Veolia Water East Limited

Statutory & Regulatory Accounts for 2010-2011

Registered Office: Veolia Water East Limited, Mill Hill, Manningtree, Essex CO11 2AZ

VEOLIA WATER EAST LIMITED

ANNUAL REPORT AND FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2011

(Registered Number 2663338)

Veolia Water East Limited

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Veolia Water East Limited

Chairman's statement

I am pleased to present the statutory accounts for the year ended 31st March 2011.

The water industry operates on five-yearly cycles called Asset Management Plan (AMP) periods. Price limits for water and sewerage services are set by the water and sewerage regulator Ofwat before the beginning of each period and 2010/11 is the first year of the latest five year period, AMP 5. 2010-11 was a reasonably successful year for Veolia Water East and we commenced this new quinquennium as we had finished the last, with the provision of reliable, high quality and predictable performance to our customers, regulators, employees and shareholders.

The focus on Health and Safety remains our highest priority. We introduced a Zero Accidents target in 2009, and we continue to monitor our performance against this objective. Results for 2010/11 indicate deterioration in our performance compared with the previous year, and our campaign on health and safety awareness has been stepped up as a consequence. We believe that we are creating a strong safety culture in all that we do throughout the Company, thereby providing a far safer working environment for all of our employees.

Our financial performance for the year to 31st March 2011 is disappointing in comparison to the previous year, operating profit before asset disposals being £3.953m compared with £5.446m in 2009/10, a decrease of 27.4%. However, the results for the current year include depreciation on revalued assets which increased operating expenses by £0.632m. On a comparative basis, excluding this extra depreciation, operating profit before asset disposals would have been £4.585m which is still 15.8% below the prior year.

Turnover was down on the previous year at £14.678m (2009/10 £15.148m). The amount of water delivered has fallen in 2010/11 and this is one of the major reasons why turnover is significantly below the level of the Ofwat AMP 5 determination.

The introduction of a new performance indicator for AMP 5, the Service Incentive Mechanism (SIM), was a challenge for all Companies across the industry to implement, but we believe that the results for 2010/11 will indicate that it is 'business as usual' for Veolia Water East as we expect to top the ranks for our high quality customer service. This same message was delivered by the customer satisfaction surveys that were carried out in each quarter of the year for 2010/11, as the results when announced placed us first overall.

Our water resource availability remains strong and we did not place any restrictions on customers' use of water.

We maintained the serviceability of the physical water supply assets at a stable level and, despite another harsh winter, the number of bursts experienced was lower than both the previous year and the reference level set within our AMP5 determination.

This second consecutive severe winter once again challenged our ability to meet our annual leakage target. An increased focus on leakage detection, aided by newly implemented L'Mars leakage management software, ensured that our target was achieved. We consistently achieve the lowest level of leakage in the industry which contributes to both our environmental objectives and to maintaining the security of supply to our customers. However, this low level of leakage makes it increasingly difficult to find further, cost effective, reductions.

We continue to actively promote the efficient use of water to our customers through metering and water efficiency advice. We encourage customers to have a meter installed in order to sustain our focus on demand management and improve water efficiency and we anticipate that 78% of our household customers will be metered by 2015.

We have begun preparations for our defined output for 2010-15, the construction of a new treated water reservoir and pumping station at Dovercourt. Land has been acquired and the tender process underway. It is hoped that the construction of the reservoir will commence in July 2011.

Veolia Water East Limited

Chairman's statement (continued)

Veolia Water East procures services in water quality analysis, scientific and corporate responsibility services, procurement, communications and public relations, human resources, health and safety, legal, and IT from Veolia Water Shared Services Limited (VWSS). VWSS is a separate group company that sits outside of the regulatory ring fence and which provides these services to all of the companies in the Veolia Water UK Group. VWSS operates without profit and all charges are completely transparent to audit. Through this facility we continue to benefit from the group's extensive range of technical skills, together with the enhanced purchasing power and dilution of operating costs generated by the larger group, all of which provides benefit to our customers.

An annual incentive scheme is operated which rewards all employees for our performance against set criteria: zero accidents; a reduction in customer complaints against the set target; a reduction in supply interruptions against a set target; a top three ranking in quarterly consumer experience satisfaction surveys; zero adverse variance to budgeted profit. Performance against the first four criteria is measured quarterly for bonus purposes, the fifth is an annual measurement.

In summary, we continue to deliver strongly for the benefit of both our customers and the environment. We are meeting the outputs set down in the Final Determination for AMP 5 where these are controllable by us, and the delivery of our one defined output for the AMP is well underway. Most importantly our customers continue to enjoy an extremely high quality water efficient service.

Jeffery Herbert
Chairman
24 June 2011

Veolia Water East Limited

Directors

Nevil Muncaster (Managing Director)
Nevil Muncaster was appointed on 1 May 2007. He was previously head of programme management at Veolia Water Central Limited. He was appointed as Managing Director of Veolia Water Southeast in October 2010.

Non Executive:

Jeffrey Herbert (Chairman)
Jeffrey Herbert was appointed in December 2002 and was appointed the chairman on 21 March 2005. He is a member of the remuneration and employment committee, and the audit committee since 1 April 2010. He is also a company director of the Thrombosis Research Institute.

Peter Martin
Peter Martin was appointed in January 2003. He is the Chairman of the audit committee. He is also the Leader of the Essex County Council.

Frederic Devos
Frederic Devos is French and was appointed a director on 31 December 2007. He is also the Chief Executive of Veolia Water UK PLC and a director of Veolia Environnement UK Limited and of other Veolia Water UK PLC subsidiaries.

Barbara Ruffell MBE (Resigned 17 November 2010)
Barbara Ruffell was appointed in April 1998. She was a member of the audit committee and chairman of the remuneration and employment committee, and was the former vice chairman of the consumer council for water central and eastern. She is a founder trustee of the British Gas Energy Trust since 2006. Barbara resigned as a Director of VWE on the 17th November 2010.

Jean Claude Banon (Resigned 31 December 2010)
Jean Claude Banon is French and has been a long serving Director of VWE. He resigned as a Director on the 31st December 2010.

Veolia Water East Limited

Board Committees, Executives and Advisers

Audit Committee

Peter Martin	Chairman
Barbara Ruffell	(resigned 17th November 2010)
Jeffrey Herbert	(since 1 April 2010)

Executive Management Committee

Nevil Muncaster	Chairman
Martin Henderson	Head of Operations
Graham Oliver	Head of Finance
Teresa Manning	Head of Customer Services
Frederic Devos	Managing Director of Veolia Water UK PLC
Richard Bienfait	Chief Finance Officer of Veolia Water UK (until April 2010)
Bruno Vinel	Group Financial Controller of Veolia Water UK PLC (until May 2010)
Andrew Dench	Chief Finance Officer of Veolia Water UK (from November 2010)
Reuben Shamu	Group Financial Controller UKIN (from June 2010)
Nigel Paterson	Chief Operating Officer Veolia Water UK PLC (from September 2010)

Remuneration and Employment Committee

Barbara Ruffell	Chairman (resigned 17th November 2010)
Jeffery Herbert	

Company Secretary and Registered Office

Graham Oliver
Tim Monod (Joint Secretary, appointed 20 September 2010)
Mill Hill
Mistley
Manningtree
Essex
CO11 2AZ

Registered Auditors

Ernst & Young LLP
1 More London Place
London SE1 2AF

Veolia Water East Limited

Report of the Directors

Introduction

The directors present their report and the audited statutory financial statements for the year ended 31 March 2011.

Principal activity

The company is a private limited company and holds an Instrument of Appointment issued by the Secretary of State for the Environment as a water undertaker under the Water Act 1989.

The company supplies water to a resident population of approximately 157,000 persons within an area of 352 square kilometres of north-east Essex. The continuing development of the company is referred to in the Chairman's Statement to shareholders.

Directors

The directors of the company, together with their periods of office and their biographical details, are shown on page 4.

Going concern

The company has adequate resources to meet its current operational and financial obligations, and the directors have a reasonable expectation that this will continue for the foreseeable future. This assessment is based on the consideration of the company's budgeted cash flows and long term forecasts, and related assumptions, available debt facilities, and support of the wider Veolia group. For this reason, the directors continue to adopt the going concern basis in the statutory financial statements.

Statement of directors' responsibilities

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law, the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period.

In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable UK 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, and
- be responsible for the maintenance and integrity of the website on which the financial statements have been published.

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

Report of the Directors (continued)

Business review and financial performance

This review describes our business environment, our strategies, the principal challenges and risks, and how, we performed in the year.

Business environment

We operate under a rolling 25 year licence from the Secretary of State for the Environment, Food and Rural Affairs to provide water services within our statutory area of supply, which is described in the report of the directors. The Water Services Regulation Authority (Ofwat) regulates our performance in meeting licence conditions and our principal duties under the Water Industry Act.

We are also regulated by:

- the Drinking Water Inspectorate on drinking water quality;
- the Environment Agency, who ensure proper use of water resources; and
- General business regulators, including the Health and Safety Executive.

Ofwat sets price limits every five years reflecting what it considers the company needs to charge to finance its services to customers. Limits were set in November 2009 for the AMP 5 April 2010 to March 2015.

Although the water industry appears to be a natural monopoly, some competition does exist. Customers using over 50 million litres of water a year are entitled to switch supplier and there is competition to supply new developments. From 1 April 2010 this limit has changed such that any customer using over 5 million litres of water a year is able to switch supplier. New entrants can now apply for licences.

Strategy

Our strategy is to concentrate on our core activity of regulated water supply, improving our returns through efficient service to customers. Our central aim is to provide a reliable and sustainable service for present and future customers, delivered through affordable, high quality, water efficient service

We take a long-term view which is consistent with the timeframe of our rolling licence (25 years), water resource plans (25 years) and five yearly periods for price setting.

Our business is highly capital intensive, delivering water to customers through a system of reservoirs, boreholes, treatment plant and pipe networks. All these assets have a total replacement cost of £291m. Some of these assets last for over 100 years.

We measure their serviceability on a regular basis and promote sensible, long-term approaches to asset replacement and renewal in our plans submitted to regulators.

We currently provide reliable high quality and predictable performance to all of our stakeholders. Our strategy for the period to 2015 is to maintain these standards and performance within a framework that is affordable to customers. We are currently focussing our attention on improving the qualitative aspects of our performance and on maintaining the asset stock, both above and below ground. This will ensure that the achievements made to date are sustained in the years to come.

Veolia Water East Limited

Report of the Directors (continued)

Challenges, risks, and opportunities

In November 2009 Ofwat announced their final determination on our plan, which was accepted by the Board on the 21st January 2010.

We have just completed the first year of the new AMP and our performance has been reasonably successful. We have achieved most of the targets set by our determination however our financial performance has been poor, in particular turnover is 3.1% down on last year and 3% down on the determination. Some of this shortfall in turnover may be recoverable in the next Asset Management Plan period through the revenue correction mechanism, a potential opportunity that will now be explored.

Performance for the year ended 31 March 2011

Financially, our performance during the year ended 31 March 2011 was poor. Operationally we have delivered a high standard of service, and we continue to perform strongly against the regulatory performance indicators. The majority of these performance measures run to 31 March, in parallel with both the statutory and the regulatory year, and these will be reported extensively in the 2011 June Return submission to Ofwat.

- The amount of water pumped into supply during the period at 28.96 megalitres/day (Ml/d) is 0.7 Ml/day lower than the level for 2009/2010 (29.66 Ml/d).

- Water quality data is reported to the Drinking Water Inspectorate. The Inspectorate assesses water company performance using a number of indices. The main parameter that reflects the quality of water delivered to our customers is 'mean zonal compliance', and is derived from a number of determinands measured in samples taken from customers' taps. In 2010 the company achieved 100% mean zonal compliance from 2,634 determinands (2009: 99.97% from 2,764 determinands).

- The free optional metering scheme has continued and during the year the company fitted 826 free meters. At 31 March 2011, 73.4% of total domestic customers connected were metered (2010: 72.2%).

- We operated throughout the year without applying any restrictions on the use of water by our customers.

Financial performance for the year ended 31 March 2011

Operating profit

Our financial performance to 31st March 2011, as reported, looks disappointing in comparison to the previous year. Appointed operating profit before asset disposals being £3.953m compared with £5.446m in 2009/10, a decrease of 27.4%. However, the results for the current year include depreciation on revalued assets which increased operating expenses by £0.632m. On a comparative basis, excluding this extra depreciation, appointed operating profit before asset disposals would have been £4.585m which is still 15.8% below the prior year.

Report of the Directors (continued)

Financial performance for the year ended 31 March 2011 (continued)

Taxation

The tax charge of £0.581m for the year is at an effective tax rate of 20.0% compared to £1.521m at 27.3% in 2009/10. The low effective tax rate in 2010/11 is due to the reduction in the rate of corporation tax. The full reconciliation, including prior year adjustments and timing adjustments, appears in note 10 to the accounts on page 31.

Cash flow

There was a net cash inflow before financing in the year of £0.329m reflecting substantial decrease in capital expenditure compared to prior year, offset by impact on costs from revaluation of assets.

Net debt decreased to £13.434m at the end of March 2011 compared to £13.763m at the end of March 2010.

Capital expenditure

During 2010/11 £1.957m was invested in fixed assets compared to £4.908m in 2009/10, of which £1.396m was to renew underground infrastructure (2009/10: £2.468m). This amount was reduced by £0.185m (2009/10: £0.265m) of capital expenditure, which was funded by third party contributions. Disposals included £0.962m revaluation element, mainly contributing to the loss on disposal of assets in the year of £0.372m.

Financial instruments

The company finances its operations through a mixture of retained profits, bank borrowings and borrowings from the parent company. Treasury policies are agreed in conjunction with the parent company (including liquidity and interest rate risks). The company does not undertake speculative transactions. Interest rate exposure is managed by using a mixture of fixed and floating rate borrowings. Liquidity is managed by utilisation of a mixture of bank overdrafts and short-term borrowings from the immediate parent company.

Capital finance

A new three year intra group loan agreement was agreed on 1 April 2009, with a maximum loan facility of £13.0m. This facility will expire on 31 March 2012. Although the loan expires in one year from 31st March 2011 it will be immediately renewed and therefore in these accounts it has been classified as a long-term liability thereby not distorting the level of debt.

