

DEE VALLEY WATER PLC
REGULATORY FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2005

DEE VALLEY WATER PLC

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DEE VALLEY WATER PLC

DIRECTORS' REPORT FOR THE YEAR ENDED 31 MARCH 2005

Directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing those financial statements, the directors are required to:

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

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

Licence condition F6A

In the opinion of the Directors, the Appointee will have available to it sufficient financial resources and facilities to enable it to carry out, for at least the next 12 months, the Regulated Activities (including the investment programme necessary to fulfil its obligations under the Appointment).

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.

Licence condition K3

In the opinion of the Directors, the Company is in compliance with paragraph 3.1 of Condition K of the Licence.

Transactions with associated companies

To the best of the directors' knowledge, all appropriate transactions with associated companies have been disclosed in these financial statements.

On behalf of the board

D J Guest
Director
17 June 2005

DEE VALLEY WATER PLC

INDEPENDENT AUDITORS' REPORT TO THE DIRECTOR GENERAL OF WATER SERVICES AND DIRECTORS OF DEE VALLEY WATER PLC

We have audited the Regulatory Accounts of Dee Valley Water plc for the year ended 31st March 2005 on pages 5 to 30 which comprise:

- (a) the regulatory historical cost accounting statements comprising the regulatory historical cost profit and loss account, the regulatory historical cost balance sheet; and
- (b) 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 Director General of Water Services (the Regulator) in order to meet the requirements of Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the company as a water and sewage undertaker under the Water Industry Act 1991 (the Regulatory Licence). Our audit work has been undertaken so that we might state to the company and the Regulator those matters that we have agreed to state to them in our report, in order (a) to assist the company to meet its obligation under the company's Instrument of Appointment to procure such a report and (b) to facilitate the carrying out by the Regulator 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 Regulator, 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 1985.

Respective responsibilities of the regulator, the directors and auditors

The nature, form and content of Regulatory Accounts are determined by the Regulator. It is not appropriate for us to assess whether the nature of the information being reported upon is suitable or appropriate for the Regulator'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 1.

DEE VALLEY WATER PLC

INDEPENDENT AUDITORS' REPORT (continued) TO THE DIRECTOR GENERAL OF WATER SERVICES AND DIRECTORS OF DEE VALLEY WATER PLC

Our responsibility is to audit the Regulatory Accounts in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board, except as 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 on pages 5 and 6 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 3.05 (Guideline for the contents of regulatory accounts) and Regulatory Accounting Guideline 4.02 (Guideline for the analysis of operating costs and assets); and whether the regulatory current cost accounting statements on pages 7 to 9 have been properly prepared in accordance with Regulatory Accounting Guideline 1.03 (Guideline for accounting for current costs and regulatory capital values), Regulatory Accounting Guideline 3.05 and Regulatory Accounting Guideline 4.02.

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 1.03, Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.05, and Regulatory Accounting Guideline 4.02.

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 performance 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 Auditing Standards 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 Regulator, 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 section 235 of the Companies Act 1985.

DEE VALLEY WATER PLC

INDEPENDENT AUDITORS' REPORT (continued) TO THE DIRECTOR GENERAL OF WATER SERVICES AND DIRECTORS OF DEE VALLEY WATER PLC

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 5 and 6 have been drawn up in accordance with Regulatory Accounting Guideline 3.05 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 1985 is given in note 25.

Opinion

In our opinion the Regulatory Accounts of the company for the year ended 31 March 2005 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 and sewerage undertaker under the Water Industry Act 1991, the Regulatory Accounting Guidelines issued by the Regulator and the accounting policies set out on pages 11 to 14, the state of the company's affairs at 31 March 2005 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 1.03, Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.05 and Regulatory Accounting Guideline 4.02 issued by the Regulator;
- (c) the regulatory historical cost accounting statements on pages 5 and 6 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 3.05 and Regulatory Accounting Guideline 4.02 issued by the Regulator;
- (d) the regulatory current cost accounting statements on pages 7 to 9 have been properly prepared in accordance with Regulatory Accounting Guideline 1.03, Regulatory Accounting Guideline 3.05 and Regulatory Accounting Guideline 4.02 issued by the Regulator.

Saffery Champness

17 June 2005

Chartered Accountants
Registered Auditors

Lion House
Red Lion Street
London
WC1R 4GB

DEE VALLEY WATER PLC

**HISTORIC COST PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31 MARCH 2005**

		Appointed	Non	Total	Appointed	Non	Total
		2005	appointed	2005	2004	appointed	2004
Notes		£000	2005	£000	£000	2004	£000
Turnover	3	16,806	1	16,807	16,597	64	16,661
Operating costs		(11,022)	(72)	(11,094)	(11,124)	(142)	(11,266)
Operating profit		<u>5,784</u>	<u>(71)</u>	<u>5,713</u>	<u>5,473</u>	<u>(78)</u>	<u>5,395</u>
Other income		32	1,210	1,242	36	1,147	1,183
Other interest receivable and similar income	7	577	-	577	276	-	276
Interest payable and similar charges	8	<u>(2,513)</u>	<u>-</u>	<u>(2,513)</u>	<u>(2,424)</u>	<u>-</u>	<u>(2,424)</u>
Historic cost profit before taxation		<u>3,880</u>	<u>1,139</u>	<u>5,019</u>	<u>3,361</u>	<u>1,069</u>	<u>4,430</u>
Taxation	9	<u>(1,335)</u>	<u>(342)</u>	<u>(1,677)</u>	<u>(1,625)</u>	<u>(321)</u>	<u>(1,946)</u>
Historic cost profit after taxation		<u>2,545</u>	<u>797</u>	<u>3,342</u>	<u>1,736</u>	<u>748</u>	<u>2,484</u>
Dividends	10	<u>(1,287)</u>	<u>(797)</u>	<u>(2,084)</u>	<u>(1,290)</u>	<u>(748)</u>	<u>(2,038)</u>
Historic cost profit retained		<u><u>1,258</u></u>	<u><u>-</u></u>	<u><u>1,258</u></u>	<u><u>446</u></u>	<u><u>-</u></u>	<u><u>446</u></u>

