspectorate. After reviewing all the evidence submitted for the Hearing, the Inspector appointed has decided that the evidence should be reviewed in a Public Inquiry, which is more formal and allows challenge to the representations. The Inquiry is unlikely to be held before September 2010.

Until the outcome of the Public Inquiry is known there is uncertainty as to when the Havant Thicket reservoir would be required, and a long delay would likely mean that much of the environmental work carried out to date and held in Fixed Assets would have to be revalidated at a later date. Details of the expenditure to date is shown in note 10 to the accounts on page 22.

Leakage

Leakage for the year was recorded at an average of 28.7Ml/d. The leakage targets were set out in the Company's Business Plan for the last Periodic Review and agreed by Ofwat as part of the Final Determination in 2004.

KPI - 6 Leakage

Target	Performance 2009/10
Average leakage of 29.7 Ml/d	Average leakage of 28.7 Mld

Employees

The Company employs 226 people and believes it recruits and retains the right people key to the successful performance of the business.

The Company is firmly committed to the development of its employees and that they should all have opportunities to reach their full potential and, as a result, a number during the year have undertaken Degrees, HNC's, NVQ's along with associated professional qualifications.

In line with this objective the Company fully supports the principle of Modern Apprenticeships for example, all new employees within the Customer Services department aged under 25 are employed through the Modern Apprenticeship scheme which leads to a minimum NVQ level 2 qualification with many going on to achieve level 3.

A key part of staff development is the Company involvement with the Institute of Water. The Institute of Water is a professional body whose purpose is to promote the advancement of knowledge within the water industry. To this end, Area and National Committees organise meetings, seminars, technical visits and conferences, as well as a variety of social events. These activities provide a shop window for the latest technological developments in the industry and a forum for the discussion of major topics. The Company encourages its staff to belong to the IoW and gain the benefit for both their personal and professional development by attending these events.

One of our employees, Steve Youell, recently won the Continuing Professional Development (CPD) Award for 2010. The CPD award is given to an employee in the water industry who has demonstrated an effective approach to their own personal development.

Staff turnover, excluding retirees was 6.8% in the calendar year 2009 (2008 – 7.5%), which compares favourably with the national average which was 7.7% in 2009 (Source CIPD: Annual Survey Report 2009).

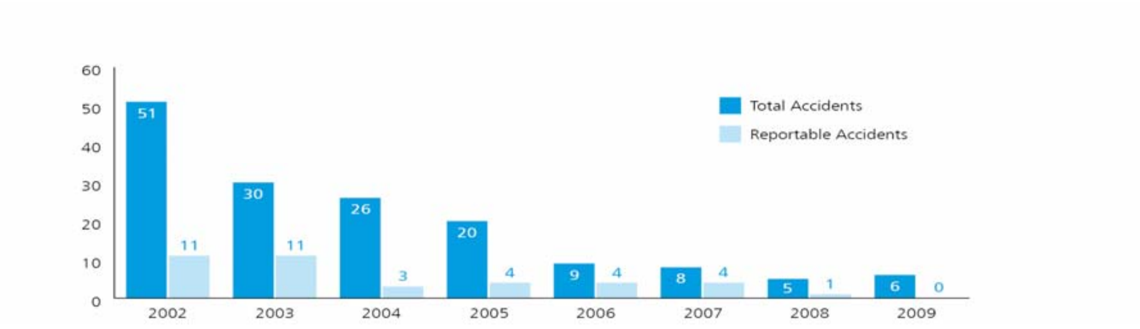
Total absence (days per employee per year) was 4.9. This figure compares with 4.1 for last year and is below the average for private companies of the same size at 7.4 (Source: CIPD: Annual Survey Report 2009).

Health and Safety

Health and safety of employees is considered fundamental to the success of the business and the Company is committed to achieving high standards across the organisation. The Company has put health and safety at the top of the agenda and from the Board down has made it a high priority.

Considerable time and resources have continued to be directed into raising the awareness of Health and Safety and the statistical results for the year 2009 show very positive results from these efforts, with no reportable accidents being recorded.

Total Accidents and Reportable Accidents



It is pleasing to report that our efforts have again been recognised externally through the RoSPA Health and Safety Awards, by the Company being awarded the Gold Medal. This is in recognition of our Health and Safety record over the last five years where we have received five Gold awards and an Industry sector award. This award is again recognition of the efforts of all employees who should feel proud of their achievements in making the Company a safer place.

CORPORATE RESPONSIBILITY

Environmental Performance

The Company recognises its impact on the environment and seeks to carry out its activities in a sustainable manner, which is highlighted by the initiatives shown below.

Conservation

The Company's total licensed area of supply covers an attractive part of Southern England between the South Downs and the coastal areas of Hampshire and West Sussex. It includes the historic cities of Portsmouth and Chichester, and the popular holiday resorts of Bognor Regis, Selsey and Hayling Island. The harbours of Portsmouth, Langstone, Chichester and Pagham have a number of important environmental designations under the EU Habitats Directive and are popular water activity venues.

Biodiversity Action Plan

The Company's policy is to conserve and enhance the natural environment of its land and water areas and to preserve historic buildings and equipment, so far as is consistent with the primary duty of providing a sufficient supply of wholesome water at reasonable cost. Where possible, the Company explores opportunities to encourage recreational use.

Sustainable Procurement

In procuring goods and services, the Company has a policy which seeks to ensure that its impact on the environment is minimised. This includes the use of low sulphur content diesel fuel, timber from replanted forests and predominantly recycled material for reinstatement.

Water Efficiency

The Company has continued, through various channels of communication such as its newsletter and website, to promote the need for the efficient use of water, both by domestic and commercial customers. Specific initiatives have included:

Cistern Devices

Approximately 11,800 'Save-a-Flush' bags were issued to customers during the year.

Measured Customers

All new properties are charged on the basis of a metered supply and all customers opting to install a meter received a leaflet, 'Saving Water at Home,' to ensure that customers most likely to benefit from water efficiency are reminded of the advantages, and each customer receives two 'Save-a-Flush' bags.

Commercial Water Audits

A leaflet entitled 'Saving Water in Your Business' is included on the Company website.

In-House Efficiency Study

A series of initiatives at the Company's Head Office has resulted in an overall saving since 2004 of 50% of previous water usage.

Work in the Community

Amenities and Recreation

In September 2004 Portsmouth Water entered into Educational Partnership with Staunton Country Park. This partnership has seen the creation of a curriculum linked water themed programme, 'Water is Life', suitable for primary school children. The 'Water is Life' programmes cover all aspects of water from its role in the planet, the water cycle as well as the treatment and supply process. A key element of water conservation underpins the whole programme.

Drinking Water Bottles

The Company has continued to promote the benefits to children of drinking water and as part of our 'Water for Health' initiative we have offered a drinking water bottle at the subsidised cost of 30p per bottle for every child in local primary, infant and junior schools.

The Water Bottles for Schools offer has gone from strength to strength with 30,000 delivered last year and which has seen nearly 230,000 water bottles through the schools being delivered to our local children.

Community Talks

Employees continue to give community talks to local schools, colleges, clubs and groups such as Age Concern, Rotary and the Women's Institute. To cope with the increasing demand for talks, a community talk team has been set up with volunteers from the Company.

Festivals and Fairs

The Company once again sponsored the Primary Schools Science Fair which is promoted by the Portsmouth and South East Hampshire Business and Education partnership. The three-day event held within the historic Dockyard utilising the HMS Warrior and Action Stations to house the exhibitor's stands saw over 1,200 children from local schools visiting the exhibits.

The Company's demonstrations this year included water treatment and how different filters work, the sampling process, and finished off with a short session on the need for all of us to conserve water.

Hampshire Water Festival

The Company played a key role in organising this festival which was held at Staunton Country Park in July 2009. The event which was attended by 15,000 visitors promoted the efficient use of water in the home.

FUTURE DEVELOPMENT AND PERFORMANCE

Cautionary statement regarding forward-looking statements

This section should be read in conjunction with the financial statements and notes thereto included elsewhere in this Annual Report. This Annual Report contains certain forward-looking statements with respect to the financial condition, results of operation and business of Portsmouth Water.

Statements that are not historical facts, including statements about Portsmouth Water's beliefs and expectations, are forward-looking statements. Words such as 'believes', 'anticipates', 'expects', 'intends', 'seeks' and 'plans' and similar expressions are intended to identify forward-looking statements, but are not the exclusive means of identifying such statements. These statements are based on current plans, estimates and projections and, therefore, undue reliance should not be placed on them. Forward-looking statements speak only as of the date they are made, and it should not be assumed that they have been revised or updated in the light of new information or future events.

Performance through the 5 years to 2015
The period from April 2010 to March 2015 is referred to in the Industry as the Asset Management Plan 5 (AMP5)

The Company will continue to focus on service delivery to customers and will aim to remain at the efficiency frontier for operating and capital maintenance expenditure.

Financial performance will be driven by the price limits set by the regulator Ofwat in November 2009, which for the five year period to 2015, are as follows:

	2010/11	2011/12	2012/13	2013/14	2014/15
% (reduction) in bills before inflation	(4.8)	(2.1)	(1.7)	(1.4)	(0.6)

Each year customer bills are adjusted by the previous November's RPI plus the above limit therefore, given that RPI for November 2009 was 0.3%, for 2010/11 charges to customers will reduce by 4.5%.