Pensions

In July 2010, the government announced that it would, in future, use the Consumer Price Index (CPI) rather than the Retail Price Index (RPI) as the basis for determining the statutory minimum percentage increase for revaluation and indexation of pensions paid from private sector occupational pension schemes. The CPI basis has therefore been used for the calculation of pension scheme related amounts as indicated in Note 25, with the change being treated as an actuarial gain in the benefit obligation reconciliation, and resulting in a significant decrease in the overall obligation at 31 March 2011.

Dividend policy

The dividend policy aims to remunerate the ordinary equity share holder with a return that is broadly in line with the equity return allowed by Ofwat in the cost of capital assumption from the final determination for the AMP.

The dividend reflects a yield and a real growth consistent with the return on equity allowed by Ofwat in the determination for the current AMP, where yield is defined as the return on equity less the level of real growth in annual dividends.

Report of the Directors (continued)

Financial performance for the year ended 31 March 2011 (continued)

This policy ensures that financial capital in real terms is not reduced, the ability to finance our regulated business is not impaired and we are rewarding efficiency and the management of economic risk. It is felt that this represents a sustainable approach.

The directors have declared and paid the following dividends during the year ended 31 March 2011:

Ordinary dividends:	**£000**
Interim – paid June 2010	2,644
Interim – paid December 2010	1,432
	4,076

Employees

Communication and participation is a central theme to maintaining the employee relationship throughout the company. The company's policy is to consult both formally and informally, on matters that affect employees, through the Joint Staff Consultative Committee and through a planned system of team briefings and other meetings.

We continued to place the highest priority on health and safety, and this subject remains the first agenda item at our Board meetings and monthly management meetings.

We maintained our focus on Health and Safety following the introduction of our Zero Accidents target in 2009. Performance was slightly worse than the previous year but we are continuing to develop a strong safety culture in all that we do. Further to this we maintain a high level of training in health and safety matters to underpin our commitment to Zero accidents.

In the year ended 31 March 2011 the number of recorded accidents was 9 (2010: 5), and the number of days lost to accidents was 23 (2010: 15). We continue to review the circumstances around any accidents or incidents and where appropriate we will amend our practices and procedures accordingly.

The total number of days lost in the year due to sickness, accidents and occupational ill-health was 665 days, which was a deterioration over the previous year (2009/10: 508).

We are currently working towards the implementation of procedures to the requirements of the health and safety standard OHSAS 18001, and we plan to achieve certification for this standard by the end of 2011.

Donations and political contributions

The Company continues to make donations, largely to water-related and local organisations which aim to:

- improve opportunities and create worthwhile experiences for the disadvantaged
- improve the quality of life of senior citizens and the vulnerable within our community and
- educate young people about water and sustainability issues.

Donations are funded through operating expenditure and in 2010/11 £13k was contributed to the Veolia Water Trust Fund. The Veolia Water Trust fund is a charitable fund with a board of trustees, administered by Charis Grants Limited.

No political contributions were made during the year.

Veolia Water East Limited

Report of the Directors (continued)

Creditor payment policy

The company recognises the importance of having a reasonable payment policy with its suppliers to:

- settle the terms of payment with those suppliers when agreeing the terms of each transaction;
- ensure that those suppliers are made aware of the terms of payment by inclusion of the relevant terms in contracts; and
- pay in accordance with its contractual and other legal obligations.

The payment policy applies to all payments to creditors for revenue and capital supplies of goods and services without exception.

Post balance sheet events

The Company has granted a three year option to Scott Properties for the purchase of the entire Bockings Elm site for £3m. If the option is exercised then the depot currently situated at Bockings Elm will have to be relocated to an alternative site.

Disclosure of information to auditors

So far as each person who was a director at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing its report, of which the auditor is unaware. Having made enquiries of fellow directors and the company's auditor, each director has taken all the steps that he or she is obliged to take as a director in order to make himself or herself aware of any relevant audit information and to establish that the auditor is aware of that information.

Auditors

In accordance with Section 485 of the Companies Act 2006, a resolution to re-appoint the auditors, Ernst & Young LLP, will be proposed at the annual general meeting.

By order of the Board

Nevil Muncaster
Managing Director
24 June 2011

Corporate governance report

Introduction

Although the company is a subsidiary, the business is conducted as if it was a separate public company and particular regard is given to the Principles of Good Governance and Code of Best Practise set out in the Combined Code. The company has adopted the provisions of the Combined Code as far as possible in relation to a wholly owned subsidiary.

The exceptions to the Code are explained in more detail below.

The Board

The full board met four times during the year. It determines the overall strategy of the company and approves strategic plans, regulatory matters, major items of capital expenditure and significant financing matters. There is a procedure in place for any director to take independent professional advice where necessary to best perform their duties.

The shareholders make appointments to the Board. Certain Board members are also directors of other group companies. This enables them to bring a wide experience of related industries during discussions at meetings and on other occasions. All directors declare their position when a conflict of interest may arise.

All directors have access to the advice and services of the Company Secretary, who is responsible for ensuring that the Board and its committees are provided with papers of sufficient quality to enable the directors to consider matters in good time for meetings and enable them to discharge their duties effectively. Only the Board as a whole can remove the Company Secretary. The Company Secretary is also responsible to ensuring that every director received appropriate training, both on appointment and subsequently as necessary.

Board composition and independence

The Board comprises of an executive director and three non-executive directors at 31 March 2011. Brief biographies of the directors may be found on page 4. The directors consider that the present composition of the Board continues to provide an appropriate balance for the current size of the company. The roles of the Chairman and the Managing Director are not exercised by the same individual and are clearly defined. The role of the Chairman is undertaken by Jeffrey Herbert who is a non-executive and a non-group director and is considered to be independent under the provisions of the Combined Code

The Combined Code requires at least one third of the Board to be non-executive directors, the majority of whom should be independent. The directors consider Jeffrey Herbert and Peter Martin to be independent and together they represent two out of three of the non-executive directors. The non-executive directors do not have business relationships that would interfere with their independent judgement.

Non-executive directors are appointed for three-year terms. Their normal retirement age is 70. The requirements of the company's articles result in each director being reappointed every three years in rotation. Those directors over 70 years of age are re-appointed every twelve months.

Board Processes

The Board operates an Audit Committee and a Remuneration and Employment Committee. The Combined Code suggests that a Nominations Committee be established. However, it is the view of the Board that a Nominations Committee is not required, as the Board performs this function. The members of each Committee are listed on page 5. Each of the Board's committees operates within defined terms of reference. Minutes of the committee meetings are presented to the full Board.
All arrangements regarding the appointment or removal of directors are settled in accordance with the Articles of Association.

Corporate governance report (continued)

Audit Committee

The Audit Committee comprises two non-executive directors of the Company. Peter Martin chairs the Committee, which normally meets three times a year. The Board considers the majority of the committee members to be independent in accordance with the Combined Code. The Managing Director, Head of Finance, Veolia Water UK representatives, Group Internal Auditors, Reporter and external auditors attend the meetings as appropriate. Separate meetings with the external auditors also occur without management present.

The Committee is responsible to the Board for reviewing the effectiveness and integrity of the system of internal control that safeguard the shareholder's investment and the company's assets. It receives reports from management and auditors concerning the system of internal control and any material control weaknesses. The review also covers the risk policy and management and significant risk issues are referred to the Board for consideration.

Discussions are held with the external auditor before audits commence, and once the work is completed, to establish the nature and scope of the audit work, its cost effectiveness, the auditors' independence and objectivity and the results of the audit work.

The Committee keeps under review the level of audit fees, the appointment, re-appointment or removal of the external auditors, and the nature and extent of other services provided by them, seeking to balance the maintenance of objectivity with value for money.

The Committee reviews the company's annual financial statements prior to submission to the Board to ensure that the Report and Accounts are balanced and fair and conform to accounting standards.

The Committee adopts the same policy as Veolia Water UK PLC for the engagement of external auditors to supply non-audit services.

Executive Management Committee

The Executive Management Committee membership is shown on page 5. The committee meets regularly (typically monthly) and its duties are to consider certain strategic, financial, operational and regulatory matters delegated by the Board.

Remuneration and Employment Committee

The Remuneration and Employment Committee currently consists of only one non-executive director as Barbara Ruffell resigned as a director in 2010. The Committee meets as required, and Director of Human Resources of Veolia Water UK PLC attends by invitation. The Board considers the committee members to be independent in accordance with the Combined Code. The Committee reviews and provides advice on the remuneration and benefits packages of the senior executives. Members of the Committee are excluded from discussions regarding their own remuneration and conditions of employment. Remuneration of non-executive directors is set in accordance with the Articles of Association.

Senior executives may be paid an annual bonus. This is designed to reward short-term performance. It is Company policy to exclude the bonus element of remuneration from pensionable earnings. In framing its remuneration policy, the Committee has given full consideration to Section B of the Best Practice provisions annexed to the Listing Rules of the UK Listing Authority.

Corporate governance report (continued)

Attendance at meetings for year

	Board	Audit Committee	Executive Management Committee	Remuneration & Employment Committee
No. of meetings in the year	**4**	**3**	**10**	**1**
Jean-Claude Banon	1	-	-	-
Nevil Muncaster	4	3	10	-
Frederic Devos	2	-	6	-
Jeffrey Herbert	3	2	-	1
Peter Martin	4	3	-	-
Barbara Ruffell	2	2	-	1

"-" denotes non-membership of that committee.

Relationships with shareholders

The Board attaches a high priority to communications with shareholders. The Annual General Meeting is normally attended by all directors and provides an opportunity for communication with shareholders attending. Notice of the Annual General Meeting is given to shareholders at least 20 working days in advance. During the meeting the Chairman also invites questions from shareholders. The Annual General Meeting is to be held in September 2011. The resolutions to be proposed at the Annual General Meeting, together with explanatory notes, appear in the separate Notice of Annual General Meeting sent to all shareholders.

Internal control

The Board of Directors has overall responsibility for the company's system of internal control and for reviewing the effectiveness of these systems, including financial, operational and compliance controls and risk management. The systems are designed to manage rather than eliminate the risk of failure to achieve the company's business objectives and can only provide reasonable, and not absolute, assurance against material misstatement or loss. Formal policies and procedures are established and documented in key areas.

The company has complied with the Combined Code provisions on internal control throughout the year.

Risk

A formal, continuous process for identifying, evaluating and managing the significant risks faced by the company has been in place throughout the year under review and up to the date of approval of the Report and Accounts. The directors review the effectiveness of internal controls at least annually.

The company's Risk Management Committee comprises members of the company's Executive Management Committee and reports to the Audit Committee. Its purpose is to advance the application and impact of risk management within the company. During the year the Committee has met to prioritise actions for managing significant risks, reporting on progress of risk management, review internal controls, and identify and assess risks for the forthcoming year.

The company operates a number of controls to meet its needs, which are communicated through its ISO 9001:2000 Quality Systems Manual and Financial Procedures.

The company contributes to the compliance of Veolia Environnement SA with the US Sarbanes-Oxley Act, necessary under the terms of Veolia's listing on the New York Stock Exchange.

Veolia Water East Limited

Corporate governance report (continued)

In addition, the Board approves the company's annual budget and annual capital expenditure budget and regularly reviews actual performance. There is a defined organisational structure with appropriate delegation of authorities to line management and all major transactions are reviewed and approved by the Board as a whole.

By order of the Board

Nevil Muncaster
Managing Director
24 June 2011

Veolia Water East Limited

Remuneration report

Introduction

The Board has a Remuneration and Employment Committee; the members are listed on page 5. All arrangements regarding the appointment of directors are settled in accordance with the Articles of Association.

The Remuneration & Employment Committee provides advice to the Board on the remuneration of the executive director and the senior management team. The Committee comprises:

Barbara Ruffell (Chairman) (resigned 17 November 2010)
Jeffrey Herbert

Basic Salary
The Committee aims to set a basic salary level for the Managing Director that it feels is sufficient to retain the director but is not excessive given our market position and the regulated nature of our business. Basic salaries are normally set at levels at or just below the medium level for comparable positions in other market sector companies. In setting the basic salary level for the executive director the following factors are taken into account:

- Relevant market data of comparable positions (with regard to both responsibility and size of organisation).
- The individual performance of each executive director along with their progression within their appropriate pay structure.
- The general trends and levels of remuneration within the company ensuring that executive directors continue to be rewarded and motivated at an appropriate level in comparison to their colleagues.

Bonus Schemes
The Managing Director and the senior management team participate in bonus schemes that are designed to ensure their full focus is on the key strategic requirements of the Company. The bonus schemes have been operating since 2002.

The Remuneration and Employment Committee determines the level of bonus awarded to the Managing Director and each member of the senior management team.

The Committee takes into account, among other things, the measurements and reports provided by Ofwat which cover the performance of the Company against the key measures of customer service, leakage and the company's annual financial performance. The bonus scheme has been designed to encourage overachievement of the key targets against the following measures:

- Earnings before interest and tax (EBIT) and capital expenditure in comparison with the Company plan.
- Performance by the company against regulatory and customer service standards. Achievement of individual performance targets set for each executive director in respect of the year in relation to the improvement of the business.

At the end of the year the results of the company and the performance of the Managing Director is carefully considered by the Committee and a non-pensionable bonus, if any, awarded. There is no long term incentive plan.

Remuneration report (continued)

Other Benefits
A package of other benefits is offered to the Managing Director which is in line with market practice. This includes membership of a private health scheme and a fully expensed company car or car allowance. The level of car corresponds to the medium level on offer by comparative organisations.

Share Options
Share options are occasionally awarded by the parent company, Veolia Environnement SA, against a broad range of criteria including:

- Seniority
- Performance of the company
- The contribution of the executive director to the company
- Performance of Veolia Water UK PLC and Veolia Environnement SA.

Directors' notice periods

In respect of the Managing Director the notice period from the company to the Executive and from the Executive to the company is six months.

Directors' emoluments

The aggregate remuneration of non-executive directors was fixed at a maximum of £100,000 per annum at the Annual General Meeting held on 18 July 2001. Full details are provided within note 7 on page 30.

Directors' interests

There are no disclosable interests under the Companies Act 2006.
Shares held in Veolia Environnement SA are not disclosed in accordance with SI 1985/802(3).

By order of the Board

Nevil Muncaster
Managing Director
24 June 2011

Independent Auditor's Report to the Members of Veolia Water East Limited

We have audited the financial statements of Veolia Water East Limited for the year ended 31 March 2011 which comprise the profit and loss account, the balance sheet, the cash flow statement, the statement of total recognised gains and losses and the related notes 1 to 28. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As explained more fully in the Statement of directors' responsibilities set out on page 6, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

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

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2011 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements and the information given in the Corporate Governance Report set out on pages 12 to 15 with respect to internal control and risk management systems in relation to financial reporting processes and about share capital structures is consistent with the financial statements.