DEE VALLEY WATER PLC

HISTORIC COST BALANCE SHEET
AS AT 31 MARCH 2005

		Appointed	Non	Total	Appointed	Non	Total
		2005	appointed	2005	2004	appointed	2004
Notes		£000	2005	£000	£000	2004	£000
Fixed assets							
Tangible assets		45,228	59	45,287	41,683	59	41,742
		<u>45,228</u>	<u>59</u>	<u>45,287</u>	<u>41,683</u>	<u>59</u>	<u>41,742</u>
Current assets							
Stocks	13	173	-	173	145	-	145
Debtors: amounts falling due within one year	14	3,614	-	3,614	4,013	-	4,013
Debtors: amounts falling due after more than one year	14	767	-	767	549	-	549
Short term investments		15,565	243	15,808	16,178	243	16,421
Cash at bank and in hand		(552)	571	19	(478)	518	40
		<u>19,567</u>	<u>814</u>	<u>20,381</u>	<u>20,407</u>	<u>761</u>	<u>21,168</u>
Creditors: amounts falling due within one year	15	<u>(8,623)</u>	<u>(873)</u>	<u>(9,496)</u>	<u>(9,076)</u>	<u>(820)</u>	<u>(9,896)</u>
Net current assets/(liabilities)		<u>10,944</u>	<u>(59)</u>	<u>10,885</u>	<u>11,331</u>	<u>(59)</u>	<u>11,272</u>
Total assets less current liabilities		<u>56,172</u>	<u>-</u>	<u>56,172</u>	<u>53,014</u>	<u>-</u>	<u>53,014</u>
Creditors: amounts falling due after more than one year	16	<u>(40,814)</u>	<u>-</u>	<u>(40,814)</u>	<u>(39,704)</u>	<u>-</u>	<u>(39,704)</u>
Provisions for liabilities and charges	17	<u>(8,811)</u>	<u>-</u>	<u>(8,811)</u>	<u>(8,021)</u>	<u>-</u>	<u>(8,021)</u>
		<u>6,547</u>	<u>-</u>	<u>6,547</u>	<u>5,289</u>	<u>-</u>	<u>5,289</u>
Capital and reserves							
Called up share capital		240	-	240	240	-	240
Other reserves		614	-	614	614	-	614
Profit and loss account		5,693	-	5,693	4,435	-	4,435
		<u>6,547</u>	<u>-</u>	<u>6,547</u>	<u>5,289</u>	<u>-</u>	<u>5,289</u>

DEE VALLEY WATER PLC**CURRENT COST PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31 MARCH 2005**

		2005	2004
	Notes	£000	£000
Turnover	3	16,806	16,597
Operating costs	4 / 5	(12,297)	(12,656)
Working capital adjustment		135	75
Current cost operating profit	6	4,644	4,016
Other income	3	32	3
Other interest receivable and similar income	7	577	276
Interest payable and similar charges	8	(2,513)	(2,424)
Financing adjustment		(762)	(532)
Current cost profit before taxation		1,978	1,339
Taxation	9	(1,335)	(1,625)
Current cost profit/(loss) attributable to shareholders		643	(286)
Dividends	10	(1,287)	(1,290)
Current cost loss retained		(644)	(1,576)

DEE VALLEY WATER PLC**CURRENT COST BALANCE SHEET
AS AT 31 MARCH 2005**

	Notes	2005 £000	2004 £000
Fixed assets			
Tangible assets	11	359,521	289,133
Third party contributions since 1989-90		(12,100)	(11,067)
		<hr/>	<hr/>
		347,421	278,066
Working capital	12	4,005	2,542
		<hr/>	<hr/>
Net operating assets		351,426	280,608
Cash and investments		4,354	5,633
Non-trade debtors		593	1,277
Non-trade creditors due within one year		(799)	(880)
Creditors due after one year		(37,819)	(36,709)
Provisions for liabilities and charges	17	(8,811)	(8,021)
Dividends payable		(859)	(867)
		<hr/>	<hr/>
Net assets employed		308,085	241,041
		<hr/> <hr/>	<hr/> <hr/>
Capital and reserves			
Called up share capital		240	240
Current cost reserve	19	319,736	252,048
Other reserves		614	614
Profit and loss account		(12,505)	(11,861)
		<hr/>	<hr/>
Total capital and reserves		308,085	241,041
		<hr/> <hr/>	<hr/> <hr/>