Energy costs represent over 12% of total costs and given the volatility of prices in recent years is a significant risk to the Company. The current electricity contract terminates in October 2011, but the Company has fixed the wholesale price from this date through to December 2014 at rates considerably less than the current contract and less than that allowed by Ofwat at the 2009 price determination.

Gross capital expenditure in AMP5 will be £40m (2009/10 prices), with mains renewals contributing approximately 50% of the total. This compares to £58m (2009/10 prices) for AMP4.

RISKS AND UNCERTAINTIES

The Company identifies risks under six main headings - Operational, Water Quality, Financial, Environmental, Regulatory and Health and Safety of Employees. Individual risks facing the Company are identified and recorded in a risk register. For each risk the consequences, impact and likelihood of failure are identified, together with the management controls in place. The register also clearly allocates management responsibility and whether any further actions are required to control the risks.

The Board reviews the risk register and the controls established to mitigate these risks on an annual basis. It also receives regular reports on operational matters, including a monthly review of water quality matters directly with the Water Quality Manager and a quarterly review of health and safety matters with the Personnel and Safety Manager. The Directors also receive reports from independent regulatory bodies, which comment on the performance of the core water business.

The Audit Committee meets at least three times a year, monitors the effectiveness of the systems which are in place and reports to the Board as a whole.

The key operational risks facing the Company are the loss of a treatment works or part of the mains network, which would result in a failure to supply water to customers. To mitigate this risk, the supply network has been enhanced over several years to connect different supply areas, such that in most situations water can be transferred to compensate for a failure at a treatment works. The Company also has a fully documented Emergency Plan which is initiated in the event of an incident, impacting either its ability to supply water to the public or resulting in a water quality issue.

To ensure water quality standards are maintained, the Company has a fully documented Drinking Water Safety Plan which identifies the potential risks throughout the supply process. Water quality is also monitored by a comprehensive sampling regime in accordance with DWI standards. Furthermore, a telemetry system linked to all treatment works provides an alarm if there is a failure of equipment. The Company also maintains two days' storage of treated water in service reservoirs to provide sufficient time for any water quality issues at treatment works to be rectified before supply to customers. In addition, it has membrane filtration at five treatment works considered most at risk from cryptosporidium being present in the raw water.

The risk of financial loss is addressed through comprehensive insurance cover for a range of risks, including damage to property, public and employee liability, fraud and terrorism. A system of internal controls is in place to manage the risks. In early 2007, the Auditors conducted a special review of the Company's internal control systems. The review did not reveal any significant weaknesses and has recently been updated to reflect system changes. A disaster recovery plan is also in place to enable the Company to operate in the event of an incident disrupting its computer systems. At a remote site ten miles from its Head Office, the Company has an additional mainframe computer, which is 'backed up' every evening, and several workstations for employees to operate.

The major environmental risk faced by the Company at the present time is a potential loss of abstraction licence resulting from measures that may be required by the EA to allow the UK to comply with the Water Framework Directive. Over the next few years the Company will be undertaking a study to identify the impact of its abstraction at key points and to identify solutions where required.

The flooding in various parts of the UK during the summer of 2007 has prompted several national reports. Whilst the Company was not affected in 2007, it has conducted an assessment of the risks at each of its sites and included a small amount of expenditure which was allowed in the Final Determination of prices to remedy those sites where there is a risk of damage as a result of flooding.

Regulatory risk relates to decisions taken by Ofwat at the five yearly price review and the potential failure to meet the level of service and capital programme agreed with Ofwat for the AMP 5 period, which could result in Ofwat taking action, including financial penalties. The price review is conducted in an open and transparent manner and the Company actively participates in the process. The performance against the regulatory targets is reviewed on a monthly basis by the Board or the Executive Directors. The annual performance against the targets is discussed on pages 4 to 5.

The health and safety of employees is taken very seriously and a number of initiatives have been introduced over several years to reduce the number of accidents and the impact of injury.

These include:

– A Health and Safety Committee comprising Management and the Trade Unions
– A risk assessment programme that has seen over 500 assessments produced
– A system of workplace inspection ensuring that all manned premises are inspected at least twice per year
– Specific training for those at high risk of injury
– A limited free physiotherapy service for employees to deal with injuries

N J Roadnight	**N Smith**
Managing Director	**Finance & Regulation Director**

23 June 2010

This report has been prepared in accordance with the requirements of the Companies Act 2006 and the Listing Rules of the Financial Services Authority.

INFORMATION NOT SUBJECT TO AUDIT

Remuneration Committee

The Remuneration Committee met three times during the year to consider and approve, on behalf of the Board, the conditions of service of the executive Directors of the Company. It comprises the three independent non-executive Directors, Mr. R. L. Sullivan (Chairman of the Remuneration Committee), Mr. T. M. Lazenby MBE and Mr. R. J. Tennant.

The Level and Make-up of Remuneration

The objective is to attract, retain and motivate high calibre senior executives through pay arrangements which are competitive and fair and reasonable for the responsibilities involved. In addition to individual performance, reference is made to pay levels in companies of similar size and within the same industry.

The remuneration package of the executive Directors, as reported in the accounts, did include a performance related element. The salary of the executive Directors includes a performance related element, which is based upon the achievement of agreed financial, customer service and personal targets for the whole of the previous year.

The executive Directors have one year service contracts with the Company, which are in accordance with the Combined Code on Corporate Governance. None of the executive Directors serves as a non-executive Director for another company. The non-executive Directors do not have service contracts.

The service contracts of the executive Directors include notice periods of one year, both by the Company and by the Director. There are no provisions for termination payments, other than payments for the period of notice.

Fees payable to the non-executive Directors are determined by the Board as a whole and reflect the time, commitment and responsibilities of the role.

No Director is involved in deciding his own remuneration.

INFORMATION SUBJECT TO AUDIT

Directors' remuneration:	**2010**	2009
	£000	£000
Total remuneration	**531**	578
Highest paid Director	**162**	160

Remuneration is analysed by Director below:

	Salary/Fees	Benefits	**Total 2010**	Total 2009
	£000	£000	**£000**	£000
Executive:				
J E Cogley	43	9	**52**	114
A R Neve	105	12	**117**	111
N J Roadnight	144	18	**162**	160
N Smith	114	15	**129**	122
Non-executive:				
T M Lazenby MBE (Chairman)	31	-	**31**	31
R L Sullivan	20	-	**20**	20
R J Tennant	20	-	**20**	20
	477	54	**531**	578

During the year Mr N Smith and Mr A R Neve received bonus payments of £6,000 and £3,000 respectively. This is included in salary/fees above.

Fees paid in respect of Mr T M Lazenby MBE are paid to Seamab Consultancy Limited.
Benefits comprise company cars and medical insurance.
Mr J E Cogley left service on the 31 August 2009.

Long-term incentive schemes

The Company does not operate any long-term performance linked bonus scheme.

Share options

The Company does not operate an Executive Share Option Scheme.
The Directors' beneficial holdings of shares in South Downs Capital Limited, the ultimate parent undertaking, are detailed below and, in total, represent 15% of the issued share capital of that Company. They have no interests in the shares of Portsmouth Water Limited.

	'C' Ordinary Shares
A R Neve	30
N J Roadnight	55
N Smith	45

Mr J E Cogley left service during the year but continues to have a beneficial holding of 20 shares in South Downs Capital Limited.

Pensions

The Company participates in the Brockhampton Pension Scheme to provide defined benefits based primarily on final pensionable pay for its employees, including the executive Directors. The maximum pension payable under this Scheme is 2/3 of final pensionable pay.

Benefits in kind relating to company cars are considered to be part of pensionable pay for all employees under the Scheme.

The executive Directors have accrued pension benefits under the Brockhampton Pension Scheme, which is a defined benefits scheme, during the year as detailed below:

	Increase in Accrued Pension During Year to 31 March 2010 £000	Transfer Value of Increase £000	Accumulated Accrued Pension at 31 March 2010 £000	Accumulated Accrued Pension at 31 March 2009 £000
J E Cogley[1]	1	19	69	68
A R Neve	5	124	74	69
N J Roadnight	4	91	97	93
N Smith	5	95	61	56

The accumulated accrued pension is the leaving service benefit to which the Director would be entitled to if he were to leave service at the end of the year. It includes any benefits earned as an employee prior to becoming a Director, as well as those earned for qualifying services after becoming a Director.

The increase in accrued pension excludes any increase for inflation, although inflation over the year was negative so the full increase in accrued pension has been shown.

The transfer value has been calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11. The transfer value of the increase (excluding inflation) is then reduced by the amount of each member's contribution paid during the year.

[1]Mr J E Cogley left service on the 31 August 2009 and therefore his leaving service benefit is his entitled benefit using his actual date of leaving.