Independent Auditor's Report to the Members of Veolia Water East Limited (continued)

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

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

Ernst & Young LLP

Steven Dobson (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London
29 June 2011

Veolia Water East Limited

Profit and loss account
for the year ended 31 March 2011
(Registered Number 2663338)

	Note	**2011** **£000**	2010 £000
Turnover	2	14,678	15,148
Operating costs	3	(11,236)	(10,237)
Other operating income	4	511	535
Operating profit	5	3,953	5,446
(Loss) / profit on disposal of fixed assets		(372)	835
Profit on ordinary activities before interest and taxation		**3,581**	**6,281**
Bank interest receivable		-	129
Interest payable and finance charges	8	(613)	(654)
Other finance charges	9	(70)	(191)
Profit on ordinary activities before taxation		**2,898**	**5,565**
Tax on profit on ordinary activities	10	(581)	(1,521)
Profit on ordinary activities after taxation and for the financial year		**2,317**	**4,044**

All amounts relate to continuing operations.

Veolia Water East Limited

Statement of total recognised gains and losses for the year ended 31 March 2011

(Registered Number 2663338)

	Note	**2011 £000**	2010 £000
Profit for the financial year		2,317	4,044
Actuarial gain / (loss) recognised in the pension schemes	25	2,062	(1,786)
Deferred tax movement relating to actuarial gain / (loss)	25	(535)	500
Revaluation of fixed assets		-	31,235
Total recognised gains for the year	22	**3,844**	**33,993**

Veolia Water East Limited

Balance sheet
as at 31 March 2011
(Registered Number 2663338)

	Note	**2011 £000**	2010 £000
Fixed assets			
Tangible assets	12	66,063	69,324
Investment	13	1	1
		66,064	**69,325**
Current assets			
Stocks	14	267	314
Debtors	15	3,274	3,569
Cash at bank and in hand		151	87
		3,692	3,970
Creditors - amounts falling due within one year	16	(4,170)	(4,990)
Net current liabilities		**(478)**	**(1,020)**
Total assets less current liabilities		**65,586**	**68,305**
Creditors - amounts falling due after more than one year	17	(14,305)	(14,605)
Provisions for liabilities and charges	18	(2,255)	(2,772)
Deferred income	19	(61)	(74)
Net assets excluding pension liability		**48,965**	**50,854**
Net pension liability	25	(279)	(1,892)
Net assets including pension liability		**48,686**	**48,962**
Capital and reserves			
Called up share capital	20	1,174	1,174
Capital redemption reserve	21	1,500	1,500
Revaluation reserve	21	29,641	31,235
Profit and loss account	21	16,371	15,053
Shareholders' funds	22	**48,686**	**48,962**

The statutory financial statements on pages 20 to 47 have been approved by the Board of Directors and were signed on 24 June 2011 on its behalf by:

Jeffrey Herbert
Chairman

Nevil Muncaster
Managing Director

Veolia Water East Limited

Cash Flow Statement
for the year ended 31 March 2011
(Registered Number 2663338)

	Note	**2011** **£000**	2010 £000
Net cash inflow from operating activities	a	7,249	8,425
Returns on investments and servicing of finance			
Interest paid		(620)	(640)
Net cash outflow from returns on investments and servicing of finance		(620)	(640)
Taxation		(1,118)	(771)
Capital expenditure and financial investment			
Purchase of tangible fixed assets		(1,886)	(4,486)
Capital contributions		185	262
Proceeds on disposal of tangible fixed assets		639	844
Net cash outflow from capital expenditure and financial investment		(1,062)	(3,380)
Equity dividends paid to shareholders		(4,120)	(4,433)
Net cash inflow / (outflow) before financing		**329**	**(799)**
Financing			
Decrease / (increase) in short term financing		35	(442)
Loan (repaid) / advanced		(300)	1,100
Net cash (outflow) / inflow from financing		(265)	658
Increase / (decrease) in net cash	b/c	64	(141)

Notes to the Cash flow statement

a Reconciliation of operating profit to net cash inflow from operating activities

	2011 £000	2010 £000
Operating profit	3,953	5,446
Depreciation of tangible fixed assets	3,422	2,838
Amortisation of deferred credit	(13)	(14)
Decrease / (increase) in stocks	47	(87)
Decrease / (increase) in debtors	261	(209)
(Decrease) / increase in creditors	(421)	451
Net cash inflow from operating activities	7,249	8,425

b Reconciliation of net cash flow to movement in net debt

	2011 £000	2010 £000
Increase / (decrease) in cash in the year	64	(141)
(Decrease) / increase in short term financing	(35)	442
Loans repaid / (advanced)	300	(1,100)
Movement in net debt in the year	329	(799)
Net debt at the beginning of the year	(13,763)	(12,964)
Net debt at the end of the year	(13,434)	(13,763)

c Analysis of net debt

	At 1 April 2010 £000	Cash Flow £000	At 31 March 2011 £000
Net cash			
Bank	87	64	151
Debt			
Short term financing	751	(35)	716
Debt due after 1 year	(14,601)	300	(14,301)
	(13,850)	265	(13,585)
Net debt	(13,763)	329	(13,434)

Veolia Water East Limited

Notes to the financial statements for the year ended 31 March 2011

1. Statement of accounting policies

Basis of accounting

These financial statements have been prepared on the going concern basis, under the historical cost convention, as modified by the revaluation of certain tangible fixed assets described below, and in accordance with the Large and Medium-sized Companies and Groups Regulations 2008 (SI 2008/410), which forms part of the Companies Act 2006, and applicable UK accounting standards, except for the treatment of certain grants and contributions, described below.

No transactions have been recognised in respect of share based payments in the years ended 31 March 2011 and 31 March 2010 because the amounts were not material.

Use of estimates

The preparation of accounts in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the accounts and the reported amounts of revenues and expenses during the reporting period. Actual outcomes could differ from those estimates

Change of accounting policy in the prior year

The company adopts a policy of revaluing certain classes of fixed assets to market value, in accordance with the fair value provisions of FRS 15 'Tangible fixed assets'. This is a change from the previous policy, under which all fixed assets were stated at historic cost, except for the treatment of certain grants and contributions.

The impact on the prior year financial statements of this change in accounting policy was to:

- increase the net book value of land and buildings as at 31 March 2010 by £16,843,000;
- the impact of the above was an increase in the value of property, plant and equipment of £14,392,000, which was booked as an increase on cost or valuation of £14,392,000;
- recognise a credit of £31,235,000 against the revaluation reserve, representing the revaluation adjustment of £31,235,000.

The above revaluation of fixed assets incorporated changes from the final determination issued to the company on 26 November 2009.

Bad debt provisioning

The bad debt provision is calculated by applying a range of different percentages to debt of different ages. These percentages also vary between categories of debt. Higher percentages are applied to those categories of debt which are considered to be of greater risk and also to debt of greater age. The value of the debt provision is sensitive to the specific percentages applied.

Revenue recognition

Revenue is recognised in accordance with FRS 5, 'Reporting the substance of transactions', in the period in which it is earned. The company does not recognise revenue where payment is received in advance.

1. Statement of accounting policies (continued)

Revenue recognition (continued)

However, payments made in the previous period in respect of the current period will be recorded as revenue in the current period. In accordance with Application Note G of FRS 5, the company does not recognise revenue where available historic evidence indicates that the company will probably never be able to collect the revenue billed. Where relevant, this includes an estimate of the sales value of water supplied to customers between the date of the last meter reading and the period end together with unbilled waste water charges, exclusive of value added tax.

Tangible fixed assets and depreciation

FRS 15 requires fixed assets which are carried at revalued amounts to be shown at their current value at the balance sheet date. To achieve this all the tangible fixed assets are subject to a full valuation every five years with an interim valuation carried out in the third year of this cycle.

Tangible fixed assets comprise:
- Infrastructure assets - mains and associated underground pipe-work;
- Other assets - land and buildings, operational structures, fixed plant, vehicles and mobile plant.

Infrastructure assets (being mains and associated underground pipe-work) comprise a network of systems. Expenditure on infrastructure assets, including renewals, is treated 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. Disposals of infrastructure assets are calculated based on the estimated lives of the assets before they are replaced.

Depreciation is provided on all other fixed assets except freehold land and is calculated to write off their cost over their estimated useful lives on a straight-line basis. Assets acquired under finance leases are depreciated over the shorter of their useful life or the lease term. The performance of assets is continually monitored and where impairment is identified, fixed assets are written down to recoverable amount.

Tangible fixed assets are reviewed for impairment at the end of each reporting period when the estimated remaining useful economic life of the assets exceeds 50 years. Information on the condition of assets is also provided to the Regulator every five years as part of the price review mechanism.

The estimated useful lives of these assets are:

Buildings, reservoirs and towers	50-80 years
Wells and boreholes	40-60 years
Plant and machinery	3-20 years
Vehicles	3-5 years
Fixtures, fittings and other	1-10 years
Meters	15 years

Land is not depreciated.

Capital contributions

Infrastructure charges received in respect of connections to the mains network are allocated to fixed assets, surface and infrastructure, in accordance with the basis on which the charges are calculated.

Veolia Water East Limited

Notes to the financial statements
for the year ended 31 March 2011 (continued)

1. Statement of accounting policies (continued)

Capital contributions (continued)

Grants and contributions receivable relating to infrastructure assets have been deducted from the cost of tangible fixed assets. This is not in accordance with Large and Medium-sized Companies and Groups Regulations 2008 (SI 2008/410) which forms part of the Companies Act 2006, which requires tangible fixed assets to be shown at cost, and hence grants and contributions are accounted for as deferred income. This departure from the requirements of the Companies Act 2006 is, in the opinion of the directors, necessary for the financial statements to show a true and fair view as, while a provision is made for depreciation of infrastructure assets, these assets have indefinite economic lives and therefore no basis exists on which to recognise grants and contributions in the profit and loss account. The contributions received during the period are disclosed in note 12.

Capital contributions received in respect of tangible fixed assets, other than infrastructure assets, are deferred and credited to the profit and loss account by instalments over the expected useful lives of the related assets.

Leased assets

Rentals paid under operating leases are charged against profits on a straight-line basis over the life of the lease.

Deferred taxation

Deferred tax is provided, except as noted below, on timing differences that have arisen but not reversed by the balance sheet date, where the timing differences result in an obligation to pay more tax, or a right to pay less tax, in the future. Timing differences arise because of differences between the treatment of certain items for accounting and taxation purposes.

In accordance with FRS 19, deferred tax is not provided on timing differences arising from:

a revaluation gains on land and buildings, unless there is a binding agreement to sell them at the balance sheet date;
b gains on the sale of non-monetary assets, where on the basis of all available evidence it is more likely than not that the taxable gain will be rolled over into replacement assets;
c fair value adjustment gains to fixed assets and stock to uplift prices to those ruling when an acquisition is made.

Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered.

Deferred tax is measured at the tax rates that are expected to apply in the periods when the timing differences are expected to reverse, based on tax rates and law enacted or substantively enacted at the balance sheet date.

Where law or accounting standards require gains and losses to be recognised in the statement of total recognised gains and losses, the related taxation is also taken directly to the statement of total recognised gains and losses in due course.

The company has adopted a policy of discounting deferred tax assets and liabilities to reflect the time value of money. Deferred tax assets and liabilities are discounted using a discount rate equivalent to the post tax yield that could be obtained at the balance sheet date on government bonds with similar maturity dates and currencies. The increase or decrease in the discount deducted in arriving at the deferred tax balance is included in the deferred tax charge or credit in the profit and loss account.

1. Statement of accounting policies (continued)

Stocks and work in progress

Stocks are valued at the lower of cost or net realisable value after allowance for obsolete and slow moving items. In accordance with established practice in the water industry no value has been placed upon the water in reservoirs, mains or in the course of treatment. Work in progress for chargeable services is valued at cost.

Research and development

The costs of research and development are written off in the period in which they are incurred.

Pension costs

The company operates two pension schemes providing benefits based on final pensionable salary. These schemes closed to new members in April 1996 and September 2004. The assets of the scheme are held separately from those of the company.

Pension scheme assets are measured using market values. Pension scheme liabilities are measured using a projected unit method and discounted at the current rate of return on a high quality corporate bond of equivalent term to the liability.

Actuarial gains and losses are recognised in the statement of total recognised gains and losses.

For the defined contribution scheme, the company pays contributions on a contractual or voluntary basis. Contributions are expensed as incurred.

The company also has an unfunded obligation to pay pensions to former non-executive directors and employees. A provision in respect of this obligation is included within the net pension liability.

Ardleigh Reservoir

The company and Anglian Water Services Limited own the reservoir and ancillary works jointly in approximately equal shares, the company's share of the capital expenditure being included in tangible fixed assets in note 12. The reservoir is operated on behalf of both undertakings through the Ardleigh Reservoir Committee, and the company's share of the expense is included within Abstraction Licences and Bulk Purchase.

Financial instruments

Income and expenditure arising on financial instruments is recognised on an accruals basis, and credited or charged to the profit and loss in the financial period in which it arises.

2. Turnover

Turnover represents income from the supply of water and other chargeable services exclusive of VAT arising wholly within the United Kingdom. Turnover relating to unmeasured supplies comprises amounts due to the company for the accounting year.