DEE VALLEY WATER PLC

**CURRENT COST CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 MARCH 2005**

	Appointed	Non	Total	Appointed	Non	Total
	2005	appointed	2005	2004	appointed	2004
	£000	£000	£000	£000	£000	£000
Net cash flow from operating activities	8,112	1,139	9,251	9,365	1,069	10,434
Interest received	311	-	311	275	-	275
Interest paid	(1,403)	-	(1,403)	(1,354)	-	(1,354)
Net cash outflow for returns on investments and servicing of finance	<u>(1,092)</u>	<u>-</u>	<u>(1,092)</u>	<u>(1,079)</u>	<u>-</u>	<u>(1,079)</u>
Taxation	<u>(403)</u>	<u>(321)</u>	<u>(724)</u>	<u>(289)</u>	<u>(299)</u>	<u>(588)</u>
Capital expenditure						
Payments to acquire tangible assets	(5,430)	-	(5,430)	(7,285)	-	(7,285)
Receipt of grants and contributions	679	-	679	929	-	929
Infrastructure renewals expenditure	(1,927)	-	(1,927)	(2,233)	-	(2,233)
Receipts from sales of tangible assets	78	-	78	-	-	-
Net cash outflow for capital expenditure	<u>(6,600)</u>	<u>-</u>	<u>(6,600)</u>	<u>(8,589)</u>	<u>-</u>	<u>(8,589)</u>
Equity dividends paid	<u>(1,295)</u>	<u>(765)</u>	<u>(2,060)</u>	<u>(1,255)</u>	<u>(713)</u>	<u>(1,968)</u>
Net cash outflow before management of liquid resources and financing	<u>(1,278)</u>	<u>53</u>	<u>(1,225)</u>	<u>(1,847)</u>	<u>57</u>	<u>(1,790)</u>
Management of liquid resources						
Current asset investments	1,199	-	1,199	1,704	-	1,704
(Decrease)/increase in cash	<u>(79)</u>	<u>53</u>	<u>(26)</u>	<u>(143)</u>	<u>57</u>	<u>(86)</u>

DEE VALLEY WATER PLC

NOTES TO THE CURRENT COST CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 MARCH 2005

1 Reconciliation of current cost operating profit to net cash inflow from operating activities	2005	2004
	£000	£000
Current cost operating profit	4,644	4,016
Working capital adjustment	(135)	(75)
Change in stocks	(28)	29
Receipts from other income	32	36
Current cost depreciation	2,424	2,643
Profit on disposal	(43)	-
Increase in debtors	(781)	(1,242)
Increase/(decrease) in creditors	72	1,725
Infrastructure renewals expenditure	1,927	2,233
Net cash flow from operating activities	8,112	9,365

2 Analysis of net debt	1 April 2004	Cash flow	Other non-cash changes	31 March 2005
	£000	£000	£000	£000
Net cash:				
Bank overdrafts	(788)	(79)	-	(867)
Liquid resources:				
Current asset investments	6,421	(1,200)	-	5,221
Debts falling due within one year	-	-	-	-
Debts falling due after one year	(36,709)	-	(1,110)	(37,819)
Net debt	(31,076)	(1,279)	(1,110)	(33,465)

**NOTES TO THE REGULATORY FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2005**

1 Current cost accounting policies

These accounts have been prepared for the Appointed Business of Dee Valley Water plc in accordance with guidance issued by the Director General of Water Services for modified real terms financial statements suitable for regulation in the water industry.

They measure profitability on the basis of real financial capital maintenance in the context of assets which are valued at their current cost value to the business with the exception of assets acquired prior to 31 March 1990.

Except as set out below, the accounting policies used are the same as those adopted in the historical cost accounts, an abstract from which is set out for reference purposes in note 2 to these accounts.

1.1 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 the possible funding of future replacements of pre 31 March 1990 assets by contributions from third parties and to the extent that some of those assets would on replacement be so funded, replacement cost again differs from value to the business. Redundant assets are valued at their recoverable amounts.

Land and buildings

Specialised operational properties acquired since 31 March 1990 are valued at the lower of depreciated replacement cost and recoverable amount, restated annually between periodic Surface Investment Requirement ('SIR') reviews by adjusting for inflation as measured by changes in the RPI. The unamortised portion of third party contributions received is deducted in arriving at net operating assets (as described below).

Infrastructure assets

Mains, impounding and pumped raw water storage reservoirs are valued at replacement cost determined principally on the basis of data provided by the Asset Management Plan ('AMP').

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

Other fixed assets

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

Grants and other third party contributions

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

**NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005**

1 Current cost accounting policies (continued)

1.2 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 Retail Price Index ('RPI') over the year to the opening total of trade debtors and stock less trade creditors.

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.

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.

1.3 Principles of cost allocation used to prepare activity costing analysis

The job costing function within the Company's accounting system plays a key role in ensuring expenditure is correctly allocated between operating costs, capital costs and capital maintenance.

The allocation of general and support costs relating to departments providing a company wide service is based, where possible, on a measurement of the level of service provided to a business area. Where no such measure is available costs are allocated in proportion to direct costs for a business area. Whilst every effort is made to ensure year on year consistency of allocation, changes have been made where necessary to adhere as closely as possible to the regulatory reporting guidelines.

1.4 Dividend policy

The board sets the dividend payable by Dee Valley Water plc on a prudent basis, taking into account the future financing requirements of the business as evidenced by the latest financial projections. The board also takes into account the financial covenants agreed with the loan provider, which effectively place an upper limit on the cash which can be paid out as dividend.

**NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005**

2 Extract from historic cost accounting policies

2.1 Turnover

Turnover represents amounts receivable for goods and services net of VAT and trade discounts.

2.2 Tangible fixed assets and depreciation

Tangible fixed assets other than freehold land are stated at cost less depreciation. Depreciation is provided at rates calculated to write off the cost less estimated residual value of each asset over its expected useful life, as follows:

Freehold land, buildings and fixed plant - 50 to 80 years

Infrastructure assets - 5 to 25 years

Mobile plant, vehicles and equipment - 3 to 20 years

This accounting policy differs from that now adopted in the published statutory accounts of the Company with regard to the depreciation of infrastructure assets, the policy in respect of which is detailed below.

2.3 Infrastructure assets

Infrastructure assets comprise underground systems of mains and impounding and pumped raw water storage reservoirs. As these systems are maintained in perpetuity and have no finite lives, no depreciation is charged on such assets. Expenditure on replacing and maintaining the assets is charged as an operating cost and expenditure to increase or enhance the assets is capitalised.