By order of the Board

T M Lazenby MBE
Chairman
Havant
23 June 2010

HISTORICAL COST PROFIT AND LOSS ACCOUNT

For the year ended 31 March 2010

	Notes	Appointed 2010 £000	Non Appointed 2010 £000	Total 2010 £000	Appointed 2009 £000	Non Appointed 2009 £000	Total 2009 £000
TURNOVER	2	37,306	36	37,342	35,384	20	35,404
Operating costs	3	(25,743)	(22)	(25,765)	(25,188)	(19)	(25,207)
Historical cost depreciation		(3,329)	-	(3,329)	(3,264)	-	(3,264)
Operating income	4	(22)	-	(22)	(37)	-	(37)
OPERATING PROFIT		8,212	14	8,226	6,895	1	6,896
Other income	5	-	64	64	-	56	56
Interest receivable	6	1,405	-	1,405	4,537	-	4,537
Other finance income	20	714	-	714	1,676	-	1,676
Interest payable and similar charges	7	(1,944)	-	(1,944)	(7,351)	-	(7,351)
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION		8,387	78	8,465	5,757	57	5,814
Taxation	8						
- Current Tax		(2,077)	(22)	(2,099)	(892)	(16)	(908)
- Deferred Tax		(944)	-	(944)	(775)	-	(775)
PROFIT FOR THE FINANCIAL YEAR		5,366	56	5,422	4,090	41	4,131
Dividends	9	(4,607)	(56)	(4,663)	(4,623)	(41)	(4,664)
RETAINED PROFIT/(LOSS) FOR THE FINANCIAL YEAR		759	-	759	(533)	-	(533)

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

For the year ended 31 March 2010

	Notes	Appointed 2010 £000	Non Appointed 2010 £000	Total 2010 £000	Appointed 2009 £000	Non Appointed 2009 £000	Total 2009 £000
Profit for the financial year		5,366	56	5,422	4,090	41	4,131
Actuarial (loss) on pension scheme	20	(2,636)	-	(2,636)	(13,020)	-	(13,020)
Deferred tax relating to actuarial loss on Pension scheme	18	738	-	738	3,646	-	3,646
Total recognised gains and losses relating to the year		3,468	56	3,524	(5,284)	41	(5,243)

As at 31 March 2010

	Notes	Appointed 2010 £000	Non Appointed 2010 £000	Total 2010 £000	Appointed 2009 £000	Non Appointed 2009 £000	Total 2009 £000
FIXED ASSETS							
Tangible	10	91,234	-	91,234	88,068	-	88,068
Investments							
- Loan to group company	11	59,468	-	59,468	60,633	-	60,633
- Other	13	4	-	4	4	-	4
		150,706	-	150,706	148,705	-	148,705
CURRENT ASSETS							
Stores		553	-	553	415	-	415
Debtors	12	4,935	-	4,935	4,032	-	4,032
Cash and short-term deposits	14	1,931	-	1,931	2,604	-	2,604
Infrastructure renewals prepayment		3,324	-	3,324	919	-	919
		10,743	-	10,743	7,970	-	7,970
CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR							
Borrowings	15	(6,284)	-	(6,284)	(4,284)	-	(4,284)
Corporation tax payable		(742)	-	(742)	-	-	-
Unpaid dividend		(1,875)	-	(1,875)	(1,875)	-	(1,875)
Creditors	16	(11,646)	-	(11,646)	(10,895)	-	(10,895)
NET CURRENT LIABILITIES		(9,804)	-	(9,804)	(9,084)	-	(9,084)
TOTAL ASSETS LESS CURRENT LIABILITIES		140,902	-	140,902	139,621	-	139,621
CREDITORS: AMOUNTS FALLING DUE AFTER ONE YEAR							
Borrowings	17	(80,136)	-	(80,136)	(81,263)	-	(81,263)
PROVISIONS FOR LIABILITIES							
Deferred Taxation	18	(10,272)	-	(10,272)	(9,131)	-	(9,131)
NET ASSETS EXCLUDING PENSION ASSET		50,494	-	50,494	49,227	-	49,227
Pension asset	20	9,774	-	9,774	12,180	-	12,180
NET ASSETS INCLUDING PENSION ASSET		60,268	-	60,268	61,407	-	61,407
CAPITAL AND RESERVES							
Called up share capital		1,078	-	1,078	1,078	-	1,078
Share premium account	19	1,539	-	1,539	1,539	-	1,539
Capital redemption reserve	19	3,250	-	3,250	3,250	-	3,250
Profit and loss account	19	54,401	-	54,401	55,540	-	55,540
		60,268	-	60,268	61,407	-	61,407

For the year ended 31 March 2010

	Statutory UK GAAP £m	Regulatory £m	Commentaries
PROFIT AND LOSS ACCOUNT			
Operating profit	8,312	8,226	See a) below
BALANCE SHEET			
Tangible fixed assets (net book value)	96,030	91,234	See b) below

a) The difference relates to the way these figures have been presented in both sets of accounts. In the Statutory Accounts, this figure excludes the (£0.022m) for loss on sale of fixed assets as it is reported below the operating profit line in the profit and loss account, but includes other income of £0.064m. In the Regulatory Accounts the amount shown includes the (£0.022m) for loss on sale of fixed assets but reports the other income below the operating profit line.

b) The difference relates to the different accounting treatments for infrastructure renewals accounting in each set of accounts. In the Statutory Accounts the Company has followed common industry practice and adopted the infrastructure renewals accounting policy as set out in FRS 15. This has not been applied in the Regulatory Accounts, at the request of Ofwat.

1 ACCOUNTING POLICIES

The accounts have been prepared under the historical cost convention and in accordance with applicable United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) and with the provisions of the Companies Act 1985, except for the treatment of capital contributions as detailed in note 1.(c), and the non-application of FRS 15 for infrastructure renewals accounting, as required by Ofwat for the purposes of producing the regulatory accounts.

In view of the licence conditions under which the Company operates as a water supplier, it has to publish information about its annual results as if it were a company covered by the Listing Rules of the Financial Services Authority, except where it is considered inappropriate to do so. Earnings per share disclosures required by FRS 22 are not presented as the Company is a wholly owned subsidiary.

The principal accounting policies which have been applied consistently are as follows:

(a) Turnover

Turnover, which excludes value added tax, represents the income receivable for goods and services provided to external customers in the ordinary course of business. It comprises the value of water supplied and other related charges. Turnover from the regulated water business includes amounts billed for the year, together with an estimation of amounts unbilled at the year end, for measured water customers. Unmeasured income bills are based on the rateable value of properties. Measured income arises from customers who have meters fitted at their premises and amounts billed, therefore, are based on actual water consumption. The estimation of the amounts unbilled at the year end uses a defined methodology based upon a measure of unbilled water consumed, which is calculated from historical customer data.

The Company does not make any provision for revenue recognition in accordance with Note G of FRS5, therefore the revenues reported in these regulatory accounts are identical with those reported in the statutory accounts. Irrecoverable amounts are not provided for, but are written off on an ongoing basis over the course of the year as they are identified.

All properties on the customer database are billed at the commencement of the billing year. Properties which are unoccupied or unfurnished are then written off during the year, following either contact from the customer and/or an inspection of the property carried out by the Company. Normal charges apply to furnished unmetered vacant properties.

A metered customer can request their supply to be temporarily turned off, after which they will not be charged until their supply is restored. Disconnected properties are not charged.

A property which is believed to be occupied, but the occupier's details are not known, is charged once the occupier's details are established.

Cash received from 'charges on income' is not treated as revenue, but is applied to reduce the outstanding debt derived from the turnover recognition policy. When the income was invoiced or accrued, it was recognised in line with the accounting policy.

Revenue from new properties is recognised from the date the meter is installed and the customer details have been obtained. Properties are only added to the billing system, once sufficient details have been obtained.

(b) Fixed assets

(i) Infrastructure assets - mains

Infrastructure assets comprise a network of systems. Expenditure on infrastructure assets relating to increases in capacity or enhancement of the network is treated as an addition and included in tangible fixed assets at cost. Expenditure on maintaining the operating capability of the network is classified as infrastructure renewals expenditure and charged as an operating cost.

No depreciation is charged on infrastructure assets because the network is required to be maintained in perpetuity and therefore has no finite economic life.

(ii) Other assets

Depreciation is provided on all other fixed assets with the exception of freehold land. It is calculated to write off the cost of assets less estimated residual values over their estimated useful economic lives using the straight line method. Those lives are estimated as follows:

Buildings and Reservoirs	100 years
Pumping Plant	15-25 years
Vehicles and Mobile Plant	5-7 years
Office Equipment	7 years

(c) Capital contributions

(i) Mains contributions

In certain circumstances third parties make non-returnable contributions towards the cost of specific infrastructure assets. They are treated as capital contributions and the Directors consider it appropriate that, in order to present a true and fair view, they should be deducted from fixed assets, as shown in note 10 to the accounts on page 22. In accordance with the Companies Act 2006 requirement to include fixed assets at cost, such contributions would normally be treated as deferred income and released to the profit and loss account over the useful life of the corresponding assets. However, the assets to which they relate do not have determinable finite lives and, accordingly, no basis exists on which to recognise those contributions as deferred income.

(ii) Infrastructure charges

Infrastructure charges are made in respect of new connections in accordance with Condition 'C' of the Instrument of Appointment. These charges are treated as capital contributions and deducted from fixed assets, as more fully explained in note 1.(c)(i) above.

(d) Investments

Investments are stated at the lower of cost or net realisable value.

(e) Stocks

Stocks of raw materials are valued at the lower of cost or net realisable value. In accordance with established practice in the water industry, no value is placed upon the water in reservoirs, mains or in the course of treatment.

(f) Deferred taxation

Deferred tax is recognised on all timing differences where the transactions or events that give the Company an obligation to pay more tax in the future, or the right to pay less tax in the future, have occurred by the balance sheet date. Deferred tax assets are recognised when it is more likely than not that they will be recovered. Deferred tax is measured using rates of tax that have been enacted or substantively enacted by the balance sheet date.