	2011	2010
	£000	£000
Turnover by class is analysed below:		
Unmeasured supplies	3,867	3,745
Measured supplies	10,434	11,077
Non-portable water	16	-
Chargeable services	36	145
Reservation fees	325	181
	14,678	15,148

3. Operating costs

	2011	2010
	£000	£000
Resources and treatment	453	499
Network	764	688
Abstraction licences and bulk purchase	674	757
Billing and collection	1,461	1,523
Rechargeable work expenses	35	126
Rates and charges	1,146	1,164
Depreciation – non infrastructure assets	2,376	1,401
Less amortisation of capital contributions	(13)	(14)
Depreciation – infrastructure assets	1,678	1,437
Administrative expenses	2,662	2,656
	11,236	10,237

4. Other operating income

	2011	2010
	£000	£000
Non-appointed business income	511	535

5. Operating profit

	2011	2010
	£000	£000
Operating profit is stated after charging/(crediting):		
Auditor's remuneration - audit	55	47
Auditor's remuneration - regulatory returns and non-statutory audit	42	24
Operating lease rentals - other	15	20

Veolia Water East Limited

Notes to the financial statements for the year ended 31 March 2011 (continued)

6. Employees and directors

	2011 **£000**	2010 £000
Staff costs (including directors) consist of:		
Wages and salaries	2,308	2,108
Social security costs	200	183
Defined contribution pension costs	46	43
Other pension costs current service costs	291	177
	2,845	2,511

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

	2011 **Number**	2010 Number
Operations	26	27
Finance and administration	46	46
	72	73

7. Directors' emoluments

	2011 **Salary and fees** **£000**	**2011** **Benefits in kind** **£000**	**2011** **Bonus** **£000**	**2011** **Total** **£000**	**2010** **Total** **£000**
Non-executives					
Jeffrey Herbert	30.0	-	-	30.0	30.0
Frederic Devos	17.5	-	-	17.5	17.5
Jean-Claude Banon	17.5	-	-	17.5	17.5
Peter Martin	17.5	-	-	17.5	17.5
Barbara Ruffell	14.6	-	-	14.6	17.5
Executives					
Nevil Muncaster	112.0	22.6	25.0	159.6	156.8
	209.1	22.6	25.0	256.7	256.8

Pensions (defined benefits)

	Accumulated total accrued pension at 31 March 2010		Increase in accrued pension during year				Accumulated total accrued pension at 31 March 2011	
	£'000 p.a.	Transfer Value £'000	Increase net of inflation £'000 p.a.	Member contribution £'000	Transfer value of increase (net of member contributions) £'000	Total change in transfer value (net of member contributions) £'000	£'000 p.a.	Transfer Value £'000
N Muncaster	22	331	3	7	43	51	27	389

8. Interest payable and finance charges

	2011 £000	2010 £000
Interest on loan from group undertaking	613	654
	613	654

9. Other finance charges

	2011 £000	2010 £000
Expected return on pension scheme	978	748
Interest on pension scheme liabilities	(1,048)	(939)
	(70)	(191)

10. Tax on profit on ordinary activities

	2011 £000	2010 £000
Current taxation		
Current tax on profit for the year	1,199	1,258
Adjustment in respect of prior years	(101)	(22)
Current taxation	1,098	1,236
Deferred taxation		
Origination and reversal of timing differences	(37)	249
Adjustment in respect of prior years	-	23
Impact of change in tax rate	(476)	-
Increase in discounting	(4)	13
Deferred tax charge for the year	(517)	285
Tax on profit on ordinary activities	581	1,521
Current taxation reconciliation		
Profit on ordinary activities before taxation	2,898	5,565
Theoretical tax at UK corporation tax rate of 28% (2010: 28%)	811	1,558
Effects of:		
Adjustment to tax in respect of prior years	(101)	(22)
Accelerated capital allowances	41	(195)
Other short term timing differences	(4)	(54)
Other timing differences	(52)	-
Permanent differences	403	(51)
Actual current taxation charge	1,098	1,236

Notes to the financial statements for the year ended 31 March 2011 (continued)

10. Tax on profit on ordinary activities (continued)

The tax charge relating to profits on disposal of fixed assets amounts to £84,000 (2010: £234,000).

Factors that may affect future tax charges:

Changes to the UK capital allowance regime will impact the capital allowances the company can claim. Based on current capital investment plans the company expects to continue to be able to claim capital allowances in excess of depreciation in future years to similar levels to the current year.

Tax on recognised gains and losses not included in the profit and loss account (note 21):

	2011 £000	2010 £000
UK corporation tax rate of 26% (2010: 28%)		
Other deferred tax movements relating to pension schemes	535	(500)

A change in the UK main corporation tax rate from 28% to 27% was substantively enacted on 20 July 2010 and became effective from 1 April 2011. Further reductions in the UK corporation tax rate were announced in the March 2011 Budget, including an additional decrease in the main corporation tax rate to 26% effective from 1 April 2011. As a result the relevant deferred tax balances have been re-measured at 26%, as this is the rate substantively enacted at the balance sheet date.

The further reductions from 26%, which are expected to be enacted separately each year, propose to reduce the rate by 1% per annum to 23% by 1 April 2014. The changes had not been substantively enacted at the balance sheet date and, therefore, are not recognised in these financial statements.

11. Dividends

	2011 £000	2010 £000
Paid: Ordinary – first interim of 225.28p per share (2010: 224.86p)	2,644	2,639
Paid: Ordinary – second interim of 122.00p per share (2010:149.1p)	1,432	1,750
Paid: Preference – first interim of 0.5p per share (2010: 0.5p)	22	22
Paid: Preference – second interim of 0.5per share (2010: 0.5p)	22	22
	4,120	4,433

Veolia Water East Limited

Notes to the financial statements for the year ended 31 March 2011 (continued)

12. Tangible Fixed Assets

	Land, buildings, reservoirs and towers £000	Wells and bore-holes £000	Under-ground Mains £000	Meters £000	Plant and Machinery £000	Fixtures, fittings, tools and equipment £000	Vehicles £000	Assets in the course of construction £000	Total £000
Cost									
At 1 April 2010	36,209	882	45,253	1,381	13,781	5,062	684	2,225	105,477
Additions	(15)	-	1,396	28	84	235	22	207	1,957
Transfers to complete	260	-	-	-	426	1,434	-	(2,120)	-
Capital contributions	-	-	-	(185)	-	-	-	-	(185)
Disposals	(961)	(21)	-	-	(2)	(6)	(69)	-	(1,059)
At 31 March 2011	35,493	861	46,649	1,224	14,289	6,725	637	312	106,190
Depreciation									
At 1 April 2010	4,381	314	16,557	1,141	9,530	3,812	418	-	36,153
Charge for the year	395	16	1,678	42	598	605	88	-	3,422
Disposals	(2)	(6)	-	-	(2)	(6)	(64)	-	(80)
Revaluation	221	8	-	4	291	108	-	-	632
At 31 March 2011	4,995	332	18,235	1,187	10,417	4,519	442	-	40,127
Net book value									
At 31 March 2011	30,498	529	28,414	37	3,872	2,206	195	312	66,063
At 31 March 2010	31,828	568	28,696	240	4,251	1,250	266	2,225	69,324

The company's tangible fixed assets were professionally valued at 31 March 2010 by independent qualified valuers, PricewaterhouseCoopers LLP ('PwC'), a firm of independent chartered accountants. This valuation was performed in accordance with FRS 15 which requires that assets subject to a policy of revaluation should be carried at their current value. Current value is defined in FRS 15 as the lower of replacement cost and recoverable amount. The recoverable amount is further defined as the higher of Net Realisable Value ("NRV") and Value in Use ("VIU").

Having considered the above definitions of value, PwC concluded that the most reliable valuation method to determine the current value for the tangible fixed assets of a UK water company was a 2 step approach:

- Step 1: Estimating the business VIU, using a discounted cash flow ("DCF") model to determine the business enterprise value, cross-checked against the Regulatory Capital Value ("RCV"), followed by

- Step 2: Allocating the VIU of the business (less relevant working capital balances, deferred tax liabilities and other adjustments) to individual classes of tangible fixed assets.

12. Tangible Fixed Assets (continued)

Such valuations were incorporated into the financial statements with the resulting revaluation adjustments taken to the revaluation reserve. The revaluation during the year ended 31 March 2010 resulted in a total revaluation surplus of £31.235m. Deferred tax has not been not provided on timing differences arising from the revaluation of fixed assets unless, by the balance sheet date, a binding commitment to sell the asset has been entered into and it is unlikely that any gain will be rolled over.

If the revalued assets were stated on a historical cost basis, the amount would be £75.917m (2010: £74.242m).

13. Investment

	2011	2010
	£000	£000
Investment in subsidiary undertaking	1	1

The company has an investment of £572 in the shares of Water Resource Committee ("WRC"). The principal activity of WRC is to undertake projects on behalf of all water companies, aimed at the improvement of water services and water quality.

14. Stocks

	2011	2010
	£000	£000
Pipes and stores	267	314

15. Debtors

	2011	2010
	£000	£000
Due within one year		
Trade debtors	852	730
Accrual for unbilled metered customers	2,443	2,641
Receipts in advance	(1,181)	(1,145)
Amounts due from group companies	716	851
Other debtors	356	437
Prepayments and accrued income	88	55
	3,274	3,569

16. Creditors – amounts falling due within one year

	2011	2010
	£000	£000
Payments received in advance	221	200
Trade creditors	740	1,176
Capital creditors	135	712
Amounts due to group companies	1,031	1,165
Corporation tax	698	717
Other taxes and social security	81	69
Other creditors	148	42
Deferred income and accruals	1,116	909
	4,170	4,990

Amounts due to group companies include £60,000 (2010: £67,000) of interest and commitment fees payable to Veolia Water Capital Funds on group financing arrangement (see Note 28).

17. Creditors – amounts falling due after more than one year

	2011	2010
	£000	£000
4% irredeemable debenture stock	1	1
Amount due to group company	14,300	14,600
Other long term liabilities	4	4
	14,305	14,605

Notes to the financial statements for the year ended 31 March 2011 (continued)

18. Provisions for liabilities and charges

	Deferred tax £000
At 1 April 2010	2,772
Credited to the profit and loss account	(513)
Decrease in discounting utilised during the year	(4)
At 31 March 2011	2,255

Deferred tax (see note 10)

	2011 £000	2010 £000
Accelerated capital allowances	6,215	6,734
Other timing differences	(26)	(31)
Undiscounted provision for deferred tax	6,189	6,703
Discount	(3,934)	(3,931)
Discounted provision for deferred tax	2,255	2,772
Deferred tax asset on pension liability (see note 25)	(100)	(736)
Provision at the end of the year including deferred tax on pension liability	2,155	2,036

Deferred tax asset relating to pension deficit

	2011 £000	2010 £000
At 1 April	736	286
Deferred tax charged to the profit and loss account	(101)	(50)
Deferred tax charged to the statement of total recognised gains and losses:		
- on actuarial (gain) / loss	(535)	500
At 31 March	100	736

The deferred tax asset of £100,000 (2010: £736,000) has been deducted in arriving at the net pension liability on the balance sheet.

Factors that may affect future tax charges:

Based on current capital investment plans, the group expects to continue to claim capital allowances in excess of depreciation in future years at a similar level to the current year.

Reference should also be made to note 10 regarding recently proposed changes to the UK tax system.

19. Deferred income – Third party contributions

	2011 £000	2010 £000
At 1 April	74	88
Less credited to profit and loss account	(13)	(14)
At 31 March	61	74

20. Share capital

		2011 £000	2010 £000
Allotted, called up and fully paid share capital			
1,088,860	Ordinary shares of 25p each	272	272
84,770	Ordinary non voting shares of 25p each	21	21
4,456,116	Preference shares of 10p each	446	446
4,346,109	Deferred shares of 10p each	435	435
		1,174	1,174

Rights to dividends

Preference shares are entitled to a fixed cumulative 10% of the nominal value, payable half yearly on 1 November and 15 July. Deferred shares have no entitlement to dividends.

Priority and amounts receivable on a sale or winding up

In the event of liquidation or a repayment only of the capital, the surplus assets after the payment of liabilities of the company shall be applied in the following priority:

First, to the preference shareholders for any arrears, deficiencies or accruals of dividends

Secondly, to the holders of the ordinary and ordinary non-voting shares one million times the paid up capital.

Thirdly, to the holders of the preference and deferred shares, the capital paid on such shares who shall not otherwise be entitled to share in surplus assets.

The balance shall be distributed amongst the holders of the ordinary shares and the ordinary non-voting shares according to the amount paid up thereon.

Voting rights

Non-voting ordinary shareholders have the right to receive notice of but not to attend or to vote at any general meeting unless the meeting involves a variation in any rights attached to such shares.

Ordinary shareholders have the right to receive notice of, attend and vote at all general meetings.

Veolia Water East Limited

Notes to the financial statements for the year ended 31 March 2011 (continued)

21. Reserves

	Profit and loss account £000	Capital redemption reserve £000	Revaluation reserve £000
At 1 April 2010	15,053	1,500	31,235
Dividends	(4,120)	-	-
Actuarial gain recognised in the pension scheme	2,062	-	-
Movement on deferred tax relating to pension liability	(535)		-
Transfer to profit and loss account from revaluation reserve	1,594	-	(1,594)
Profit for the financial year	2,317	-	-
At 31 March 2011	16,371	1,500	29,641

Note of Historical Cost Profits and Losses

	2011 £000	2010 £000
For the year ended 31 March		
Reported profit on ordinary activities before taxation	2,898	5,565
Realisation of property revaluation gains of previous years	962	-
Difference between historical cost depreciation charge and the actual depreciation charge of the year calculated on the revalued amount	632	-
Historical cost profit on ordinary activities before taxation	**4,492**	**5,565**
Historical cost profit for the year retained after taxation	**3,911**	**4,044**

22. Reconciliation of movements in shareholders' funds

	2011 £000	2010 £000
Profit for the financial year	2,317	4,044
Other recognised gains/losses in year	1,527	29,949
Total gains recognised for the year	3,844	33,993
Less: dividends	(4,120)	(4,433)
Net reduction to shareholders' funds	(276)	29,560
Opening shareholders' funds	48,962	19,402
Closing shareholders' funds	48,686	48,962

23. Capital commitments

The directors have authorised no capital expenditure which is not provided for in the accounts.

The company has not entered into any guarantee arrangement or had legal disputes that would represent contingent liabilities at 31 March 2011, other than those provided for in these financial statements.

24. Commitments under operating leases

The company leases had annual commitments under non-cancellable operating leases as follows:

	2011 £000	2010 £000
Operating leases which expire:		
Within one year	13	19
In two to five years	12	30
	25	49

25. Pensions

Composition of the schemes:

The company operates two defined benefit pension schemes; one is the Veolia Water Supply Companies' Pension Plan and the other the Veolia UK Pension Plan.

Veolia Water Supply Companies' Pension Plan (VWSCPP)

Until 31 March 1996, the company was a member of The Water Companies' Association Pension Scheme, which provided benefits based on final pensionable pay. On 1 April 1996 the assets and liabilities of the General Utilities Plc subsidiaries which participated in the Water Companies' Association Scheme were transferred to a "mirror image" plan called Veolia Water Supply Companies Pension Plan which was closed to new members. This plan continues to provide benefits on a no less favourable basis than those previously provided for existing members of the scheme.