Charges for infrastructure renewals expenditure take account of planned expenditure on maintaining the operating capability of infrastructure assets in accordance with the Company's investment programme. The timing of the investment programme and operational considerations may result in uneven patterns of infrastructure renewals expenditure. Charges to the profit and loss account are adjusted by way of accruals or deferrals, as appropriate, to take account of any significant fluctuations between actual and planned expenditure.

This accounting policy is not in accordance with FRS12 and differs from that now adopted within the published statutory accounts of the Company. Following the introduction of FRS12 and in accordance with FRS15, expenditure on infrastructure assets relating to increases in capacity or enhancement of the network and on maintaining the operating capability of the network in accordance with defined standards of service is treated in the statutory accounts of the Company as an addition and included at cost after deducting grants and contributions.

The depreciation charge for infrastructure assets is the estimated level of annual expenditure required to maintain the operating capability of the network which is based on the Company's independently certified asset management plan.

For Regulatory Accounts purposes, expenditure to refurbish mains for quality enhancement is capitalised in accordance with OFWAT guidelines.

For statutory accounts purposes, all refurbishment expenditure is accounted for in accordance with FRS15 and included within the planned annual expenditure upon which the depreciation charge is based.

**NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005**

2 Extract from historic cost accounting policies (continued)

2.4 Grants and contributions

Grants and contributions receivable relating to infrastructure assets have been deducted from the cost of tangible fixed assets. This is not in accordance with the Companies Act 1985 which requires tangible fixed assets to be shown at cost and hence grants and contributions as deferred income. This departure from the requirements of the Companies Act 1985 is, in the opinion of the Directors, necessary for the financial statements to show a true and fair view, as these assets do not have determinable finite lives and therefore no basis exists on which to recognise grants and contributions as deferred income.

2.5 Stock

Stock is valued at the lower of cost and net realisable value.

2.6 Pensions

The regular cost of providing retirement pensions and related benefits is charged to the profit & loss account over the employees' service lives on the basis of a constant percentage of earnings. Any difference between the charge to the profit and loss account and the contributions paid to the scheme is shown as an asset or liability in the balance sheet.

2.7 Taxation

Current tax, including UK corporation tax and foreign tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date. Timing differences are differences between the Company's taxable profits and its results as stated in the financial statements that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the financial statements.

A net deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax is not recognised when fixed assets are revalued unless by the balance sheet date there is a binding agreement to sell the revalued assets and the gain or loss expected to arise on sale has been recognised in the financial statements. Neither is deferred tax recognised when fixed assets are sold and it is more likely than not that the taxable gain will be rolled over, being charged to tax only if and when the replacement assets are sold.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax is measured on a discounted basis.

DEE VALLEY WATER PLC

**NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005**

3 Analysis of turnover and operating income for the appointed business

	2005	2004
	£000	£000
Turnover		
Measured	8,145	7,736
Unmeasured	8,517	8,696
Other sources	144	165
	<hr/>	<hr/>
Total turnover	16,806	16,597
	<hr/> <hr/>	<hr/> <hr/>
Operating income		
Current cost (loss)/profit on disposal of assets	-	(33)
Other operating income	32	36
	<hr/>	<hr/>
Total operating income	32	3
	<hr/> <hr/>	<hr/> <hr/>
Working capital adjustment	135	75
	<hr/> <hr/>	<hr/> <hr/>

DEE VALLEY WATER PLC

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

4 Activity costing analysis for the year ended 31 March 2005

	Service analysis			Business analysis		
	Water resource & treat	Water distbn	Water supply sub-tot	Customer services	Scientific services	Cost of regulation
Direct costs						
Employment costs	515	658	1,173			
Power	320	342	662			
Agencies	-	-	-			
Hired and contracted services	94	38	132			
Associated companies	-	-	-			
Materials and consumables	337	123	460			
Service charges NRA	639	-	639			
Bulk supply imports	38	-	38			
Other direct costs	118	11	129			
Total direct costs	2,061	1,172	3,233	734	332	216
General and support expenditure	1,215	757	1,972	237	99	-
Functional expenditure	3,276	1,929	5,205	971	431	216
Total business activities						
Local authority rates			1,175			
Doubtful debts			103			
Exceptional items			-			
Total Opex less third party services			8,101			
Third party services - opex			157			
Total operating expenditure			8,258			
Capital costs						
Infrastructure renewals expenditure	282	1,589	1,927			
Movement in infrastructure renewals prepayment	-	(312)	(312)			
Current cost depreciation (allocated)	1,696	395	2,091			
Amortisation of deferred credits			-			
Amortisation of intangible assets			-			
Business activities current cost depreciation			333			
Capital maintenance excluding third party services			4,039			
Third party services - capital maintenance			-			
Total capital maintenance			4,039			
TOTAL OPERATING COSTS			12,297			
CCA (MEA) values						
Service activities	91,101	303,389	394,490			
Business activities			5,968			
Water supply total			400,458			
Services for third parties			-			
Total			400,458			

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

5 Activity costing analysis for the year ended 31 March 2004

	Service analysis			Business analysis		
	Water resource & treat	Water distbn	Water supply sub-tot	Customer services	Scientific services	Cost of regulation
Direct costs						
Employment costs	489	632	1,121			
Power	252	245	497			
Agencies	-	-	-			
Hired and contracted services	103	33	136			
Associated companies	-	90	90			
Materials and consumables	329	111	440			
Service charges NRA	594	-	594			
Bulk supply imports	54	-	54			
Other direct costs	112	73	185			
Total direct costs	1,933	1,184	3,117	702	393	435
General and support expenditure	1,218	790	2,008	223	118	-
Functional expenditure	3,151	1,974	5,125	925	511	435
Total business activities						
Local authority rates			1,153			
Doubtful debts			139			
Exceptional items			-			
Total Opex less third party services			8,288			
Third party services - opex			157			
Total operating expenditure			8,445			
Capital costs						
Infrastructure renewals expenditure	833	1,339	2,233			
Movement in infrastructure renewals prepayment	-	(665)	(665)			
Current cost depreciation (allocated)	1,659	440	2,099			
Amortisation of deferred credits			-			
Amortisation of intangible assets			-			
Business activities current cost depreciation			544			
Capital maintenance excluding third party services			4,211			
Third party services - capital maintenance			-			
Total capital maintenance			4,211			
TOTAL OPERATING COSTS			12,656			
CCA (MEA) values						
Service activities	89,760	239,258	329,018			
Business activities			9,094			
Water supply total			338,112			
Services for third parties			-			
Total			338,112			