The deferred tax balances have been discounted using a post-tax yield to maturity that could be obtained at the balance sheet date on government bonds with maturity dates similar to when the timing differences are expected to reverse.

(g) Leases

All leases are regarded as operating leases. Operating lease payments are charged to the profit and loss account on a straight line basis over the period of the lease.

(h) Pension costs and other post retirement benefits

Portsmouth Water Limited is the principal employer and its parent company, Brockhampton Holdings Limited, is the participating employer in the Brockhampton Pension Scheme. This scheme is a defined benefit scheme. The assets of the scheme are held in a separate trustee administered fund.

The current service costs are charged to the profit and loss account and included as staff employment costs. The interest cost and expected return on assets are shown as a net amount within other finance income. Actuarial gains and losses are recognised immediately in the Statement of Recognised Gains and Losses.

Pension scheme liabilities are measured on an actuarial basis using the projected unit method and are discounted to their present value using the AA corporate bond rate.

Pension scheme assets are valued at market value at the balance sheet date. The pension scheme surplus is recognised in full on the balance sheet.

The deferred tax relating to a defined benefit asset is offset against the defined benefit asset and not included with other deferred tax liabilities.

Detailed information regarding the surplus and actuarial position of the scheme is given in note 20 to the accounts on pages 26 to 28.

(i) Financial instruments

When a financial asset or liability is recognised initially it is measured at its fair value plus or minus transaction costs. The Company subsequently categorises financial instruments as follows:

Fixed asset investments consist of loans to Group undertakings, which earn interest based on London Interbank rates and are classified as loans and receivables. They are measured at amortised cost.

Other financial assets consist of short term bank deposits and debtors and are classified as loans and receivables. They are measured at amortised cost.

The Company’s financial liabilities consist of fixed rate borrowings in the form of perpetual debentures and an index linked loan. These instruments are classified as other liabilities and are measured at amortised cost.

2. TURNOVER

	Appointed 2010 £000	Non Appointed 2010 £000	Total 2010 £000	Appointed 2009 £000	Non Appointed 2009 £000	Total 2009 £000
Unmeasured supplies	22,572	-	22,572	22,242	-	22,242
Measured supplies	10,197	-	10,197	9,438	-	9,438
Measured large users	2,543	-	2,543	2,079	-	2,079
SWS Bulk Supply	518	-	518	518	-	518
Third party services	1,377	36	1,413	982	20	1,002
Other sources	99	-	99	125	-	125
	37,306	36	37,342	35,384	20	35,404

3. ANALYSIS OF OPERATING COSTS

This note has been prepared in accordance with Condition 'F' of the Company's Instrument of Appointment.

	Appointed 2010 £000	Non Appointed 2010 £000	Total 2010 £000	Appointed 2009 £000	Non Appointed 2009 £000	Total 2009 £000
Manpower costs	7,706	18	7,724	7,883	15	7,898
Other costs of employment	296		296	182	-	182
Power	2,281	-	2,281	1,984	-	1,984
Rates	2,475	-	2,475	2,390	-	2,390
Hired and contracted services	3,927		3,927	3,902	-	3,902
Materials and consumables	1,551	4	1,555	1,475	4	1,479
Service charges	1,804	-	1,804	1,865	-	1,865
Infrastructure renewals charge	4,561	-	4,561	4,420	-	4,420
Provision for bad and doubtful debts	630	-	630	589	-	589
Other operating costs	512		512	498	-	498
	25,743	22	25,765	25,188	19	25,207

Other operating costs include payments made to the EOS Foundation, which is a charitable trust used to assist customers in debt. A donation of £25,000 was made in the year (2009 - £25,000).

4. OPERATING INCOME

	Appointed 2010 £000	Non Appointed 2010 £000	Total 2010 £000	Appointed 2009 £000	Non Appointed 2009 £000	Total 2009 £000
(Loss) arising on disposal of fixed assets	(22)	-	(22)	(37)	-	(37)

5. OTHER INCOME

	Appointed 2010 £000	Non Appointed 2010 £000	Total 2010 £000	Appointed 2009 £000	Non Appointed 2009 £000	Total 2009 £000
Rents	-	59	59	-	51	51
Home Assistance Service	-	5	5	-	5	5
	-	64	64	-	56	56

6. INTEREST RECEIVABLE

	2010 £000	2009 £000
Loan to Group Company	1,381	4,303
Repayment interest	-	138
Interest on short term deposits	16	81
Other interest receivable	8	15
	1,405	4,537

7. INTEREST PAYABLE AND SIMILAR CHARGES

		2010 £000	2009 £000
£66.5m loan	- interest	2,937	2,956
	- indexation	(1,184)	3,967
	- amortisation of fees	57	57
	- administration expenses	25	22
		1,835	7,002
Other bank loans and overdraft		94	312
Debenture stocks		10	10
Other interest payable		5	27
		1,944	7,351

8. TAXATION

	2010 £000	2009 £000
Current tax		
United Kingdom corporation tax at 28% (2009 - 28%)	2,102	1,430
Adjustment in respect of prior periods	(3)	(522)
	2,099	908
Deferred tax		
Origination and reversal of timing differences	1,192	644
(Increase)/decrease in discount	(51)	143
Difference between pension cost charge and pension cost relief	(197)	(12)
	944	775
Tax on profit on ordinary activities	3,043	1,683

The adjustment in respect of prior periods relates to a tax refund received following a change in the tax treatment of infrastructure renewals expenditure.

The tax charge for the year is lower (2009 - lower) than the standard rate of corporation tax in the UK of 28% (2009 - 28%). The difference is explained as follows:

	2010 £000	2009 £000
Profit on ordinary activities before tax	8,465	5,814
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 28% (2009 - 28%)	2,370	1,628
Effect of:		
Expenses not deductible for tax purposes 19	23	
Capital allowances for the period in excess depreciation	(608)	(447)
Revenue items charged to capital	124	214
Difference between pension cost charge and pension cost relief	197	12
Adjustments to tax charge in respect of prior periods	(3)	(522)
Current tax charge for year	2,099	908

9. DIVIDENDS

	2010 £000	2009 £000
Equity: Ordinary/'A' Ordinary		
- interim paid	2,050	2,576
- final paid	2,613	2,088
	4,663	4,664

The Directors have approved the payment of a final dividend of £1.885m for the year ended 31 March 2010.

Dividend Policy

The dividends for 2010/11 will be rebalanced, in line with the approach taken by Ofwat in the 2009 Final Determination, to thereafter show dividend growth in real terms of 2.1% per annum.

10. TANGIBLE FIXED ASSETS

	Operational Assets £000	Infrastructure Assets £000	Other Tangible Assets £000	Total £000
HISTORICAL COST				
At 1 April 2009	77,316	43,960	11,862	133,138
Additions	3,939	1,796	1,353	7,088
Disposals	-	-	(486)	(486)
At 31 March 2010	81,255	45,756	12,729	139,740
DEPRECIATION				
At 1 April 2009	18,795	-	7,497	26,292
Charge for year	2,160	-	1,169	3,329
Disposals during year	-	-	(445)	(445)
At 31 March 2010	20,955	-	8,221	29,176
NET BOOK VALUE				
At 31 March 2010	60,300	45,756	4,508	110,564
At 1 April 2009	58,521	43,960	4,365	106,846
CAPITAL CONTRIBUTIONS				
At 1 April 2009	-	18,778	-	18,778
Received during year	-	552	-	552
At 31 March 2010	-	19,330	-	19,330
NET BOOK VALUE AFTER DEDUCTING CAPITAL CONTRIBUTIONS				
At 31 March 2010	60,300	26,426	4,508	91,234
At 1 April 2009	58,521	25,182	4,365	88,068

Included within operational assets at cost above is an amount of £2.208m relating to a capital project involving the design and construction of a winter storage reservoir at Havant Thicket. Costs incurred to date are in respect of initial design, planning application and environmental impact studies. No depreciation has been provided for to date on this expenditure. The current position with this project is reported in the Operating and Financial Review.

In the preparation of its Statutory Accounts, the Company has followed common industry practice and adopted the infrastructure renewals accounting basis as set out in FRS 15 : Tangible Fixed Assets. However, for the purposes of the Regulatory Accounts, Ofwat has requested that FRS 15 is not applied for infrastructure renewals accounting, thereby providing a basis consistent with prior years. There has been no change to this policy in 2009/10. A reconciliation to the balance sheet shown in the Statutory Accounts is provided below:

	Infrastructure Assets £000
COST	
Cost at 31 March 2010 per Regulatory Accounts	45,756
Adjustment to opening balance	31,136
Infrastructure renewals expenditure capitalised since 1 April 1999	43,365
Disposals since 1 April 1999	(2,395)
Cost at 31 March 2010 per Statutory Accounts	117,862
DEPRECIATION	
At 31 March 2010 per Regulatory Accounts	-
Adjustment to opening balance	31,136
Depreciation charge for infrastructure renewals since 1 April 1999	38,569
Disposals	(2,395)
At 31 March 2010 per Statutory Accounts	67,310
NET BOOK VALUE	
At 31 March 2010 per Regulatory Accounts	45,756
Adjustments for infrastructure renewals accounting since 1 April 1999	4,796
At 31 March 2010 per Statutory Accounts	50,552

11. FIXED ASSET INVESTMENT

	Loan to Group Undertakings
At 1 April 2009	60,633
Repayment	(1,165)
At 31 March 2010	59,468

12. DEBTORS

	2010 £000	2009 £000
Trade debtors	1,912	1,133
Amounts owed by Group companies	23	26
Prepayments and accrued income	2,771	2,749
Other debtors	229	124
	4,935	4,032

All of the above amounts fall due within one year

As at 31 March 2010, trade debtors had a carrying value of £4.100m (2009 - £3.175m) before provision for bad debt. Trade debtors in arrears are provided for in full, but only an element of current debt is provided for. The amount of the provision was £2.188m as at 31 March 2010 (2009 - £2.042m).