The most recent triennial valuation of the plan for the company, determined by an independent qualified actuary, was at 31 December 2007. The valuation was made on the "attained age" funding method. The actuarial valuation made the following assumptions:

Rate of investment return	6.85% (pre-retirement), 5.35% (post-retirement)
Rate of increase in remuneration	4.8%
Rate of pension increase	3.3%

The valuation as at 31 December 2007 stated the market valuation of the plan to be £14,500,000 with a funding level of 95%. A valuation as at 31 December 2010 will be available by the end of 2011.

Contributions to the plan over the period ended 31 March 2011 were paid by members in accordance with the rules of the plan and by the company at 45.3% of the pensionable salary.

The contributions expected to be paid in the year from the balance sheet date are £443,000 (2010: £420,000).

Veolia UK Pension Plan (VUKPP)

A new scheme was inaugurated as at 1 April 1996, the Générale des Eaux UK Retirement Benefits Scheme. This scheme was merged with the Générale des Eaux UK Pension Plan on 1 April 1998 to form the Veolia UK Pension Plan, which was open to all new staff and existing members. The scheme provides a selection of benefits based upon final pensionable pay or money purchase according to the members' wishes. The final salary section was closed to new members on 30 September 2004.

The latest formal valuation of the plan for the company, determined by an independent qualified actuary, was at 31 December 2007. The valuation was made on the "attained age" funding method. The actuarial valuation made the following assumptions:

Rate of investment return	6.75% (pre-retirement), 5.25% (post-retirement)
Rate of increase in remuneration	4.9%
Rate of pension increase	3.4%

The valuation as at 31 December 2007 stated the market valuation of the plan to be £666,000 with a funding level of 95%. A valuation as at 31 December 2010 will be available by the end of 2011.

Contributions to the Veolia UK Pension Plan over the period ended 31 March 2011 were paid by members in accordance with the rules of the plan and by the company at 37.4% of the pensionable salary.

The contributions expected to be paid in the year from the balance sheet date are £103,000 (2010: £98,000).

Non Executive Directors Pension Plan

A provision of £102,000 (2010: £107,000) was created in the year in respect of unfunded pension obligations to former employees and non executive directors of the company.

Principal assumptions

The present values of pension liabilities are estimated by discounting pension commitments, including salary growth, at an AA corporate bond yield.

In calculating the liabilities of the plan, the following financial assumptions have been used:

	2011	2010	2009
Discount rate	**5.5% pa**	5.65% pa	7.1% pa
Salary growth	**4.9% pa**	5.05% pa	4.7% pa
RPI	**3.4% pa**	3.55% pa	3.2% pa
CPI *	**2.9% pa**	-	-
VWSCPP pension-in payment increases	**2.9% pa**	3.55% pa	3.2% pa
VUKPP pension-in payment increases	**3.4% pa**	3.55% pa	3.2% pa
VWSCPP – Life expectancy for a male pensioner age 65 (yrs)	**22.2**	21.8	21.8
VWSCPP – Life expectancy for a male non-pensioner age 65 (yrs)	**25.8**	24.9	24.9
VUKPP – Life expectancy for a male pensioner age 65 (yrs)	**23.0**	22.6	22.6
VUKPP – Life expectancy for a male non-pensioner age 65 (yrs)	**26.7**	25.8	25.8

* The impact of statutory increases is now being linked to the movement in CPI rather than RPI based on legal advice received by the Trustees for, as follows:

- VWSCPP - the change applies to deferred revaluation and pension increases in payment
- VUKPP - the change applies to deferred revaluation only

Deferred pensions are revalued to retirement age in line with the CPI assumption of 2.9% per annum unless otherwise prescribed by statutory requirements or the plan rules.

The assets of the above plans are held separately to those of the company, being invested by independent fund managers.

The total pensions charge including the defined contributions scheme for the period ended 31 March 2011 was £337,000 (2010: £220,000).

Notes to the financial statements for the year ended 31 March 2011 (continued)

The assets of the scheme and the weighted average expected rate of return were:

	VWSCPP at 31 March 2011		VUKPP at 31 March 2011		VWSCPP at 31 March 2010		VUKPP at 31 March 2010	
	Value £m	Long term rate of return expected (% pa)	Value £m	Long term rate of return expected (% pa)	Value £m	Long term rate of return expected (% pa)	Value £m	Long term rate of return expected (% pa)
Equities	6.7	7.85	0.60	7.85	6.4	8.0	0.48	8.0
Bonds	5.1	5.55	0.20	5.55	4.6	5.5	0.16	5.5
Gilts/ cash	5.1	4.35	0.20	4.35	4.3	4.5	0.16	4.5
Fair value of assets	16.9		1.00		15.3		0.80	

VWSCPP – amounts for current period and previous four periods are as follows:

	Year ended 31 March 2011	Year ended 31 March 2010	Year ended 31 March 2009	15 months to 31 March 2008	Year ended 31 December 2006
Defined benefit obligation (£m)	17.0	17.6	12.8	15.4	15.4
Plan assets (£m)	16.9	15.3	11.9	13.7	14.9
Surplus/(deficit) (£m)	(0.1)	(2.3)	(0.9)	(1.7)	(0.5)
Difference between expected and actual return on plan assets: Percentage of plan assets	(5%)	19%	(21%)	(8%)	1%
Experience gains/(losses) on plan liabilities: Percentage of plan liabilities	0%	0%	(4%)	0%	0%

Veolia Water East Limited

Notes to the financial statements for the year ended 31 March 2011 (continued)

VUKPP – amounts for current period and previous four periods are as follows:

	Year ended 31 March 2011	Year ended 31 March 2010	Year ended 31 March 2009	15 months to 31 March 2008	Year ended 31 December 2006
Defined benefit obligation (£m)	**1.1**	1.0	0.6	0.8	0.7
Plan assets (£m)	**1.0**	0.8	0.5	0.6	0.5
Surplus/(deficit) (£m)	**(0.1)**	(0.2)	(0.1)	(0.2)	(0.2)
Difference between expected and actual return on plan assets:					
Percentage of plan assets	**(2%)**	24%	(39%)	(7%)	1%
Experience gains/(losses) on plan liabilities:					
Percentage of plan liabilities	**0%**	0%	(8%)	0%	0%

Reconciliation of present value of scheme liabilities:

	VWSCPP £000	**VUKPP £000**	**NED PP £000**	**Total £000**
At 1 April 2009	12,765	596	103	13,464
Current service cost	149	28	-	177
Interest cost	891	41	7	939
Actuarial (gain)/loss	4,379	427	17	4,823
Benefits paid	(626)	(84)	(20)	(730)
Contributions by scheme participants	40	11	-	51
At 31 March 2010	17,598	1,019	107	18,724
Current service cost	235	56	-	291
Interest cost	984	59	5	1,048
Actuarial (gain)/loss	(1,190)	(35)	10	(1,215)
Benefits paid	(640)	(1)	(20)	(661)
Contributions by scheme participants	38	12	-	50
At 31 March 2011	**17,025**	**1,110**	**102**	**18,237**

Veolia Water East Limited

Notes to the financial statements
for the year ended 31 March 2011 (continued)

Reconciliation of fair value of scheme assets:

	VWSCPP £000	VUKPP £000	NED PP £000	Total £000
At 1 April 2009	11,908	535	-	12,443
Contributions paid by employer	420	107	-	527
Contribution by scheme participants	40	11	-	51
Expected return on scheme assets	710	38	-	748
Actuarial gain/(loss)	2,843	194	-	3,037
Benefits paid	(626)	(84)	-	(710)
At 31 March 2010	15,295	801	-	16,096
Contributions paid by employer	429	99	-	528
Contribution by scheme participants	38	12	-	50
Expected return on scheme assets	920	58	-	978
Actuarial gain/(loss)	831	16	-	847
Benefits paid	(640)	(1)	-	(641)
At 31 March 2011	**16,873**	**985**	**-**	**17,858**
Pension liability before deferred tax	2,303	218	107	2,628
Related deferred tax	(645)	(61)	(30)	(736)
Net pension liability at 31 March 2010	1,658	157	77	1,892
Pension liability before deferred tax	152	125	102	379
Related deferred tax	(40)	(33)	(27)	(100)
Net pension liability at 31 March 2011	**112**	**92**	**75**	**279**

The amounts recognised in the profit and loss account are as follows:

	VWSCPP £000	VUKPP £000	NED PP £000	Total £000
For year ended 31 March 2010				
Current service cost	149	28	-	177
Expected return on scheme assets	(710)	(38)	-	(748)
Interest on pension scheme liabilities	891	41	7	939
Total charge	330	31	7	368
For year ended 31 March 2011				
Current service cost	235	56	-	291
Expected return on scheme assets	(920)	(58)	-	(978)
Interest on pension scheme liabilities	984	59	5	1,048
Total charge	**299**	**57**	**5**	**361**

Total actuarial gains and losses recognised in the statement of total gains and losses:

	VWSCPP £000	VUKPP £000	NED PP £000	Total £000
For year ended 31 March 2010				
Actuarial gains/(losses) on scheme assets	2,843	194	-	3,037
Actuarial gains/(losses) on scheme liabilities	(4,379)	(427)	(17)	(4,823)
Total charge	(1,536)	(233)	(17)	(1,786)
Deferred tax arising thereon	430	65	5	500
Charge after deferred tax	(1,106)	(168)	(12)	(1,286)
For year ended 31 March 2011				
Actuarial gains/(losses) on scheme assets	831	16	-	847
Actuarial gains/(losses) on scheme liabilities	1,190	35	(10)	1,215
Total credit	2,021	51	(10)	2,062
Deferred tax arising thereon	(525)	(13)	3	(535)
Credit / (charge) after deferred tax	**1,496**	**38**	**(7)**	**1,527**

Defined contributions pension scheme

The contributions made into the money purchase scheme under the Veolia UK Pension Plan (which is a defined contribution plan) were £45,500 (2010: £43,000). At the end of the year, there were no outstanding contributions (2010: NIL).

26. Billing on behalf of Anglian Water

The company bills and collects charges in respect of sewerage and infrastructure within its area on behalf of Anglian Water Services Limited. No amounts are included in the accounts in respect of uncollected sewerage and sewerage infrastructure charges at 31 March 2011 (2010: Nil).

Notes to the financial statements for the year ended 31 March 2011 (continued)

27. Ultimate parent company, controlling party and related parties

The company is a 99.23% owned subsidiary of Veolia Water Capital Funds Limited.

Veolia Water UK PLC, a company registered in England & Wales, is the parent undertaking of the smallest group to consolidate the statutory financial statements of the company. Veolia Environnement SA, a company incorporated in France, is the parent undertaking of the largest group to consolidate these statutory financial statements and is the ultimate holding and controlling company.

Copies of the group financial statements of Veolia Water UK PLC may be obtained from the Company Secretary, Veolia Water UK PLC, Kings Place, Fifth Floor, 90 York Way, London N1 9AG.

Copies of the accounts of Veolia Environnement SA may be obtained from the head office at 36 – 38 Avenue Kléber, 75116 Paris, France.

The company had a number of transactions with related parties, in the normal course of business, during the year. The transactions are disclosed below.

			2011		2010	
Purchases	**Nature of Relationship**	**In respect of**	**Value £'000's**	**Balance £'000's**	Value £'000's	Balance £'000s
Veolia Water UK PLC	Parent undertaking	Management and technical support, group tax relief, insurance premiums	**616**	**531**	508	488
Veolia Water Central Ltd	Common ownership	Central services recharges	**10**	**3**	163	345
Veolia Water Shared Services Ltd	Common ownership	Central services recharges	**785**	**352**	469	265
Veolia Water Southeast Ltd	Common ownership	Telemetry, payroll, regulations	**86**	**-**	41	-
Veolia Water Capital Funds Ltd	Shareholder	Financing and dividends	**4,701**	**60**	5,018	67
Veolia Environnement UK Ltd	Common ownership	Pension recharges	**3**	**1**	3	-
Ardleigh Reservoir Committee	Common ownership	Bulk purchase of treated water	**126**	**83**	373	180
Veolia Trust		Trust fund	**12**	**-**	n/a	n/a

Sales	**Nature of Relationship**	**In respect of**	**Value £'000's**	**Balance £'000's**	Value £'000's	Balance £'000s
Ardleigh Reservoir Committee	Common ownership	Administration and recharges	**9**	**9**	17	-
Veolia Water Central Ltd	Common ownership	Customer services database and other recharges	**-**	**-**	21	-
Veolia Water Southeast Ltd	Common ownership	Debt collection, joint managing director and recharges	**229**	**37**	92	87
Veolia Water Outsourcing Ltd	Common ownership	Recharges	**-**	**-**	11	13

Notes to the financial statements for the year ended 31 March 2011 (continued)

28. Financial instruments and risk management

The company's financial instruments comprise borrowings, debentures, some cash and various items, such as trade debtors and trade creditors that arise directly from operations. The main purpose of these financial instruments is to raise finance for the company's operations.

It is, and has been throughout the year under review, the company's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the company's financial instruments are interest rate risk and liquidity risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below.

The company finances its operations through a mixture of retained profits, bank borrowings and borrowings from the parent company. Treasury policies are agreed in conjunction with the parent company (including liquidity and interest rate risks). The company does not undertake speculative transactions. Interest rate exposure is managed by using a mixture of fixed and floating rate borrowings. Liquidity is managed by utilisation of a mixture of bank overdrafts and borrowings from the immediate parent company. No change is expected in the immediate future.

Financial assets

The company has no financial assets, other than short-term debtors and cash at bank.

Financial liabilities

The interest rate profile of the company's financial liabilities excluding non-debt current liabilities and deferred credits at 31 March 2011 was as follows:

As at	Total £000	Floating rate financial liabilities £000	Fixed rate financial liabilities £000
31 March 2011	14,301	7,800	6,501
31 March 2010	14,601	8,100	6,501

Interest rate for redeemable debentures is 4% (2010: 4%).

The maturity profile for the company's financial liabilities at 31 March 2011 was as follows:

	2011 £000	2010 £000
In one year or less or on demand (1)	-	-
In more than one year but not more than two years(2)	7,801	-
In more than two years but not more than five years(2)	-	8,101
In more than five years(3)	6,500	6,500
	14,301	14,601

The short term loans are repayable on demand and are classified as long-term liabilities as they are due to related parties and are not expected to be called for repayment. The company has undrawn committed borrowing facilities.