DEE VALLEY WATER PLC

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

6 Operating profit	2005	2004
	£000	£000
Current cost operating profit is stated after charging:		
Depreciation of tangible assets	2,424	2,642
Operating lease rentals	439	436
Auditors' remuneration	18	18
Remuneration of auditors for non-audit work	53	101
	<u> </u>	<u> </u>
7 Other interest receivable and similar income	2005	2004
	£000	£000
Bank and other interest	311	276
Interest received from group companies	266	-
	<u> </u>	<u> </u>
	577	276
	<u> </u>	<u> </u>
8 Interest payable	2005	2004
	£000	£000
On bank overdrafts	5	4
Loan interest	1,389	1,349
Loan indexation	1,110	1,071
On overdue tax	9	-
	<u> </u>	<u> </u>
	2,513	2,424
	<u> </u>	<u> </u>
9 Taxation	2005	2004
	£000	£000
Domestic current year tax		
U.K. corporation tax	573	579
Adjustment for prior years	(141)	-
Payment in respect of group relief	114	95
	<u> </u>	<u> </u>
Current tax charge	546	674
Deferred tax		
Deferred tax charge	789	951
	<u> </u>	<u> </u>
	1,335	1,625
	<u> </u>	<u> </u>

DEE VALLEY WATER PLC

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

10 Dividends			2005	2004
			£000	£000
Ordinary interim paid			429	423
Ordinary final proposed			858	867
			<u>1,287</u>	<u>1,290</u>
			<u><u>1,287</u></u>	<u><u>1,290</u></u>
11 Tangible fixed assets	Infrastructure assets	Operational assets	Other tangible assets	Total
	£000	£000	£000	£000
Gross replacement cost				
At 1 April 2004	223,532	107,593	6,904	338,029
AMP adjustment	81,239	(30,588)	(5,606)	45,045
RPI adjustment	9,741	2,460	41	12,242
Additions	1,249	3,612	565	5,426
Disposals	-	-	(80)	(80)
	<u>315,761</u>	<u>83,077</u>	<u>1,824</u>	<u>400,662</u>
At 31 March 2005	315,761	83,077	1,824	400,662
Depreciation				
At 1 April 2004	-	45,660	3,236	48,896
AMP adjustment	-	(8,688)	(2,642)	(11,330)
RPI adjustment	-	1,182	19	1,201
On disposals	-	-	(50)	(50)
Charge for the year	-	2,229	195	2,424
	<u>-</u>	<u>40,383</u>	<u>758</u>	<u>41,141</u>
At 31 March 2005	-	40,383	758	41,141
Net book value				
At 31 March 2005	<u>315,761</u>	<u>42,694</u>	<u>1,066</u>	<u>359,521</u>
At 31 March 2004	<u><u>223,532</u></u>	<u><u>61,933</u></u>	<u><u>3,668</u></u>	<u><u>289,133</u></u>

DEE VALLEY WATER PLC

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

12 Working capital	Note	2005	2004
		£000	£000
Stocks	13	173	145
Trade debtors		804	853
Trade creditors		(6,294)	(6,664)
Infrastructure renewals prepayment		2,126	1,776
Other accruals		(321)	(306)
Trade payments in advance		(571)	(531)
Payroll related taxes and social security		(131)	(125)
Other short term group debtors		7,348	6,762
Prepayments and other debtors		871	632
		<u>4,005</u>	<u>2,542</u>
		<u><u>4,005</u></u>	<u><u>2,542</u></u>
 13 Stocks		 2005	 2004
		£000	£000
Raw materials and consumables		173	145
		<u>173</u>	<u>145</u>
		<u><u>173</u></u>	<u><u>145</u></u>
 14 Debtors		 2005	 2004
		£000	£000
Trade debtors		1,142	1,172
Corporation tax		111	715
Other debtors		2,258	2,043
Prepayments and accrued income		103	83
		<u>3,614</u>	<u>4,013</u>
Amounts falling due after more than one year		767	549
Pension prepayment		767	549
		<u>767</u>	<u>549</u>
		<u><u>4,381</u></u>	<u><u>4,562</u></u>

DEE VALLEY WATER PLC

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

15 Creditors: amounts falling due within one year

	2005 £000	2005 £000	2005 £000	2004 £000
	Appointed	Non appointed	Total	Total
Bank loans and overdrafts	315	-	315	310
Trade creditors	6,294	-	6,294	6,664
Corporation tax	162	342	504	623
Other taxes and social security costs	131	-	131	125
Other creditors	53	-	53	53
Accruals and deferred income	809	-	809	755
Proposed dividend	859	531	1,390	1,366
	8,623	873	9,496	9,896
	8,623	873	9,496	9,896

16 Creditors: amounts falling due after more than one year

	2005 £000	2004 £000
3 1/2% undated irredeemable debentures	114	114
Index linked bank loan	37,705	36,595
Amounts owed to parent and fellow subsidiary undertakings	2,995	2,995
	40,814	39,704
	40,814	39,704

17 Provisions for liabilities and charges

	Deferred taxation £000
Balance at 1 April 2004	8,021
Profit and loss account	790
Balance at 31 March 2005	8,811
	8,811

Deferred taxation provided in the regulatory accounts is as follows:

	Fully provided	
	2005 £000	2004 £000
Accelerated capital allowances	8,811	8,021
	8,811	8,021

**NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005**

18 Pension costs

Defined benefit

The company participates in a defined benefit pension scheme, the Water Companies Pension Scheme. The scheme funds are administered by trustees and are independent of the Company's finances. Contributions are paid to the scheme in accordance with the recommendations of an independent actuarial adviser.