The ageing of these debtors was as follows:

	2010 £000	2009 £000
Up to 12 months	2,182	1,393
Over 12 months	1,918	1,782
	4,100	3,175

The debtors provided for are mainly in respect of water charges for household customers where experience in the water industry has shown over time that it is likely that there will be difficulties in recovering the water charges for the periods concerned.

Movement on the provision for bad debt are as follows:

	2010 £000	2009 £000
As at 1 April 2009	2,042	1,794
Provision for bad debt required in the year	630	589
Debt written off in the year as uncollectable	(484)	(341)
As at 31 March 2010	2,188	2,042

The other classes within debtors do not contain balances that may be irrecoverable. The maximum exposure to credit risk at the reporting date is the fair value of each class of debtor mentioned above. The Company does not hold any collateral as security.

13. INVESTMENTS

	2010 £000	2009 £000
Unlisted investments	4	4

14. CASH AT BANK AND IN HAND

Of the total amount shown of £1.931m, £1.518m (2009 - £1.464m) is held specifically for the payment of the next half yearly loan interest charges.

15. BORROWINGS: DUE WITHIN ONE YEAR

	2010 £000	2009 £000
3% Perpetual debenture stock	60	60
3½% Perpetual debenture stock	185	185
4% Perpetual debenture stock	39	39
Bank loan	6,000	4,000
	6,284	4,284

The £6m bank loan is part of a five year £15m working capital facility, which is secured upon the assets of the Company and bears interest at London Interbank rates.

16. OTHER CREDITORS	Appointed 2010 £000	Non Appointed 2010 £000	Total 2010 £000	Appointed 2009 £000	Non Appointed 2009 £000	Total 2009 £000
Payments received on account	1,502	-	1,502	972	-	972
Trade creditors	1,050	-	1,050	920	-	920
Amounts owed to Group companies	203	-	203	725	-	725
Social security and other taxation	209	-	209	215	-	215
Other creditors	3,083	-	3,083	2,431	-	2,431
Accruals	422	-	422	574	-	574
Water rates in advance	5,177	-	5,177	5,058	-	5,058
	11,646	-	11,646	10,895	-	10,895

17. BORROWINGS: DUE AFTER ONE YEAR	2010 £000	2009 £000
Bank loan	81,416	82,600
Less: deferred arrangement costs	1,280	1,337
	80,136	81,263

The thirty year £66.5m index-linked loan was issued on 26 June 2002, is repayable on 30 September 2032, and is secured upon the assets of the Company. The capital value of the loan is adjusted by the change in the Retail Prices Index from year to year. The fees associated with the loan issue of £1.722m are amortised over the life of the loan. The amount owing on the loan is stated net of the unamortised issue fees.

The loan interest is calculated by adjusting the value of the loan by the Retail Prices Index and then charging interest on this inflated amount at 3.635% per annum.

18. PROVISIONS FOR LIABILITIES	2010 £000	2009 £000
DEFERRED TAXATION:		
At 1 April 2009	9,131	8,344
Provided during the year in profit and loss account	1,141	787
At 31 March 2010	10,272	9,131

The total deferred tax balance before the effect of discounting is £11.261m (2009 - £10.069m). The amount provided for deferred taxation represents timing differences caused by the excess of tax allowances over depreciation.

	2010 £000	2009 £000
Deferred tax excluding that relating to pension asset:		
Accelerated capital allowances	10,272	9,131
Pension asset (note 20)	3,801	4,736
Total provision for deferred tax	14,073	13,867
At 1 April 2009	13,867	16,738
Deferred tax charge in profit and loss account (note 8)	944	775
Deferred tax charged to the statement of total recognised gains and losses	(738)	(3,646)
At 31 March 2010	14,073	13,867

No provision has been made for deferred tax on gains recognised on the sale of properties where potentially taxable gains have been rolled over into replacement assets. Such tax would become payable only if the property were sold without it being possible to claim rollover relief. The total amount unprovided for is £0.694m (2009 - £0.694m). At present it is not envisaged that any tax will become payable in the foreseeable future.

19. RESERVES

	Share Premium £000	Capital Redemption £000	Profit and Loss £000
As 1 April 2009	1,539	3,250	55,540
Profit for financial year	-	-	5,422
Dividends	-	-	(4,663)
Actuarial loss on pension scheme	-	-	(2,636)
Movement on deferred tax relating to pension scheme	-	-	738
As 31 March 2010	1,539	3,250	54,401

20. PENSIONS

Portsmouth Water Limited is the principal employer and its parent company, Brockhampton Holdings Limited, is the participating employer in the Brockhampton Pension Scheme. This scheme provides defined benefits based primarily on final pensionable earnings. The assets of the scheme are held in a separate trustee administered fund.

The formal actuarial valuation as at 31 March 2008 was updated to the accounting date by an independent qualified actuary in accordance with FRS 17. As required by FRS 17, the value of the defined benefit liabilities has been measured using the projected unit method.

The key FRS 17 assumptions used for the scheme were as follows:

	2010 % per annum	2009 % per annum	2008 % per annum
Price inflation	3.7	3.2	3.7
Discount rate	5.5	6.9	6.7
Pension increases (RPI)	3.7	3.2	3.7
Salary growth	5.95	5.45	6.45

On the basis of the assumptions used for life expectancy, a male pensioner currently aged 60 would be expected to live for a further 28.7 years (2009 - 28.6 years). Allowance is made for future improvements in life expectancy.

The fair value of assets in the scheme, a breakdown of the assets into the main asset classes, the present value of the FRS 17 liabilities and the surplus of assets over the FRS 17 liabilities (which equals the gross pension asset) are set out below:

	2010 Expected Return % per annum	2010 Fair Value £000	2009 Expected Return % per annum	2009 Fair Value £000	2008 Expected Return % per annum	2008 Fair Value £000
Equities	7.8	74,538	8.0	53,382	7.7	66,777
Bonds	4.3	37,784	4.2	29,017	4.5	33,139
Other	2.0	1,521	1.9	4,325	3.9	7,780
	6.6	113,843	6.4	86,724	6.4	107,696

The expected return on assets is derived by taking the weighted average of the long-term expected return on each of the asset classes.

	2010 £000	2009 £000
Total fair value of scheme assets	113,843	86,724
FRS 17 value of scheme liabilities	100,268	69,808
Gross pension asset	13,575	16,916
Related deferred tax liability	3,801	4,736
Net pension asset	9,774	12,180

Under FRS 17, the scheme is represented on the balance sheet at 31 March 2010 as an asset of £13.575m (2009 - £16.916m), which amounts to £9.774m net of deferred tax (2009 - £12.180m).

The Company remained on a contribution holiday until 31 March 2010, it has agreed to begin paying contributions from 1 April 2010 at a rate of 12.4% of earnings. Based upon current earnings, this would result in Company contributions of £0.735m per annum. Members pay contributions at a rate of 5% of earnings.

The FRS 17 value of scheme liabilities moved over the period as follows:

	2010 £000	2009 £000
Opening scheme liabilities	69,808	77,718
Employer's part of current service cost	1,419	1,718
Interest cost	4,762	5,175
Contributions by scheme participants	284	277
Benefits paid	(3,306)	(2,968)
Actuarial loss/(gain)	27,301	(12,112)
Closing scheme liabilities	100,268	69,808

The FRS 17 value of scheme assets moved over the period as follows:

	2010 £000	2009 £000
Opening fair value of scheme assets	86,724	107,696
Expected return on assets	5,476	6,851
Contributions by scheme participants	284	277
Benefits paid	(3,306)	(2,968)
Actuarial gain/(loss)	24,665	(25,132)
Closing fair value of scheme assets	113,843	86,724

The following amounts have been included within operating profit under FRS 17:

	2010 £000	2009 £000
Current service cost (employer's part only)	1,419	1,718
Past service credit	-	-
Total operating charge	1,419	1,718

The following amounts have been included as other finance income under FRS 17:

	2010 £000	2009 £000
Expected return on pension scheme assets	5,476	6,851
Interest on post retirement liabilities	(4,762)	(5,175)
Net return	714	1,676
Total (expense) recognised in the profit and loss account	(705)	(42)

The following amounts have been recognised within the statement of total recognised gains and losses (STRGL) under FRS 17:

	2010	2009
Actual return less expected return on scheme assets	24,665	(25,132)
Experience gains arising on scheme liabilities	-	4,722
(Loss)/gain due to changes in assumptions underlying the FRS 17 value of scheme liabilities	(27,301)	7,390
Actuarial (loss) recognised in the STRGL	(2,636)	(13,020)

The actual return on plan assets was a gain of £30.141m in the year to 31 March 2010 (2009 - loss of £18.281m).