28. Financial instruments and risk management (continued)

The facilities available at 31 March 2011 in respect of which all conditions precedent had been met were as follows:

	2011 £000	2010 £000
Expiring in one year or less	-	-
Expiring in more than one year but not more than two years	5,200	4,900
	5,200	4,900

(1) Barclays base rate + 1.5% (unauthorised overdraft +3%)

(2) On 27 March 2009 a three year intra group loan agreement was approved by the Board, for a maximum loan facility of £13.0m. This facility will expire on 31 March 2012. Interest on the balance of the loan is charged at LIBOR plus 200 basis points. Commitment fee is charged on the unutilised balance at 100 basis points.
Although the loan expires in one year from 31st March 2011 it will be immediately renewed and therefore in these accounts it has been classified as a long-term liability thereby not distorting the level of debt.

(3) 15-year fixed interest rate loan agreement with Veolia Water Capital Funds Limited, the immediate parent company. Interest on the balance of the loan is charged at LIBOR plus 77.5 basis points.

Fair values of financial assets and liabilities

Other than the fixed rate liability in respect of the financing of assets by the company operated by other parties, the fair values calculated by market interest rates of the financial instruments are not materially different from book values.

Veolia Water East Limited

Operational Information Five Year Summary (Un-audited)

OPERATIONAL	Year ended 31 March 2011	Year ended 31 March 2010	Year ended 31 March 2009	15 months ended 31 March 2008	Year ended 31 December 2006
Water supplied (megalitres)					
Billed unmeasured	2,805	2,819	3,049	3,834	3,317
Billed measured	6,080	6,173	5,954	7,232	5,774
Distribution losses	1,679	1,834	1,845	2,126	1,858
Distribution input	10,564	10,826	10,848	13,192	10,949
Service Connections	73,589	73,209	72,860	72,538	71,765
Mains laid to date (kilometres)	908	907	907	908	908
Estimated Resident Population	157,000	156,000	155,000	155,000	153,600
Statutory area of supply (sq km)	352	352	352	352	352

Veolia Water East Limited

Financial Information Five Year Summary

FINANCIAL	Year ended 31 March 2011	Year ended 31 March 2010	Year ended 31 March 2009	15 months ended 31 March 2008	Year ended 31 December 2006
Summary Profit & Loss Accounts	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Turnover	14,678	15,148	14,405	17,128	14,367
Operating costs	(11,236)	(10,237)	(10,160)	(10,978)	(8,697)
Operating income	139	1,370	514	1,373	563
Profit on ordinary activities before interest & tax	3,581	6,281	4,759	7,523	6,233
Net interest	(613)	(525)	(639)	(701)	(517)
Other finance income	(70)	(191)	(59)	119	106
Profit on ordinary activities before tax	2,898	5,565	4,061	6,941	5,822
Taxation	(581)	(1,521)	(1,151)	(1,384)	(1,812)
Profit for the financial period	2,317	4,044	2,910	5,557	4,010

Balance Sheet	**£000**	**£000**	**£000**	**£000**	**£000**
Fixed assets	66,064	69,325	36,294	36,041	33,104
Current assets:					
Stocks	267	314	227	219	224
Debtors	3,274	3,569	2,919	2,724	4,362
Cash at bank and in hand	151	87	228	181	58
	3,692	3,970	3,374	3,124	4,644
Creditors – amounts falling due within one year	(4,170)	(4,990)	(3,400)	(4,075)	(5,768)
Net current liabilities	(478)	(1,020)	(26)	(951)	(1,124)
Total assets less current liabilities	65,586	68,305	36,268	35,090	31,980
Creditors – amounts falling due after one year	(14,305)	(14,605)	(13,505)	(11,403)	(9,404)
Provisions for liabilities and charges	(2,255)	(2,772)	(2,538)	(2,188)	(3,045)
Deferred income	(61)	(74)	(88)	(102)	(119)
Pension liability	(279)	(1,892)	(735)	(1,457)	(593)
Net assets	48,686	48,962	19,402	19,940	18,819
Capital and reserves					
Called up share capital	1,174	1,174	1,174	1,174	1,174
Capital redemption reserve	1,500	1,500	1,500	1,500	1,500
Profit and loss account	46,012	46,288	16,728	17,266	16,145
	48,686	48,962	19,402	19,940	18,819

VEOLIA WATER EAST LIMITED

REGULATORY FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2011

(Registered Number 2663338)

Veolia Water East Limited

Operating and financial review

The Operating and Financial Review (OFR) has been prepared in accordance with the 'Reporting Statement of Best Practice on the OFR' issued by the Accounting Standards Board modified to include certain additional information as required by Regulatory Accounting Guideline number 3.

Business Strategy and Objectives

The Company provides water supply and related services to a resident population of approximately one hundred and fifty seven thousand in an area of 352 square kilometres across the Tendring Peninsula in northeast Essex.

Business Environment

The Company is a regulated business and subject to economic regulation by the Water Services Regulation Authority (Ofwat). The business is effectively a monopoly and is subject to incentive based economic regulation which imposes caps on increases in customer prices, rewards efficiency and high standards of customer service and penalises inefficiency and poor standards of customer service.

Instruments of appointment (licenses) for the provision of water supply were awarded in 1989 and continue in force for an indefinite period subject to termination on 25 years notice with more immediate revocation in certain specific circumstances (including for example, failure to comply with an enforcement order made by Ofwat).

Water charges are capped in any year. Ofwat sets price limits every five years reflecting what it considers the company needs to charge to finance its services to customers. During a periodic review Ofwat considers the scale of the Company's capital investment programme, the cost of capital, operational and environmental obligations, and operating expenditure as well as the scope to improve efficiency.

OFWAT determines price limits by reference to the Company's income for the previous year, adjusting for inflation (headline RPI). This determination factor is known as 'k' and can be a positive or negative percentage value. The Company's regulated tariff evolves annually by RPI and 'k'.

The Water Act 2003 has extended opportunities for competition in the water industry by introducing a new framework for the licensing of water supply. From 1 December 2005 water supply licensees have been able to supply non-household users with an annual consumption of more than 50 megalitres per year. This was amended on 1 April 2010 when the limit changed such that any customer using over 5 megalitres of water per year is able to switch supplier.

In addition to the economic regulator (Ofwat), the water industry is subject to substantial domestic and European Union regulation placing significant statutory obligations on the Company with regards to, among other factors, the quality of treated water supplied.

Environmental regulation is the responsibility of the Secretary of State for the Environment, Food and Rural Affairs, together with:

- The Environment Agency responsible for conserving and redistributing water resources and securing the proper use of those resources, including the licensing of water abstraction;
- The Drinking Water Inspectorate which enforces drinking water quality standards and
- Natural England which is responsible for the protection of the natural environment

The Company expects the regulatory regimes in these areas to continue to evolve and become more mature.

Operating and financial review (continued)

Business strategy

Our strategy is to concentrate on our core activity of regulated water supply, improving our returns through efficient service to customers. Our central aim is to provide a reliable and sustainable service for present and future customers.

We take a long-term view which is consistent with the timeframe of our rolling licence (25 years), water resource plans (25 years) and five yearly periods for price setting. Our business is highly capital intensive, delivering water to customers through a system of reservoirs, boreholes, a treatment plant and pipe networks. All these assets have a total replacement cost of £291m. Some of these assets last for over 100 years. We measure their serviceability on a regular basis and promote sensible, long-term approaches to asset replacement and renewal in our plans submitted to regulators.

The Company's main objectives are to:

- Achieve and maintain a high level of health and safety performance with zero accidents
- Maintain an affordable high level of service for our customers
- Meet our commitments to our regulators and shareholders
- Develop our people
- Reduce our impact on the environment and promote water efficiency
- Continuous improvement in what we do

Future strategy

We currently provide a reliable high quality and predictable performance to all of our stakeholders. Our strategy for the period to 2015 is to maintain these standards and performance within a framework that is affordable to customers. During the five years to 2015 the Company will be focusing attention on improving the qualitative aspects of its performance and on maintaining the asset stock, both above and below ground. This will ensure that the achievements made to date are sustained in the years to come.

Consolidating our plans

We published a Strategic Direction Statement (SDS) in December 2007 which sets out the objectives for the business over the next 25 years and provides the foundation of our plans in the next regulatory period, 2010 – 2015. The document was produced after consultation with customers and stakeholders.

We wish to focus on two key principles:

- Ensuring the highest quality of service to our customers
- Improving water efficiency in all areas

Other key drivers are providing excellent customer value, continuing to minimise our impact on the environment, maximising the potential of our employees, and aiming to maximise our financial performance.

Challenges, risks, and opportunities

A Risk Management Committee comprises members of the Executive Management Committee and some specialists. Its purpose is to ensure that risk management is applied across the business as a whole, and evaluate its effectiveness.

During the period, and outside of the regular Executive Management Committee meetings, the committee has met once to prioritise actions for managing significant risks, receive reports of progress on risk management from risk owners, review internal controls, and identify and assess significant risks for the forthcoming period. The Risk Management Committee reports to the Audit Committee.

Threats to health and safety are considered separately and given the highest priority. The risk of weak operational performance during a time of crisis or emergency as a result of poor management was assessed to be the highest current risk for the company However this risk is mitigated by plans to review the crisis management plan and to carry out an exercise to determine its effectiveness.

Business operations

Water Resources

Maintaining a positive balance of supply over demand is supported by our two strand approach, promoting household metering and water efficiency.

Water Efficiency

We actively promote the efficient use of water to our customers through water efficiency advice. In 2007 we created a new post for a Water Efficiency Technician and we have since developed a range of activities for this technician which reduce customer consumption and promote water efficiency. Feedback from our customers has been very positive and we expect this role to continue and expand in future as a centrepiece to our Water Efficiency Strategy. We continue to promote water efficiency actively across our customer base.

Domestic Supplies Metering

We continued to sustain our focus on demand management through the use of water meters. During 2010-11 we continued to promote metering to our customers as the fairest way of charging for the use of water and the most effective tool for managing its overall demand. As at 31 March 2011, we had a meter penetration rate for properties in charge of 73.4% for domestic customers and 99.1% for commercial customers. This is a major contributor to our strong water balance position.

Our Strategic Direction Statement establishes metering as a key element of our future Water Efficiency Strategy. We also support metering because it is the fairest way to pay. We anticipate domestic meter penetration will continue increasing during AMP5 reaching circa 78% by 2015.

We continue to prefer meters to be sited externally because of the significant advantages this offers on controlling supply pipe leakage and providing access for reading and maintenance. However, the final choice rests with the customer and in the year 94% of meters were sited externally at the boundary of the property, which is consistent with the final determination. We continue with our policy of using remote meter reading technology in difficult access areas to improve service and ensure we are able to read all meters at all times.

No meter option customers chose to revert to the unmeasured tariff during the year. There are a small number of properties with meters fitted that are not on charge. It is our policy to use these meters for charging when there is a change of ownership.

During the year 1,613 household meters were renewed. This is below the average of circa 4,000 per annum forecast for the 2010-15 AMP5 period but the work will be accelerated using a dedicated technician to supplement the existing resources during 2011. Our replacement policy is age-based to reduce costs and reduce risk of meter inaccuracy.

Water Balance

Distribution input and water delivered during 2010-11 were lower (DI -2.3%) than 2009-10. Rainfall was slightly lower than the Long Term Average and we did not need to apply restrictions on customer use. We do not expect any water availability problems due to drought or the need to impose any water use restrictions during 2011.

Operating and financial review (continued)

We manage a well integrated distribution system that draws water from two principle sources. On average 82% of the water supplied originates from borehole sources in a confined chalk aquifer. The remaining 18% of water comes from Ardleigh Reservoir, which is a surface water source jointly owned and operated with Anglian Water.

We published our Water Resource Management Plan (WRMP) in 2009. The WRMP shows that the company has sufficient resources to beyond 2035 provided an expected increase in yield at Ardleigh in conjunction with additional raw water storage is completed by about 2025 and water usage continues to be efficient. This potential increase in raw water storage at Ardleigh is dependent on the extraction of circa 4 MT of aggregate. The operation to extract the aggregate from the site started during 2010.

Water Quality

Water quality data is reported to the Drinking Water Inspectorate. The Inspectorate assesses water company performance using a number of indices. The main parameter that reflects the quality of water delivered to our customers is 'mean zonal compliance', and is derived from a number of determinands measured in samples taken from customers' taps. In 2010 the Company achieved 100% mean zonal compliance 2,634 determinands (2009: 99.97% from 2,764 determinands).

During the year we installed and charged on 833 meters to existing domestic properties (2009-10: 902), which is in line with the final determination prediction of 3,961 for the 2010 – 2015 AMP5 period. All of these were optional meter installations.

Sustainable procurement

We operate a procurement policy which is transparent and fair and promotes a good relationship between all parties in the supply chain. The key principles set out in British Water's 'Guide to Sustainable Procurement' and in the Confederation of Construction Clients' Charter are incorporated in our procurement policy and procedures.

Corporate responsibility

Approach

Our approach to corporate responsibility embraces sustainable development, ethics, traditional safety, health, quality and environmental management systems, and corporate governance. We define corporate responsibility as the means by which we fulfil our obligations to our stakeholders, with whom we engage regularly, thereby ensuring that we identify and respond to their individual needs. We seek to excel in our relations with regulators, our parent company, employees and other stakeholders and are active in local communities. This annual report and accounts includes a separate report on corporate governance.

Parent company

Our ultimate parent, Veolia Environnement SA, is the world's largest environmental services group. Veolia Water, one of the four divisions of Veolia Environnement SA, is the world leader in water and wastewater services. Veolia Water UK PLC comprises Veolia Water East Limited, two other regulated water companies and a number of non-regulated businesses.

Veolia Environnement operates to high standards of corporate governance with charters for ethics and sustainable development. It is listed in a number of socially responsible indices, including FTSE4Good. For more details please visit the website www.veoliaenvironnement.com. Along with all Veolia Environnement business entities we continue to strengthen our compliance with the US Sarbanes-Oxley Act. This further improves our financial control and risk environment.

Risk

Our business strategies are based on corporate responsibility which is in turn underpinned by risk management. As a provider of an essential service where quality is paramount, we take our responsibility to manage risks most seriously.

We have a system to identify risks on a regular basis using a methodology that separately assesses their likelihood and severity. Control measures are put in place to mitigate and minimise the risks. Risk management is the responsibility of the Audit Committee, and managed at functional level by the Executive Management Committee.

Annual Corporate Responsibility Report

Our performance is captured in the Corporate Responsibility Report of Veolia Water UK. This document is available on our website at www.veoliawater.co.uk.