In line with the requirements of FRS17, published by the Accounting Standards Board in November 2000 and updated in November 2002, details in respect of the scheme are provided below in accordance with both SSAP24 and FRS17. The Company does not anticipate adopting FRS17 earlier than the mandatory requirement to do so and therefore the figures in the accounts reflect the SSAP24 details below.

i) SSAP24

Contributions to the Scheme are charged to the profit and loss account so as to spread the cost of pensions over employees' working lives with the Company. The contributions are determined by a qualified actuary on the basis of triennial valuations using the current unit method for death in service benefits and the projected unit method for other benefits.

The most recent full valuation was at 1 April 2002. In that valuation, the assumptions which had the most significant effect on the results were those relating to the rate of return on investments and the rates of increases in salaries and pensions. It was assumed that investment returns would be 7.2% pa before retirement and 5.2% pa after retirement. General salary increases were assumed to be 4.8% pa and present and future pensions were assumed on average to increase in payment at 2.8% pa.

The valuation at 1 April 2002 showed the following:

Market value of the Scheme's assets - £33,460,000

Value of assets as a percentage of the value of benefits accrued, after allowing for future increases in earnings - 116%

As a result of general falls in stock market values, it should be noted that the funding level will have fallen since the last valuation.

At 31st March 2005 the pension prepayment, calculated by the scheme's actuaries, amounted to £767,947. The prepayment at 1st April 2004 was £548,895, and the movement during the year, which has been debited to the profit and loss account, amounted to £219,052 (2004 - £216,000).

ii) FRS17

The formal actuarial valuation at 1 April 2002 was updated to the accounting date by an independent qualified actuary in accordance with the transitional arrangements of FRS17. As required by FRS17, the value of the defined benefit liabilities has been measured using the projected unit method.

The following sets out the key FRS17 assumptions used for the scheme. It also sets out, as at the accounting date, the fair value of assets, a breakdown of the assets into the main classes, the present value of the FRS17 liabilities and the deficit of assets below the FRS17 liabilities (which equals the gross pension liability).

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

18 Pension costs**(continued)**

Assumptions	2005	2004	2003
Inflation	2.9% pa	2.9% pa	2.5% pa
Pension increases	2.9% pa	2.9% pa	2.5% pa
Salary increases	4.9% pa	4.9% pa	4.5% pa
Discount rate	5.4% pa	5.5% pa	5.6% pa
Expected return			
Equities	7.7% pa	7.9% pa	7.5% pa
Bonds	4.7% pa	4.7% pa	4.5% pa
Cash	4.7% pa	4.6% pa	3.8% pa

The market value of the assets of the Scheme at 31 March 2005 was £32,893,000, composed of 49% equities and 51% bonds. At the same date, the present value of the Scheme's liabilities, under FRS17 assumptions, was £35,293,000. Under FRS17, the Scheme would therefore be represented on the balance sheet as a liability of £2,400,00 (£1,680,000 net of deferred tax).

During the year to 31 March 2005, the Company contributed £430,000 (2004 - £10,000) to the Scheme. It has been agreed that employer contributions will be 9.7% of pensionable remuneration for members on the open scale of benefits and 18.5% of pensionable remuneration for members on the closed scale of benefits from 1 April 2004.

The deficit under FRS17 moved over the period as follows:

	2005	2004
	£000	£000
		Restated
Deficit at start of year	(2,561)	(3,900)
Current service cost (employee and employer)	555	(729)
Contributions (employee and employer)	(797)	147
Other net finance income	116	61
Actuarial gain	287	1,860
	<u> </u>	<u> </u>
Deficit at end of year	<u>(2,400)</u>	<u>(2,561)</u>

The following amounts would have been included within operating profit under FRS17:

Current service cost (employer's part only)	672	591
Past service cost	-	-
	<u> </u>	<u> </u>
Total operating charge	<u>672</u>	<u>591</u>

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

18 Pension costs**(continued)**

The following amounts would have been included as net finance income under FRS17:

	2005	2004
	£000	£000
		Restated
Expected return on pension scheme assets	1,927	1,687
Interest on post retirement liabilities	(1,811)	(1,626)
	<u>116</u>	<u>61</u>
	<u><u>116</u></u>	<u><u>61</u></u>

The following amounts would have been recognised within the statement of total recognised gains and losses ("STRGL) under FRS17:

Actual return less expected return on scheme assets	1,025	4,440
Experience gains/(losses) arising on scheme's liabilities	719	(94)
Loss due to changes in assumptions underlying the FRS17 value of scheme liabilities	(1,457)	(2,486)
	<u>287</u>	<u>1,860</u>
	<u><u>287</u></u>	<u><u>1,860</u></u>

The history of experience gains and losses is:

	2005	2004
		Restated
Actual return less expected return on scheme assets (£000)	1,025	4,440
Percentage of scheme's assets	3%	15%
Experience (losses)/gains arising on scheme's liabilities (£000)	719	(94)
Percentage of the FRS17 value of the scheme's liabilities	2%	0%
Total amount recognised in the STRGL (£000)	287	1,860
Percentage of the FRS17 value of the scheme's liabilities	1%	6%