The history of experience gains and losses is:

	2010	2009	2008	2007	2006
Present value of scheme liabilities (£000)	(100,268)	(69,808)	(77,718)	(86,882)	(84,086)
Total fair value of scheme assets (£000)	113,843	86,724	107,696	108,711	104,899
Surplus (£000)	13,575	16,916	29,978	21,829	20,813
Actual return less expected return on scheme assets (£000)	24,665	(25,132)	(5,382)	(535)	13,587
Percentage of scheme’s assets	22%	(29)%	(5)%	0%	13%
Experience gains arising on scheme’s liabilities (£000)	-	4,722	-	-	65
Percentage of the FRS 17 value of the scheme’s liabilities	-	7%	-	-	-
Total amount recognised in the STRGL (£000)	(2,636)	(13,020)	7,602	(519)	4,527
Percentage of the FRS 17 value of the scheme’s liabilities	3%	19%	10%	0%	5%

The cumulative amount recognised in the STRGL as at 31 March 2010 was a loss of £22.633m (2009 - loss of £19.997m).

The Accounting Standards Board have published guidance relating to best practice for disclosure of pensions information. The Company has decided not to follow the guidance at this time.

CURRENT COST PROFIT AND LOSS ACCOUNT
FOR THE APPOINTED BUSINESS

For the year ended 31 March 2010

	Notes	2010 £000	2009 £000
TURNOVER	2	37,306	35,384
Current cost operating costs	3	(30,686)	(29,901)
Operating income	2	(65)	(48)
		6,555	5,435
Working capital adjustment	4	262	(21)
CURRENT COST OPERATING PROFIT		6,817	5,414
Interest receivable		1,405	4,537
Other finance income		714	1,676
Interest payable and similar charges		(1,944)	(7,351)
Financing adjustment	4	59	(13)
CURRENT COST PROFIT BEFORE TAXATION		7,051	4,263
Taxation			
- Current Tax		(2,077)	(892)
- Deferred Tax		(944)	(775)
CURRENT COST PROFIT FOR THE FINANCIAL YEAR		4,030	2,596
Dividends		(4,607)	(4,623)
CURRENT COST (LOSS) RETAINED		(577)	(2,027)

CURRENT COST BALANCE SHEET
FOR THE APPOINTED BUSINESS

As at 31 March 2010

	Notes	2010 £000	2009 £000
FIXED ASSETS			
Tangible fixed assets	5	753,285	719,233
Third party contributions since 1989/90		(21,653)	(20,202)
		731,632	699,031
Working capital	6	(5,991)	(5,891)
Cash		416	1,144
Short term deposits		1,515	1,460
Infrastructure renewals prepayment		3,324	919
NET OPERATING ASSETS		730,896	696,663
NON OPERATING ASSETS AND LIABILITIES			
Borrowings		(6,284)	(4,284)
Non-trade debtors		9	152
Non-trade creditors: amounts falling due within one year		(177)	(711)
Investment - loan to group company		59,468	60,633
- other		4	4
Corporation tax payable		(742)	-
Dividends		(1,875)	(1,875)
TOTAL NON OPERATING ASSETS AND LIABILITIES		781,299	750,582
CREDITORS: AMOUNTS FALLING DUE AFTER ONE YEAR			
Borrowings		(80,136)	(81,263)
PROVISIONS FOR LIABILITIES AND CHARGES		701,163	669,319
Deferred tax provision		(10,272)	(9,131)
NET ASSETS EXCLUDING PENSION ASSET		690,891	660,188
Pension asset		9,774	12,180
NET ASSETS INCLUDING PENSION ASSET		700,665	672,368
CAPITAL AND RESERVES			
Called up share capital		1,078	1,078
Share premium account		1,539	1,539
Capital redemption reserve		3,250	3,250
Profit and loss account	7	18,374	20,849
Current cost reserve	8	676,424	645,652
		700,665	672,368

For the year ended 31 March 2010

	Notes	Appointed 2010 £000	Non Appointed 2010 £000	Total 2010 £000	Appointed 2009 £000	Non Appointed 2009 £000	Total 2009 £000
NET CASH INFLOW FROM OPERATING ACTIVITIES	9	16,521	78	16,599	16,662	57	16,719
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE							
Interest received		1,420	-	1,420	4,417	-	4,417
Interest paid		(3,071)	-	(3,071)	(3,327)	-	(3,327)
NET CASHFLOW FROM RETURNS ON INVESTMENT AND SERVICING OF FINANCE		(1,651)	-	(1,651)	1,090	-	1,090
TAXATION							
UK corporation tax paid		(1,740)	(22)	(1,762)	(1,925)	(83)	(2,008)
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT							
Purchase of tangible fixed assets		(5,959)	-	(5,959)	(6,454)	-	(6,454)
Receipt of contributions		552	-	552	890	-	890
Infrastructure renewals expenditure		(6,966)	-	(6,966)	(5,067)	-	(5,067)
Sale of tangible fixed assets		12	-	12	19	-	19
NET CASH OUTFLOW FROM INVESTING ACTIVITIES		(12,361)		(12,361)	(10,612)	-	(10,612)
EQUITY DIVIDENDS PAID		(4,607)	(56)	(4,663)	(5,038)	(41)	(5,079)
CASH INFLOW/(OUTFLOW) BEFORE MANAGEMENT OF LIQUID RESOURCES AND FINANCING		(3,838)	-	(3,838)	177	(67)	110
MANAGEMENT OF LIQUID RESOURCES							
(Purchase) of short term deposits		(55)	-	(55)	-	-	-
NET CASHFLOW BEFORE FINANCING		(3,893)	-	(3,893)	177	(67)	110
FINANCING							
New loans		2,000	-	2,000	-	-	-
Loan repayment by Group Company		1,165	-	1,165	-	-	-
INCREASE/(DECREASE) IN CASH IN THE YEAR	10	(728)	-	(728)	177	(67)	110

1. ACCOUNTING POLICIES

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

The accounting policies used are the same as those adopted in the historical cost accounts as shown on pages 16 and 18, except as set out below:

Tangible Fixed Assets

Assets acquired prior to 31 March 1990 and in operational use are valued at the replacement cost of their operating capability. To the extent that the regulatory regime does not allow such assets to earn a return high enough to justify that value, this represents a modification of the value to the business principle. Also, no provision is made for possible funding of future replacements of pre 31 March 1990 assets by contributions from third parties and, to the extent that some of those assets would on replacement be so funded, replacement cost again differs from value to the business. Redundant assets are valued at their recoverable amounts.

Modern Equivalent Asset (MEA) Valuation

A review of the MEA valuation and asset stock is undertaken as part of the periodic review. The revised values arising from this review provide the basis for calculating the MEA in the current cost financial statements. The process of continuing refinement of asset records has produced adjustments to existing values. The current cost depreciation figures included in the current cost operating costs are based on the revised MEA values.

Land and buildings

Non-specialised operational properties are valued on the basis of open market value for existing use at 31 March 1993 and have been expressed in real terms by adjusting for inflation as measured by the changes in the Retail Price Index (RPI) since that date.

Specialised operational properties acquired since 31 March 1990 are valued at the lower of depreciated replacement cost and recoverable amount, restated annually between periodic Asset Management Plan (AMP) reviews by adjusting for inflation, as measured by changes in the RPI.

Infrastructure assets

Mains are valued at replacement cost, determined principally on the basis of data provided by the AMP.

A process of continuing refinement of asset records is expected to produce adjustments to existing values when periodic review of the AMP takes place. In the intervening years, values are restated to take account of changes in the general level of inflation as measured by changes in the RPI over the year.

Other operational fixed assets

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

Surplus land

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

Third party contributions

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

Real Financial Capital Maintenance Adjustments

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

Working capital adjustment - this is calculated by applying the change in the RPI over the year to the opening working capital balance.

Financing adjustment - this is calculated by applying the change in the RPI over the year to the opening balance of net finance, which comprises all monetary assets and liabilities in the balance sheet, apart from those included in working capital, deferred tax, dividends payable and index linked debt.

Other Current Cost Adjustments

Depreciation adjustment - this is the difference between depreciation based on the current cost value of assets in these accounts and depreciation charged in arriving at historical cost profit.

Disposal of fixed assets adjustment - this is the difference between the values of realised assets in these current cost financial statements and the historical cost financial statements.

There has been no change in the year to the current cost depreciation policy.

2. TURNOVER

	2010 £000	2009 £000
Unmeasured supplies	22,572	22,242
Measured supplies	10,197	9,438
Measured large users	2,543	2,079
SWS bulk supply	518	518
Third party services	1,377	982
Other sources	99	125
	37,306	35,384

OPERATING INCOME

	2010 £000	2009 £000
Current cost loss on disposal of fixed assets	(65)	(48)
Working capital adjustment	262	(21)

3. CURRENT COST OPERATING COSTS

	2010 £000	2009 £000
Operating costs per historical cost accounts	29,072	28,452
Current cost depreciation adjustment (note 1)	1,614	1,449
	30,686	29,901

4. WORKING CAPITAL AND FINANCING ADJUSTMENTS

These are the real financial capital maintenance adjustments for working capital and net finance, as described in note 1.