Environmental Policy and Strategy

We are committed to managing our environmental impacts, and balancing this with the need to provide customers with top quality drinking water. This is achieved through compliance with relevant environmental legislation and regulations, prevention of pollution and continual improvement of performance. These commitments are achieved by adoption of a number of principles, details of which are available in the Corporate Responsibility Report.

Our Employees and the local Community

The company aims to ensure that each employee or applicant for employment receives the same treatment irrespective of race, gender, disability, sexual orientation, religious beliefs, creed, marital or parental status. This extends through all company policies including recruitment.

The health and safety of our employees is of paramount importance and we continually train and remind our staff of the importance of working safely.

The Company is responsible for ensuring the safety and security of the general public as a result of activities that the Company carries out in the community.

We have set five key areas to target zero performance: zero harm; zero water quality failures; zero complaints; zero interruptions to supply and zero variance to budget. An annual incentive scheme is operated which rewards all employees for performance against these values: zero accidents; a reduction in customer complaints against the set target; a reduction in supply interruptions against a set target; a top three ranking in quarterly consumer experience satisfaction surveys; zero adverse variance to budgeted profit. Performance against the first four criteria is measured quarterly for bonus purposes, the fifth is an annual measurement.

Communication and participation is a central theme to maintaining the employee relationship throughout the company. The company's policy is to consult both formally and informally, on matters that affect employees, through the Joint Staff Consultative Committee and through a planned system of team briefings and other meetings.

Operating and financial review (continued)

Health and safety

Our focus on health and safety remains our highest priority. We introduced our Zero Accidents target in 2009, and we continue to monitor our performance against this objective. Our results for 2010/11 indicate deterioration in our performance compared with the previous year, and our campaign on health and safety awareness has been stepped up as a consequence. We believe that we are creating a strong safety culture in all that we do throughout the Company, thereby providing a far safer working environment for all of our employees.

We strongly believe that an effective safety culture has to be led from the top. Consequently, health and safety remains the first agenda item at our Board meetings and monthly management meetings, and is also the first item on the agenda for team briefings.

In 2010/11 there was one accident which was required to be reported under the RIDDOR regulations. This compares with one RIDDOR reportable accident in 2009/10 and eight in 2008/09. Total accidents in 2010/11 amounted to nine which was a significant increase over the prior year total of five. There were twenty three days lost to accidents and occupational health incidents during 2010/11, which is an increase in comparison with the eleven days lost during 2009/10. We are not satisfied with this performance particularly as once again one of our employees has suffered a reportable accident this year. Activity on health and safety awareness has been stepped up and greater encouragement has placed on employees reporting near misses. Our target remains zero accidents and a safe working environment for all of our employees.

Our health and safety strategy contains a number of key aspects which include a clear and consistent safety message, monthly briefings to all staff on safety with a new theme for each month, monthly safety visits by the senior management team of the Company covering all operational locations and regular feedback to all employees on our progress towards our goal of zero accidents.

In 2010/11 we have continued the development of our health and safety management system towards it being is certified to the OHSAS18001 standard. The first stage assessment of the system took place on the 31st May 2011 and the second stage is planned for mid July 2011. If we are successful we should achieve certification soon after the second stage assessment. There will then be continual surveillance visits (usually once a year) by our auditors to ensure that the system is maintained and continues to be effective.

Directors' pay

Basic Salary

The Remuneration Committee sets a basic salary level for the Managing Director that it feels is sufficient to retain the director but is not excessive given our market position and the regulated nature of our business. Basic salaries are normally set at levels at or just below the medium level for comparable positions in other market sector companies. In setting the basic salary level for the executive director the following factors are taken into account:

- Relevant market data of comparable positions (with regard to both responsibility and size of organisation) as provided in an independent survey.
- The individual performance of the Managing Director along with their progression within an appropriate pay structure.

- The general trends and levels of remuneration within the company ensuring that executive directors continue to be rewarded and motivated at an appropriate level in comparison to their colleagues.

Operating and financial review (continued)

Bonus Scheme

The Managing Director participates in a bonus scheme that is designed to ensure his full focus is on the key strategic requirements of the Company. The bonus scheme has been operating since 2002.

The Remuneration and Employment Committee determines the level of bonus awarded to the Managing Director.

The Committee takes into account, among other things, the measurements and reports provided by Ofwat which cover the performance of the Company against the key measures of customer service, leakage and the company's annual financial performance. The bonus scheme has been designed to encourage overachievement of the key targets against the following measures:

- Earnings before interest and tax (EBIT) and capital expenditure in comparison with the Company plan.
- Performance by the company against regulatory and customer service standards.
- Achievement of individual performance targets set for each executive director in respect of the year in relation to the improvement of the business.

Current Performance

Service Incentive Mechamism (SIM) and Standards of Service

We welcome the introduction of Ofwat's new performance measure for customers, the Service Incentive Mechanism (SIM). SIM is a qualitative measure, founded on customer feedback. We have continued to improve our customer and operational processes and anticipate that we will remain in the top ranks for our high quality customer service for the past year. This is supported by our top of industry position for customer satisfaction in 2010/11 following Ofwat's quarterly surveys.

In line with our objective of delivering a high quality service we have once more maintained high standards in all the historic regulatory performance indicators. The key statistics were:

- No properties at risk of receiving low water pressure (09/10: none)
- Only 9 properties experienced an unplanned interruption of more than 6 hours (09/10: 47)
- No restrictions on the use of water (09/10: none)
- 100% of billing contacts dealt with in 5 days or less (09/10: 100%)
- 100% of written complaints dealt with in 10 days or less (09/10: 100%)
- 100% of metered accounts based on an actual reading (09/10: 100%)
- 0% of customers calling experienced the engaged tone (09/10: 0%)
- 1.8% of customers calling abandoned the call (09/10: 3.8%)

9 properties experienced an interruption of more than 6 hours. Our priority is restoring the water supply to our customers before making any repairs to a water main. Changing focus from repair to restoration of supply has improved the service to customers despite increased bursts during a second severe winter.
Overall contact with customers speaking to an advisor was 10% lower than the previous year. The decrease was achieved through improvements to our processes and taking a more proactive approach to keeping customers informed about their billing or operational enquiry or issue. We have challenged and supported both our office based and operational teams to work better together in order to deliver a 'customer first' service. We introduced customer satisfaction surveys for our front line teams to understand what we can do better and used the valuable feedback to make improvements.

'Unwanted' contacts are where the caller has experienced some form of aggravation (however mild) and this has prompted them to make contact. Of the 70,182 calls received in the period 7,174 or 10% were

Operating and financial review (continued)

categorised as unwanted, a reduction of 39% on the previous year (2009-10: 78,309 and 11,682 or 15%). The reduction is attributed to improvements we have made together with improved reporting capability.

We received 152 written complaints, a decrease of 20% on 2009-10 (191). The number of second-stage complaints has reduced by 65% to 7 (2009-10: 20). This has been achieved through the improvements we have made to processes to ensure first time resolutions and adopting a more pragmatic and understanding approach. The number of debt recovery related complaints received was 34, which is consistent with 2009-10 (35). Customers are either unhappy about receiving final demands or complain as a payment avoidance tactic. Of the 152 complaints received 22% related to customers in debt. The proportion of measured complaints was 69% (2009-10: 71%) and the proportion of unmeasured complaints was 30% (2009-10: 27%).

All complaints were dealt with within 10 working days.

The national annual survey score for our customers on call handling satisfaction was 4.59 (1st in the industry), compared with 4.74 last year (6th in the industry). We achieved the highest score for our handling of operational contacts and the 3rd highest score for our handling of billing contacts. The 'after service' calls we introduced for operational visits have clearly contributed to increased levels of customer satisfaction.

Severe weather conditions

Steps were taken in September 2010 to ensure we did not experience the same difficulties as the previous year with staff not being able to get to work during periods of severe weather. Functionality within the internet based telephony system allowed the majority of our contact team to take calls from their homes, in addition, they were given access to the billing system via their own laptop or PC. This enabled us to maintain service levels to our customers as well as reduce risk to our staff.

Non-Financial Performance

Levels of Customer Service

The following levels of service relate to the historic standards established by Ofwat and which are still being maintained:

	2007/8	2008/9	2009/10	2010/11
DG2 Pressure of mains water				
Percentage of properties not at risk of receiving water below a pressure of 15m head at the stop tap or meter	100.0%	100.0%	100.0%	100.0%
DG3 Interruptions to supply				
Number of properties not experiencing an unplanned interruption to supply for more than 12 hours	100.0%	100.0%	99.95%	100.0%
DG4 Water use restrictions				
Percentage of properties not affected by hosepipe ban or drought order	100.0%	100.0%	100.0%	100.0%
DG6 Response to billing contacts Percentage of billing contacts responded to within 5 days	100.0%	100.0%	100.0%	100.0%
DG7 Response to written complaints				
Percentage of written complaints responded to within 10 days	100.0%	100.0%	100.0%	100.0%
DG8 Billing of metered customers Percentage of customers who receive bills for metered accounts during the year based upon actual readings and not estimates	100.0%	100.0%	100.0%	100.0%
DG9 Telephone Contacts				
Percentage of customers who abandoned calls	0.80%	0.75%	3.81%	1.8%

Veolia Water East Limited

Operating and financial review (continued)

Drinking water quality outputs

The Annual Report of the Drinking Water Inspectorate (DWI) for 2010 will continue to confirm a high level of water quality compliance, with mean zonal compliance of 100% (2009: 99.97%). Mean zonal compliance at the tap for iron was 100% (2009: 100%). We also expect the Operational Performance Index for both the 3-parameter and 6-parameter measures to be 100%, which would be for the 8th year in succession.

In response to deterioration in water quality samples taken from a customer tap in Clacton on Sea in August 2010 the company notified DWI and were required to submit a 3-day event report. Following mains repair work near a broken foul sewer a bacteriological sample failed and precautionary boil notices were issued to 7 customers who were potentially affected. Further sampling showed that the failure was likely to be property specific and unrelated to the repair work. The DWI classified the event as minor and did not require a 20 day report.

No quality related capital expenditure was planned or carried out during the year. This is consistent with the 2009 final determination.

In 2009 we gave a water quality undertaking to the DWI in respect of our surface water source at Ardleigh WTW for metaldehyde, clopyralid and total pesticides. The Undertaking requires us to eliminate exceedances for single pesticides by improving pesticide usage control through catchment management. Some pesticides notably metaldehyde (used to control slugs) and clopyralid (used to control broad leaved weeds) are not readily removed by the available treatment processes at Ardleigh. The AMP5 period includes modest operating cost expenditure for this activity and although the risk of failure remains, none occurred during 2010. The joint approach between companies, the Environment Agency and farming organisations is working well.

Leakage

	2007/8	**2008/9**	**2009/10**	**2010/11**
Leakage levels at least below the Company target of 5.10 mega litres per day	5.04	5.09	5.02	5.01

This target is set with Ofwat as part of the periodic review. It is set taking into account the operational, environmental and social costs of reducing leakage. The level of leakage reported by the Company is calculated in accordance with Ofwat guidelines and is reviewed by the Company's Reporter.

For the second consecutive year we experienced an extremely cold winter which again challenged our ability to meet our leakage target for the year. An increased focus on leakage detection, aided by newly implemented L'Mars leakage management software helped us to achieve our target.

Total leakage at 5.01 Ml/d was within the 5.10 Ml/d target for the year. In order to achieve the target we had to increase activity on active leakage control and proactively replace some inferior copper communications pipes that had been installed in the 1970s and 1980s. This programme will be continued to replace all inferior copper communication pipes within 10 years.

We consistently achieve the lowest level of leakage in the industry (as measured in litres per property per day) which contributes to both our environmental objectives and to maintaining the security of supply to our customers. However, this low level of leakage makes it increasingly difficult to find further, cost effective, reductions in leakage and this is emphasised by the fact that our monitoring plan target of 5.10 Ml/day is below the current sustainable economic level of 5.70 Ml/d.

Serviceability Assessment

The serviceability of our infrastructure and non-infrastructure assets are confirmed as stable. The number of bursts in 2010/11 was 63, a significant reduction in the level for 2009/10 of 91, this result is against the

Operating and financial review (continued)

background of another severe winter. The number of bursts in the year is also below the reference level of 77 as set by our determination for AMP 5.

In 2010 we received a serviceability assessment from Ofwat of stable but with a caveat that this assessment would be under threat if future burst rate remained at the current level. The result for 2010/11 confirms the Company's view that both our infrastructure and non-infrastructure serviceability remains stable.

Infrastructure renewals

During the year a total of 6.75 km of water mains including 0.77km of trunk mains was renewed. The distribution main renewals were spread throughout the area of supply. A new section of trunk main was laid near Horsley Cross Pumping Station which combined with some replacement sections enhances supply resilience at the most important location within the distribution system. This completed the AMP4 scheme started in 2009-10.

We continued to replace communication pipes during 2010/11 with priority being given to replacing inferior copper pipes prone to pinhole failure. The areas where these inferior copper communication pipes were concentrated have now been completed. Remaining replacements are spread over a larger area with a consequent reduction in the number completed but an increase in the unit replacement cost compared to prior years.

In summary, once again, we are able to report that our asset stock remains in good condition and is performing satisfactorily. This has been achieved despite another winter of severe weather conditions.

Defined outputs for maintaining base service

We have one defined output for AMP 5; the construction and commissioning of a treated water reservoir and pumping station at Dovercourt near Harwich. This project is the final part of a long-term strategic plan for treated water storage which started in AMP1 and which includes the construction of two similar service reservoirs and pumping stations at Clacton which were completed during AMP4. The main benefit of this strategy is to maintain good security of supply for all customers in our major urban conurbations and contribute to our high quality customer service. By completing these reservoirs we will also have a network of reservoirs less than twenty years old, meaning that there will be no further replacement programmes on this type of asset for the foreseeable future.

The completion of the replacement service reservoir and pumping station serving Dovercourt and Harwich is planned for 2012, with construction planned to start in July 2011.

Financial Performance

The Company continues to report under UK GAAP. The accounting policies are set out in Note 1 to the Historical Cost Financial Statements.

	2007/8	2008/9	2009/10	2010/11
Return on capital (%)	9.0	7.3	9.8	6.5

Return on Capital Employed (ROCE) measures the Company's current cost operating profit as a percentage of its regulatory capital value. The return on capital calculation uses data from the financial statements. Regulatory capital values were reported by Ofwat as part of the 2009 price review and are updated each year to take account of inflation and the net new capital expenditure (after allowing for current cost depreciation) assumed at the price review.