19 Movement on current cost reserve

2005 **2004**
£000 **£000**

Balance at 1 April 2004	252,048	244,645
RPI adjustments		
Fixed assets	11,041	7,203
Working capital	(135)	(75)
Financing	762	532
Third party contributions	(354)	(257)
AMP adjustment	56,374	-
	<u>319,736</u>	<u>252,048</u>
Balance at 31 March 2005	<u><u>319,736</u></u>	<u><u>252,048</u></u>

DEE VALLEY WATER PLC

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

20 Regulatory capital value

	£000
Opening regulatory capital value as at 1 April 2004	48,686
Capital expenditure (excluding infrastructure renewals)	3,444
Infrastructure renewals expenditure	1,694
Infrastructure renewals charge	(1,951)
Grants and contributions	(249)
Current cost depreciation	(3,259)
Outperformance of regulatory assumptions (5 years in arrears)	(417)
	<hr/>
Closing regulatory capital value at 31 March 2005	47,948
	<hr/> <hr/>
Average regulatory capital value for the year	48,316
	<hr/> <hr/>

21 Directors' emoluments

	2005	2004
	£000	£000
Emoluments for qualifying services	235	237
	<hr/>	<hr/>
The number of directors for whom retirement benefits are accruing under defined benefit schemes amounted to 2 (2004- 4).		
Emoluments for qualifying services	102	95
Accrued pension at the end of the year	51	46
Accrued lump sum at the end of the year	152	138
	<hr/>	<hr/>

22 Employees

Number of employees

The average monthly number of employees (including directors) during the year was:

	2005	2004
	Number	Number
Administration	89	87
Operations	92	85
	<hr/>	<hr/>
	181	172
	<hr/> <hr/>	<hr/> <hr/>

Employment costs

	£000	£000
Wages and salaries	4,273	4,063
Social security costs	367	328
Other pension costs	220	225
	<hr/>	<hr/>
	4,860	4,616
	<hr/> <hr/>	<hr/> <hr/>

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

23 Current cost profit and loss account for appointed business - five year rolling summary

The summary below is presented in 2004/05 prices, restating prior year figures using the specified average Retail Price Index (RPI).

	00/01	01/02	02/03	03/04	04/05
	£000	£000	£000	£000	£000
Turnover	17,920	17,640	17,185	17,112	16,806
Current cost operating costs	(12,309)	(12,478)	(13,943)	(13,048)	(12,297)
Operating income	-	-	-	(34)	-
Working capital adjustment	(52)	(17)	(48)	77	135
Current cost operating profit	5,559	5,145	3,194	4,107	4,644
Other income	26	177	60	37	32
Net interest	320	140	(1,180)	(2,215)	(1,936)
Financing adjustment	(468)	(240)	(753)	(548)	(762)
Current cost profit before taxation	5,437	5,222	1,321	1,381	1,978
Taxation	(1,938)	(1,839)	(931)	(1,675)	(1,335)
	3,499	3,383	390	(294)	643
Dividends	(2,992)	(9,918)	(1,324)	(1,330)	(1,287)
Current cost profit/(loss) retained	507	(6,535)	(934)	(1,624)	(644)

24 Current cost balance sheet for appointed business - five year rolling summary

The summary below is presented in 2004/05 prices, restating prior year figures using the specified average Retail Price Index (RPI).

	00/01	01/02	02/03	03/04	04/05
	£000	£000	£000	£000	£000
Tangible fixed assets	288,145	289,119	293,657	298,096	359,521
Third party contributions since 1989-90	(8,828)	(9,494)	(10,473)	(11,410)	(12,100)
Working capital	(528)	(19,591)	3,722	2,621	4,005
Net operating assets	278,789	260,034	286,906	289,307	351,426
Cash and investments	8,944	(252)	7,928	5,808	4,354
Non trade debtors	200	125	1,229	1,317	593
Non trade creditors	(4,829)	(3,776)	(621)	(907)	(799)
Creditors due after more than one year	(27,642)	(4,166)	(37,772)	(37,847)	(37,819)
Provisions for liabilities and charges	(5,004)	(5,433)	(5,400)	(8,270)	(8,811)
Dividends payable	(1,962)	(1,922)	(882)	(894)	(859)
Net assets employed	248,496	244,610	251,388	248,514	308,085
Capital and reserves					
Called up share capital	264	260	254	247	240
Profit and loss account	(1,533)	(8,042)	(8,808)	(12,227)	(12,505)
Current cost reserve	249,091	251,727	259,291	259,861	319,736
Other reserves	674	665	651	633	614
	248,496	244,610	251,388	248,514	308,085

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

25 Historic cost balance sheet reconciliation to statutory accounts

In the preparation of its statutory accounts, the company has followed common industry practice and adopted the infrastructure renewals accounting basis as set out in FRS15, Tangible Fixed Assets. However for the purposes of the Regulatory Accounts, Ofwat has requested that FRS15 is not applied for infrastructure renewals accounting, thereby providing a basis consistent with prior years. A reconciliation to the balance sheet shown in the statutory accounts is set out below.

	£000
Debtors	
At 31 March 2005 per Regulatory Accounts	4,381
Less: Infrastructure renewals prepayment	(2,112)
Add: Short term loans to group companies	10,320
	<hr/>
At 31 March 2005 per Statutory accounts	12,589
	<hr/> <hr/>
Tangible fixed assets	
Cost	
At 31 March 2005 per Regulatory Accounts	102,867
Adjustment to opening balance	1,800
Infrastructure renewals expenditure capitalised in the year	312
	<hr/>
At 31 March 2005 per Statutory Accounts	104,979
	<hr/> <hr/>
Depreciation	
At 31 March 2005 per Regulatory Accounts	44,385
Adjustment to opening balance	1,643
Depreciation charge for IRE	429
	<hr/>
At 31 March 2005 per Statutory Accounts	46,457
	<hr/> <hr/>
Net book value	
At 31 March 2005 per Regulatory Accounts	45,287
Adjustment for infrastructure renewals accounting	40
	<hr/>
At 31 March 2005 per Statutory Accounts	45,327
	<hr/> <hr/>

**NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005**

26 Financial review and commentary

Operating performance

During the reporting period turnover for the appointed business increased by 1.26%, reflecting the charge increases effective from 1 April 2004. The meter option programme continued to result in a transfer from unmeasured to measured income.