5. TANGIBLE FIXED ASSETS

	Operational Assets £000	Infrastructure Assets £000	Other Tangible Assets £000	Total £000
GROSS CURRENT REPLACEMENT COST				
At 1 April 2009	184,161	596,255	14,061	794,477
RPI adjustment	8,192	26,525	592	35,309
Disposals	(22)	-	(744)	(766)
Additions	3,939	1,796	1,353	7,088
At 31 March 2010	196,270	624,576	15,262	836,108
DEPRECIATION				
At 1 April 2009	65,817	-	9,427	75,244
RPI adjustment	2,928	-	389	3,317
Disposals during year	-	-	(681)	(681)
Charge for year	3,678	-	1,265	4,943
At 31 March 2010	72,423	-	10,400	82,823
NET BOOK VALUE				
At 31 March 2010	123,847	624,576	4,862	753,285
At 1 April 2009	118,344	596,255	4,634	719,233

The RPI adjustment relates to the increase of the current cost valuations in line with inflation.

6. WORKING CAPITAL

		2010 £000	2009 £000
Stores		553	415
Trade debtors	- measured household	46	26
	- unmeasured household	1,246	1,268
	- measured non-household	333	295
	- unmeasured non-household	9	11
	- other	919	256
Measured income accrual		2,568	2,453
Prepayments and other debtors		203	168
Trade creditors		(517)	(920)
Deferred income - customer advance receipts		(2,144)	(1,696)
Capital creditors		(3,166)	(2,037)
Accruals and other creditors		(6,041)	(6,130)
TOTAL WORKING CAPITAL		(5,991)	(5,891)

7. PROFIT AND LOSS ACCOUNT	£000
As 1 April 2009	20,849
Loss for the financial year	(577)
Actuarial loss on pension scheme	(2,636)
Movement on deferred tax relating to pension scheme	738
As 31 March 2010	18,374

8. CURRENT COST RESERVE	£000
As 1 April 2009	645,652
RPI adjustments:-	
Fixed assets	31,992
Working capital adjustment	(262)
Net finance adjustment	(59)
Third party contributions	(899)
At 31 March 2010	676,424

9. RECONCILIATION OF OPERATING PROFIT TO NET CASH INFLOW FROM OPERATING ACTIVITIES	2010 £000	2009 £000
Current cost operating profit	6,817	5,414
Working capital adjustment	(262)	21
(Decrease)/increase in working capital	(1,139)	94
Other finance charges	1,419	1,718
Current cost depreciation	4,943	4,713
Current cost loss on sale of fixed assets	72	48
Infrastructure renewals charge	4,561	4,420
Movement in provisions	110	234
NET CASHFLOW FROM OPERATING ACTIVITIES	16,521	16,662

10. ANALYSIS OF NET DEBT	As at 1 April 2009 £000	Cash Flow £000	Non Cash Movements £000	As at 31 March 2010 £000
Cash at bank and in hand	1,144	(728)	-	416
Loans due after one year	(81,263)	-	1,127	(80,136)
Loans due within one year	(4,284)	(2,000)	-	(6,284)
	(85,547)	(2,000)	1,127	(86,420)
Short term deposits	1,460	55	-	1,515
Current asset equity investments	4	-	-	4
	1,464	55	-	1,519
	(82,939)	(2,673)	1,127	(84,485)

INTEREST RATE RISK PROFILE

	Fixed rate £000	Floating Rate £000	Index linked £000	Total £000
MATURITY PROFILE				
Less than one year	(284)	(6,000)	-	(6,284)
Between one and two years	-	-	-	-
Between two and five years	-	-	-	-
Between five and twenty years	-	-	-	-
In more than twenty years	-	-	(80,136)	(80,136)
TOTAL BORROWINGS	(284)	(6,000)	(80,136)	(86,420)
Cash and investments				420
Short term deposits				1,515
NET DEBT				(84,485)

CURRENT COST ACTIVITY COST TABLE

	Resources & Treatment £000	Distribution £000	Water Supply Subtotal £000
Direct Costs			
Employment costs	172	2,486	2,658
Power	1,103	1,112	2,215
Hired and contracted services	6	598	604
Materials and consumables	327	402	729
Service charges	1,804	-	1,804
Other direct costs	59	66	125
Total direct costs	3,471	4,664	8,135
General and support expenditure	2,368	3,397	5,765
Total functional expenditure	5,839	8,061	13,900
Business Activities			
Customer services			1,749
Scientific services			952
Other business activities			340
Business activities subtotal			3,041
Local authority rates			2,475
Doubtful debts			630
Total opex less third party services			20,046
Third party services - opex			1,136
Total operating expenditure			21,182
Capital Maintenance			
Infrastructure renewals charge	-	4,561	4,561
Current cost depreciation			
- service activities	2,451	1,508	3,959
- business activities			984
Total capital maintenance			9,504
Total operating costs			30,686
CCA (MEA) Values			
Service activities	47,416	704,532	751,948
Business activities			1,337
Service totals			753,285
Services for the third parties			-
Total			753,285

Explanatory Note: For the purpose of activity costing analysis, costs are allocated between service areas using the Company's management information reports. These reports allow costs to be identified for each cost centre in the Company and therefore the costs of each service area (e.g. Resources/Treatment) can be built up using the reports and by following the RAG guidance on cost centre areas to be included for each service.

Regulatory Capital Value at 2009/10 prices

	£000
Opening Regulatory Capital Value as at 1 April 2009	113,740
Capital Expenditure (excluding infrastructure renewals)	4,141
Infrastructure renewals expenditure	4,656
Infrastructure renewals charge	(4,413)
Capital contributions	(1,430)
Current cost depreciation	(4,768)
Outperformance of regulatory assumptions (5 years in arrears)	(2,617)
Closing Regulatory Capital Value as at 31 March 2010	109,309
Price Review opening adjustments for 2010/11	2,108
Adjusted opening Regulatory Capital Value as at 01 April 2010	111,417
Average Regulatory Capital Value for the year	109,049

Explanatory Note

The Table shown above gives the build up of the Regulatory Capital Value for the financial year ended 31 March 2010 that was used by the Office of Water Services in setting price limits for the AMP4 period in the 2004 Final Determination of price limits.

The Regulatory Capital Value is the capital base for the Company on which it is allowed to earn a rate of return at the given cost of capital.

The opening Regulatory Capital Value for the year is adjusted to take account of net new investment (being new capital expenditure less capital contributions received) and the current cost depreciation charge for the year, as allowed in the 2004 Final Determination of price limits.

There is also a further adjustment made to reflect past outperformance of regulatory assumptions for the previous price setting period. This relates to capital expenditure efficiencies which were achieved in that period and which have been retained by the Company for five years, under the Office of Water Services' approach to Regulatory Capital Values.

Any differences in actual capital expenditure and depreciation charges from those allowed in the 2004 Final Determination do not affect price limits in the current period. These differences, including any capital efficiencies achieved, have been taken into account in the calculation of the Regulatory Capital Value for the next price review period from 2010 onwards.

The closing Regulatory Capital Value shown above has then been adjusted to incorporate the opening adjustments arising from the 2009 price review, to give the opening Regulatory Capital Value as at 1 April 2010.

For the purposes of the KPI indicator reported in the Operating and Financial Review on page 4, we have used this opening value as at 1 April 2010 for the Debt to Regulatory Capital Value Ratio, following the price determination.

The Directors are responsible, under Condition F of the Instrument of Appointment by the Secretary of State for the Environment, Food and Rural Affairs (Defra) and as a water undertaker under the Water Industry Act 1991, for preparing the financial statements for each financial year that give a true and fair view of the state of affairs of the Company at the end of the financial year 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 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 proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 2006;
- safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities; and
- the maintenance and integrity of the corporate and financial information included on the Company’s website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

In so far as the Directors are aware:

- there is no relevant audit information of which the Company’s auditors are unaware; and
- the Directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditors are aware of that information.

Certificate of Compliance with Licence Condition F6A

In arriving at the certificate provided below, the Board met on 23 June 2010 to consider the Appointee's financial and management requirements over the next 12 months and the available resources. The Directors reviewed the following information:

- the latest financial position of the Company through its latest Report and Accounts
- the Management Accounts for May 2010
- the current level of gearing
- the projected level of gearing through to 2011, based on its own internal budget projections
- the Company's available bank and overdraft facilities through to 2011
- the headroom between the projected key operating ratios (gearing and interest cover) and its loan covenants through to 2011

The Board were satisfied that sufficient resources existed and that they could provide the necessary assurance. In addition, compliance with the relevant sections of RAG 5.04 was also reviewed.

As required by the Water Services Regulation Authority the Board hereby certifies:

- that, in the opinion of the Directors, Portsmouth Water Limited will have available to it sufficient financial resources and facilities to enable it to carry out, for at least the next 12 months, the Regulated Activities (including the investment programme necessary to fulfil the Appointee’s obligations under the Appointment); and
- that, in the opinion of the Directors, the Appointee will, for at least the next 12 months, have available to it management resources which are sufficient to enable it to carry out those functions; and
- that, in the opinion of the Directors, all contracts entered into with any Associated Company include all necessary provisions and requirements concerning the standard of service to be supplied to the Appointee, to ensure that it is able to meet all its obligations as a water undertaker; and
- in accordance with its Instrument of Appointment under the Water Industry Act 1991, the Directors are of the opinion that the Company is in compliance with paragraph 3.1 of Condition 'K' of that Instrument.

Signed by:

T. M. Lazenby M.B.E. ....

N. J. Roadnight ....

N. Smith ....

A. R. Neve ....

R. L. Sullivan ....

R. J. Tennant ....

The transactions required to be disclosed under Condition F of the Company's Instrument of Appointment are set out below:

Borrowings or Sums Lent

There is a loan outstanding made to a Group Company, South Downs Limited, in June 2002. The balance of the loan, consisting of the principal amount and accrued interest to date, amounts to £59.468m. This loan was made as a part of the refinancing package which was carried out in the financial year 2002/03. The interest rate for the loan is based on LIBOR plus a margin.