Operating costs decreased by 1.8%. Electricity cost increases significantly in excess of inflation, were offset by operating cost efficiencies, and a reduction in the cost of regulation (which was at its peak in 2003/4 due to the five year cycle of regulatory reviews.) Historic cost depreciation rose by 7%. However current cost depreciation decreased by 8% due to the incorporation of the AMP 4 revaluation in the 2004/5 regulatory accounts.

Thus whilst historic cost operating profits increased by 6%, current cost operating profits increased by 16%.

Financing

The highly geared balance sheet reflects the effect of the Company securing a £35 million index linked loan from Artesian Finance in 2002. The proceeds of the loan were used by the parent company to return funds to shareholders. As a condition of the loan, the Company has entered into a number of covenants.

The most recent report to the lender dated 31 March 2005 and covering the period up to 31 March 2007 showed no actual or potential breach of any covenants.

Interest receivable increased in the year due to a charge being made on the net inter group indebtedness. No such charge was made in 2004.

The increase in current cost fixed assets reflects the effect of incorporating the AMP 4 revaluation in to the regulatory accounts as required by Ofwat, giving rise to an increase in net book value of £56m. This revaluation does not affect the historic cost accounts.

Taxation

The tax charge of £1,335,000 includes an undiscounted charge for deferred taxation of £789,000, which is consistent with the approach adopted in 2004, following Ofwat guidance. The discounted provision continues to be used as the basis of charge in the statutory accounts.

The Regulatory Capital Value (as calculated by Ofwat in 2004/05 prices) at 31 March 2005 was £47.9 million. The post tax return on the Regulatory Capital Value was 8.59%.

Dividends

Dividends paid by the appointed business amounted to £1,287,000.

Cashflow

The negative net cashflow of £79,000 was due to the continued high level of capital expenditure necessary to achieve the target for the 5 year period ending in March 2005.

**NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005**

26 Financial review and commentary

(continued)

Five year rolling summaries

The five year rolling summaries, notes 23 and 24, give the financial results for the last five years in real terms, that is after adjusting for the effects of inflation.

The current cost profit and loss account shows the reduction in turnover and hence profitability that took place in 2000/1 as a result of the new price limits that came into effect in that year. After adjusting for the exceptional item of £1,062,000 in 2003, operating costs have increased largely due to the rapid rise in insurance costs between 2002 and 2004 and the need to start making a SSAP 24 pension charge in 2003 (in prior years there has been a credit to operating costs).

2004/05 operating costs reductions have been reviewed in the foregoing comments on operating performance.

Dividends demonstrate the effect of the balance sheet restructuring referred to above. The dividend payment of £9.9 million in 2002 was necessary to facilitate the restructuring.

The current cost balance sheets highlight the introduction of the index linked loan in 2003, the provision for undiscounted deferred tax in 2003/4 and the AMP 4 revaluation of fixed assets in 2004/5 described in the foregoing Financing section.

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Summary

Procedures for the identification, monitoring and charging of inter-company transactions including the monitoring of cross company directorships and the composition of company Boards, which have been applied during the year, were approved by the Group Board in July 2000.

At this time there were 2 major business elements leading to inter-company transactions:

The Energy business ceased to trade during 2002/3 and as a consequence, transactions relating to the energy business have declined significantly. During 2004/5 costs charged to the energy business relate to Dee Valley Water plc personnel undertaking cash collection activities relating to the remaining Energy company debtors.

Dee Valley Services Ltd provided a contracting service under a term contract with Dee Valley Water plc, which expired in May 2003. Dee Valley Water plc did not award a new term contract. The contracting work is now being carried out 'in house' by Dee Valley Water plc. No transactions have arisen between Dee Valley Water plc and Dee Valley Services Ltd in 2004/5.

Thus the levels of inter-company transactions have been reduced to virtually nil during the year.

NOTES TO THE REGULATORY FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 31 MARCH 2005

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(continued)

Split between Core and Non-Core

There are two main sources of 'non-core' income:

Billing commission

Sewerage is billed and collected on behalf of Dwr Cymru and North West Water. The majority of costs incurred relate to the pass-through of commission paid to Wrexham County Borough Council and Flintshire County Council for collection of council house charges. Costs are allocated on the basis of marginal cost, which works out at approximately 10% of the Customer Services departmental costs.

Other

Fishing licences make up the remaining non-core income. The associated costs are already separately identified.

Conclusion

The volume of intercompany transactions has deminished to vitually nothing during the year, and in future years it is anticipated that costs apportionment will only be necessary between core and non core elements of the business.

The procedures reviewed by the Board in July 2000, set out a realistic system for monitoring current activities and to provide a framework to identify new transactions as they arise.

28 Transactions with Associated Companies

The table below sets out the transactions with associated companies

Associated Company	Description	Terms of supply	Associates	Trade
			Annual Turnover £000	Value £000
North Wales Gas Ltd	Support services provided to North Wales Gas Ltd by Dee Valley Water plc	Cost	-	6

At 31 March 2005 there is inter-group indebtedness due to Dee Valley plc of £10,319,588 (2004 - £10,000,389) and Wrexham Water plc is indebted to Dee Valley Water plc for £2,995,600 (2004 - £2,995,600)