Dividends paid to Associated Undertakings

The dividends paid to the holding company, Portsmouth Water Holdings Limited, are shown in note 9 on page 21 of these Regulatory Accounts. The dividend policy is also covered within this note.

Payments for Tax Losses

Payments relating to the surrender of tax losses to Portsmouth Water Limited, from Group Companies, made to South Downs Limited amounting to £797,672.

Supply of Services

Details of services supplied to the Appointee by associates during the year are disclosed below. No services of a material value were provided by the Appointee to associates.

Service	Associate Company	Turnover of Associate (£000's)	Terms of Supply	Value (£000's)
Rent of operational sites	Brockhampton Holdings Limited	198	Market Tested	82
Management Charge	South Downs Limited	-	Turnover	61

There is a recharge of Directors salaries amounting to £20,812 paid to Portsmouth Water Limited by Brockhampton Holdings Limited, which represents the time spent by Portsmouth Water Executive Directors on Group matters.

Statement by Board of Directors

To the best of their knowledge, the Directors of the Company declare that all appropriate transactions with associated companies have been disclosed.

REPORT OF THE INDEPENDENT AUDITOR TO THE WATER SERVICES REGULATION AUTHORITY AND DIRECTORS OF PORTSMOUTH WATER LIMITED

We have audited the regulatory accounts of Portsmouth Water Ltd on pages 13 to 38 which comprise:

- the regulatory historical cost accounting statements comprising the regulatory historical cost profit and loss account, the regulatory historical cost balance sheet, the regulatory historical cost statement of total recognised gains and losses and the historical cost reconciliation between statutory and regulatory accounts; and the regulatory current cost accounting statements for the appointed business comprising the current cost profit and loss account, the current cost balance sheet, the current cost cash flow statement and the related notes to the current cost financial statements including the statement of accounting policies.

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

Basis of Preparation

The Regulatory Accounts have been prepared in accordance with Condition F of the Appointment and the Regulatory Accounting Guidelines, the accounting policies set out in the statement of accounting policies and, in the case of the regulatory historical cost accounting statements, under the historical cost convention.

The Regulatory Accounts are separate from the statutory financial statements of the Company. There are differences between United Kingdom Generally Accepted Accounting Principles (UK GAAP) and the basis of preparation of information provided in the regulatory accounts because the Regulatory Accounting Guidelines specify alternative treatment or disclosure in certain respects. Where the Regulatory Accounting Guidelines do not specifically address an accounting issue, then they require UK GAAP to be followed. Financial information other than that prepared wholly on the basis of UK GAAP may not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in financial statements prepared in accordance with the Companies Act 2006.

Respective Responsibilities of the WSRA, Directors and Auditors

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

The Directors' responsibilities for preparing the Regulatory Accounts in accordance with Regulatory Accounting Guidelines are set out in the statement of directors' responsibilities for regulatory information on page 39.

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

We report to you our opinion as to whether the regulatory historical cost accounting statements present fairly, under the historical cost convention, the revenues and costs, assets and liabilities of the appointee and its appointed business in accordance with the Company's Instrument of Appointment and Regulatory Accounting Guideline 2.03 (Guideline for the classification of expenditure), Regulatory Accounting Guideline 3.06 (Guideline for the contents of regulatory accounts) and Regulatory Accounting Guideline 4.03 (Guideline for the analysis of operating costs and assets); and whether the regulatory current cost accounting statements on pages 29 to 38 have been properly prepared in accordance with Regulatory Accounting Guideline 1.04 (Guideline for accounting for current costs and regulatory capital values), Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03. We also report to you if, in our opinion, the Company has not kept proper accounting records as required by paragraph 3 of Condition F and whether the information is in agreement with the appointees' accounting records and has been properly prepared in accordance with the requirements of Condition F and, as appropriate, Regulatory Accounting Guideline 1.04, Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.06, and Regulatory Accounting Guideline 4.03.

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

Basis of Audit Opinion

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

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Regulatory Accounts are free from material misstatement, whether caused by fraud or other irregularity or error. However, as the nature, form and content of Regulatory Accounts are determined by the WSRA, we did not evaluate the overall adequacy of the presentation of the information, which would have been required if we were to express an audit opinion under Auditing Standards.

Our opinion on the Regulatory Accounts is separate from our opinion on the statutory financial statements of the Company on which we report, which are prepared for a different purpose. Our audit report in relation to the statutory accounts of the Company (our "Statutory" audit) was made solely to the Company's members, as a body, in accordance with sections 495, 496 and 497 of the Companies Act 2006. Our statutory audit work was undertaken so that we might state to the Company's members those matters we are required to state to them in a Statutory auditors' report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume any responsibility to anyone other than the Company and the Company's members as a body, for our Statutory audit work, for our Statutory audit report, or for the opinions we have formed in respect of that Statutory audit.

The regulatory historical cost accounting statements on pages 13 to 28 have been drawn up in accordance with Regulatory Accounting Guideline 3.06 in that infrastructure renewals accounting as applied in previous years should continue to be applied and accordingly that the relevant sections of Financial Reporting Standards 12 and 15 be disapplied. The effect of this departure from Generally Accepted Accounting Principles, and a reconciliation of the balance sheet drawn up on this basis with that drawn up under Companies Act 2006 is given on page 23.

Opinion

In our opinion the Regulatory Accounts of the Company for the year ended 31 March 2010 fairly present in accordance with Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water undertaker under the Water Industry Act 1991, the Regulatory Accounting Guidelines issued by the WSRA and the accounting policies set out on pages 16 to 18 and page 32, the state of the Company's affairs at 31 March 2010 on an historical cost and current cost basis, the historical cost and current cost profit for the year and the current cost cash flow for the year and have been properly prepared in accordance with those conditions, guidelines and accounting policies.

In respect of this information we report that in our opinion:

(a) proper accounting records have been kept by the Appointee as required by paragraph 3 of Condition 'F' of the Instrument;

(b) the information is in agreement with the Appointee's accounting records, and has been properly prepared in accordance with the requirements of Condition 'F' and, as appropriate, Regulatory Accounting Guideline 1.04, Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03 issued by the WSRA;

(c) the regulatory historical cost accounting statements on pages 13 to 28 present fairly, under the historical cost convention, the revenues and costs, assets and liabilities of the Appointee and its Appointed Business in accordance with the Company's Instrument of Appointment and Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03 issued by the WSRA; and

(d) the regulatory current cost accounting statements on pages 29 to 38 have been properly prepared in accordance with Regulatory Accounting Guideline 1.04, Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03 issued by the WSRA.

NICHOLAS KELSEY
Senior Statutory Auditor
For and on behalf of
SAFFERY CHAMPNESS
CHARTERED ACCOUNTANTS
REGISTERED AUDITORS
LION HOUSE RED LION STREET
LONDON
23 JUNE 2010

		2010 £000	2009 £000
KPI - 1			
a)	**Gearing - Debt/RCV**		
(i)	Debt		
	Bank loan (note 17, page 25)	81,416	82,600
	Bank loan (note 15, page 24)	6,000	4,000
	Debenture stock (note 15, page 24)	284	284
	Cash at bank and in hand	(1,931)	(2,604)
		85,769	84,280

For the purposes of this ratio, debt excludes the deferred arrangement costs of £1.280m (note 17, on page 25) and the current asset investment of £0.004m (note 13, on page 24).

(ii) Regulatory Capital Value (RCV)

Value established by Ofwat in Final Determination in 2009

One of the elements considered by Ofwat in assessing revenues required by the Company is a return on the capital investment in the business. The value of the capital base of each company for the purposes of setting price limits is the RCV. The RCV is widely used by the investment community as a proxy for the market value of the regulated business. For Portsmouth Water the RCV is a key element of its bond covenants.

		2010 £000	2009 £000
	Regulatory capital value indexed to 31 March	111,417	108,896
(iii)	Gearing - Debt/RCV ratio (i) ÷ (ii)	77.0%	77.4%

b) Cash interest cover

This ratio represents the number of times cashflow of the business covers interest payments.

(i) Cashflow before interest paid is derived from the cashflow statement on page 31 and is calculated as follows:

		2010 £000	2009 £000
	Net cashflow from operating activities	16,599	16,719
	Interest received, excluding amounts for inter-company loan	23	125
	Taxation, excluding payments for group relief	(965)	(724)
	Capital expenditure	(12,361)	(10,612)
	New borrowings	2,000	-
		5,296	5,508
(ii)	Interest paid	3,071	3,327
(iii)	Cash interest cover ratio (i) ÷ (ii)	1.72	1.66

KPI - 2 and 3 Customer Service Measures

Indicators are based on information supplied to Ofwat and confirmed in the Ofwat publication ‘Levels of Service for the Water Industry in England and Wales Report’

KPI - 4 Water Quality

This indicator is based on figures reported to the DWI.

KPI - 5 Efficiency

The results for this indicator are provided by Ofwat in its publication ‘Water and Sewerage Unit Costs and Efficiency’.

KPI - 6 Leakage

This indicator is based on figures supplied to Ofwat and confirmed in its report ‘Security of Supply, Leakage and the Efficient Use of Water’. The figures for 2009/10 have been supplied to Ofwat, but will not be confirmed in the Ofwat document until later in 2010.