Operating and financial review (continued)

The Company wishes to ensure it continues to be an efficient operator since this helps keep water bills for customers as low as possible. By monitoring comparative performance against the rest of the industry, the Company can inform itself as to its comparative position relative to the water industry in England and Wales.

The data is derived for this key performance indicator from Ofwat's annual report into unit costs and relative efficiency, published in December each year. This data is itself compiled by Ofwat from each water Company's annual June Return.

The target is to manage operating and maintenance costs such that the Company at least meets and where possible outperforms its target profit for the year. Its profit target is derived from internal budgeting and financial forecasting.

We are not aware of any material changes to the calculation or the definitions of the underlying data used by Ofwat to construct this indicator over the period.

Results

Our financial performance to 31st March 2011, as reported in our historic accounts, is disappointing in comparison to the previous year, appointed operating profit before asset disposals being £3.555m which is 29.4% lower than the previous year. This result includes depreciation on re-valued assets which increased operating expenses by £0.632m. On a comparative basis, excluding this extra depreciation, appointed operating profit before asset disposals is still 16.8% below the prior year. A significant cause of the poor performance is a reduction in turnover which is £0.614m down on the previous year.

The revaluation of assets also impacts the return on asset disposals which are reported as a loss of £0.372m, but increase to a historical cost profit of £0.588m if revaluation is ignored. Asset disposals in 2009/10 amounted to £0.835m.

Appointed operating profit after asset disposals is £3.183m compared with £5.868m in 2009/10, a decrease of 46%.

The 2010/11 current cost operating profit of £3.963m is also disappointing being £1.190m lower than the previous year. This includes a profit on the disposal of assets of £0.467m which is £0.379m lower than the profits from asset disposals in 2009/10.

Capital expenditure was relatively low this year at £1.957m compared with the prior year (2009/10 £4.909m), but is in line with our plans and the final determination. The principle areas of infrastructure expenditure during the year were once again ongoing distribution mains and communication pipe renewals. The main items of expenditure on non-infrastructure assets were like for like replacements. Completing the replacement of the company wide telemetry system started in 2009-10, together with other IT system replacement were the biggest single items.

Revenue

Turnover at £14.353m has fallen by £0.614m compared to the previous year (2009/10 £14.967m). Water reservation fees have been reclassified against operating costs for both years. The amount of water delivered to customers has fallen in 2010/11 by 0.76 Ml/d, unmeasured household consumption has fallen by 0.42 Ml/d while measured household consumption has risen by only 0.01 Ml/d (which includes the impact of new households and unmeasured customers switching to a metered supply during the year).

Turnover also compares badly to the FD for 2010/11, being adverse in total by £0.582m (excluding reservation fees).

Operating and financial review (continued)

Turnover (per OFWAT definition) is analysed as follows:

	2008/09	2009/10	2010/11
Prior year	13.990	14.405	14.967
Effect of RPI + k	0.530	0.355	(0.196)
(Lower)/ higher customer demand	(0.074)	0.197	(0.257)
New connections	0.052	0.026	0.043
Other	(0.093)	(0.016)	(0.204)
Current Year	**14.405**	**14.967**	**14.353**

The amount of water billed to measured household customers in 2010/11 was 10.72 Ml/d which is 0.30 Ml/d (£0.120m) below the final determination billed consumption level of 11.02 Ml/d. This, together with the impact of a lower RPI allowance in tariffs (0.3%) than the average inflation for 2010/11 (5%) and a reduction in the measured income accrual of £0.082m for a provision for bad debts, contributed to turnover being significantly lower than our determination. Some of this shortfall in turnover may be recoverable in the next AMP through the revenue correction mechanism.

Total operating expenditure

Appointed operating costs of £6.820m are £0.352m less than the previous year of £7.172m. Power costs decreased, mainly due to slightly reduced prices with consumption reasonably constant. Our debt recovery team have continued to improve recovery of outstanding debt resulting in a further reduction in bad debt expense this year. Bulk water costs have again decreased as a result of the increase in the reservation fee from Anglian Water and gains in operating efficiency.

Evolution of Operating Expenditure	**£ m**
OPEX Costs 2009/10	**7.172**
Payroll	0.090
Rates	(0.018)
Power	(0.070)
Bulk Purchase	(0.246)
Bad Debt	(0.124)
Other	0.016
OPEX Costs 2010/11	**6.820**
Change in costs	(0.352)

Infrastructure renewals charge (IRC)

The charge for the year was £1.616m (2009/10: £1.375m) which is consistent with our view of the medium to long term needs of the infrastructure asset network established in the 2009 price review for the AMP 5 period. The amount charged in 2010/11 is consistent with the level included our final determination for AMP 5.

Infrastructure renewals expenditure in the year was £1.084m which is £0.945m below the prior year figure of £2.029m and in line with the AMP 5 final determination figure.

Operating and financial review (continued)

Current cost Depreciation

Current cost depreciation has increased by £0.289m, however, inflating 2009/10 assets to 2010/11 prices account for £0.111m of this difference. Of the balance, £0.044m is CCD on 2010/11 additional assets and £0.106m from assets purchased in AMP4 but not commissioned until 2010/11.

Taxation

The total tax charge of £0.581m for the year is at an effective tax rate of 20.0% compared to £1.521m at 27.3% in 2009/10. The low effective tax rate in 2010/11 is due to the impact of both the reduction in the rate of corporation tax and the effect of timing differences on deferred tax. The full reconciliation, including prior year adjustments and timing adjustments, appears in note 10 to the statutory accounts on page 30.

Dividend policy

Our dividend policy has been agreed with our UK parent company.

The dividend policy aims to remunerate the ordinary equity share holder with a return that is broadly in line with the equity return allowed within the cost of capital assumption from the final determination for the AMP. The current policy is based on a target return on equity (regulatory capital value less net debt) of 7.1%. The policy also has regard to service performance, financial out-performance, and maintaining dividend cover. It is considered that this policy maintains financial capital and the ability to raise further capital. It also rewards efficiency, manages economic risk, and represents a sustainable approach.

Total ordinary dividends amounting to £4.076m (2009/10: £4.389m) have been paid.

Efficiencies

A number of efficiencies have been introduced during the year:

- Two vacant positions in Operations have not been filled, which is equivalent to a reduction of 3% in the workforce.
- A further 10% of the water resource available to Veolia Water East from the Ardleigh reservoir has been released to Anglian Water for the next ten years in return for an increased reservation fee.
- Veolia Water East has agreed to Anglian Water assuming responsibility for the 'day to day' management of Ardleigh Reservoir. This is achieving efficiencies that are already reducing operational costs to VWE for this source of bulk water.
- Veolia Water East has benefited from the negotiation of a contract for the supply of power across the UK group by Veolia Water Shared Services Procurement. This is resulting in a significant reduction in the level of operating expenditure.

As a result of these efficiencies, together with the efficiencies introduced at the end of AMP4, total operating expenditure in 2010/11 has decreased against the previous year by £0.352m.

2010/11 Actual Opex, in real terms, is consequently also £0.224m lower than the Final Determination for AMP5. However the final determination sets the company some tough ongoing efficiency targets, which increase cumulatively through each year of the AMP. The achievement of these future efficiency targets must be balanced against our commitment not to fail current service levels. We will continue to seek further opportunities to reduce our operating expenditure, however, this will not be achieved in a way that jeopardises our ability to provide a first class service to our customers or to deliver in full the requirements of our operating licence.

Capital expenditure

During 2010/11 £1.957m was invested in fixed assets compared to £4.908m in 2009/10, of which £1.396m was to renew underground infrastructure (2009/10: £2.468m). This amount was reduced by £0.185m (2009/10: £0.265m) of capital expenditure, which was funded by third party contributions. Disposals

Operating and financial review (continued)

included £0.962m revaluation element, mainly contributing to the loss on disposal of assets in the year of £0.372m.

Change in accounting policy for fixed assets

Last year the company changed its accounting policy for fixed assets by revaluing certain classes of fixed assets to market value in accordance with the fair value provisions of FRS 15 'Tangible fixed assets'. The increase in fair value of fixed assets resulted in a credit to a revaluation reserve of £31.235m at 31 March 2010.

Capital works activity

Capital Maintenance – Underground - Infrastructure Assets

Infrastructure expenditure for distribution mains has been similar to the average of previous years but there has been a reduction in expenditure for communication pipe replacement. Expenditure during the year on trunk main replacement was below the overall average for the AMP 5 period as major expenditure against this category is planned for 2012-13-14. We renewed 6.75 km of water main including 0.77km of trunk main during the year. In addition,1.27km of new mains including 0.17km of new trunk main were laid during the year.

We replaced 547 communication pipes, which is less than previous years. Amongst these were a large proportion made from copper of an inferior quality, which were installed during the 1970s. These have been subject to pin-hole failures resulting in increased leakage levels. We began to replace these during AMP 4 and will continue to replace during the current AMP but at a higher unit cost of doing so as areas where this material was concentrated have already been replaced. Although only involving a small total length, supply resilience has been improved by creating a trunk "ring main" for water supplied from Horsley Cross. This was identified as part of the AMP4 programme and although most expenditure was incurred in 2009-10 the scheme was completed in 2010-11.

In summary, we have made significant improvements to trunk main resilience of supply from Horsley Cross WTW while continuing to replace urban mains and communication pipes.

Capital Maintenance – Above Ground - Non-infrastructure (MNI) Assets

Expenditure during 2010-11 was less than historic averages and consisted of like-for-like replacement including work at Ardleigh which is shared with Anglian Water and other routine replacements. The biggest individual items were the completion of the company wide telemetry system replacement started in 2009-10 and other IT software. Extensive preparatory work was carried out for the replacement Service Reservoir and Pumping station at Dovercourt due to start construction in July 2011. The preparatory activity involved relatively minor expenditure.

Cash flow

There was a net cash inflow before financing in the year of £0.329m reflecting substantial decrease in capital expenditure compared to prior year.

Net debt decreased to £13.434m at the end of March 2011 compared to £13.763m at the end of March 2010.

Financing arrangements

Our aim, consistent with our risk policy, is to maintain balance sheet strength and good credit ratings and ensure that sustainable funding arrangements are in place.

Financial Instruments

The Company's financial instruments consist of borrowings, debentures, cash and various items, such as trade debtors and trade creditors that arise directly from operations. The main purpose of these financial instruments is to raise finance for the Company's operations.

Operating and financial review (continued)

The Company finances its operations through a mixture of retained profits, bank borrowings and borrowings from the immediate parent Company. Treasury policies are agreed in conjunction with the parent Company (including liquidity and interest rate risks). The Company does not undertake speculative transactions. Interest rate exposure is managed by using a mixture of fixed and floating rate borrowings. Liquidity is managed by utilisation of a mixture of bank overdrafts and short-term borrowings from the immediate parent company.

Outlook

The Company will continue to pursue its mission, strategy and priority objectives, as noted at the start of this Review.

The Company will continue to provide a reliable, sustainable and high quality service to present and future customers. We therefore take a long term view which is consistent with the timeframes of our rolling license (25 years), water resource plans (25 years) and the longevity of our network and some of our plant and equipment. We expect to continue to invest significantly in our pipe network and renew mains which suffer from high and repeated bursts. We will continue to increase household meter penetration to encourage as many of our customers as possible to use water carefully and mitigate growth in water demand.

The operating and financial review contains forward looking statements that are subject to risk factors associated with, amongst other things, the economic, business and regulatory circumstances occurring from time to time in the markets in which the Company operates. These and other factors could adversely/positively affect the customer and financial effects of the plans and events described.

Veolia Water East Limited

Certificate of compliance with licence condition F6A

To: The Chief Executive
Water Services Regulation Authority
Centre City Tower
7 Hill Street
Birmingham
B5 4UA

CERTIFICATE OF COMPLIANCE WITH LICENCE CONDITION F6A

This is to certify that, at their meeting on 20 June 2011, the directors of Veolia Water East Limited (the Appointee") resolved that in their opinion:

- The Appointee will have available to it sufficient financial resources and facilities to enable it to carry out, for at least the next 12 months, the Regulated Activities (including the investment programme necessary to fulfil the Appointee's obligations under the Appointment); and

- 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
- 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.

Nevil Muncaster
Managing Director
24 June 2011

Veolia Water East Limited

Certificate of compliance with licence condition F6A

STATEMENT OF DIRECTORS' RESPONSIBILITIES

In addition to their responsibilities to prepare financial statements in accordance with the Companies Act 2006, the directors are also responsible under Condition F of the Instrument of Appointment by the Secretary of State for the Environment, Transport and the Regions of the Company as a water undertaker as amended by the Variation and Modifications dated 18 September 2000 under the Water Industry Act 1991 for:

(a) Ensuring that proper accounting records are maintained by the Appointee to enable compliance with the requirements of Condition F and having regard also to the terms of guidelines notified by the Director General of Water Services ("the Director"), to the Appointee from time to time;

(b) Preparing on a consistent basis for each financial year accounting statements in accordance with Condition F, having regard also to the terms of guidelines notified by the Director from time to time, which so far as is reasonable practicable have the same content as the annual financial statements of the Appointee prepared under the Companies Act 2006 and which are prepared in accordance with the formats, accounting policies and principles which apply to these accounts;

(c) Preparing accounting statements on a current cost basis in respect of the same accounting period in accordance with guidelines issued by the Director from time to time or as specified under the Variation and Modifications dated 18 September 2000;

(d) Preparing such other accounting information and related information as is required by Condition F having regard also to the terms of guidelines issued by the Director from time to time.

In providing this Certificate the directors have taken into account the following:

- the Company's business plan;
- the Company's Annual Report and Accounts, which are prepared on the going concern basis;
- financial performance updates which are provided at Audit Committee and Board meetings;
- the Board's review of corporate risks.

The Chairman's Statement, Remuneration Report, Report of the Directors and Corporate Governance Report on pages 2-17 of the Statutory Accounts also apply to these Regulatory Financial Statements

Veolia Water East Limited

Compliance with condition K

CONDITION K

Compliance with Condition K

Paragraph 3.1 of the Companies Instrument of Appointment requires the Company to at all times ensure, so far as is reasonably practicable, that if a special administration order were made, it would have available to it sufficient rights and assets (other than financial reserves) to enable a special administrator to manage the affairs, business and property of the appointed business of the Company.

The Company hereby certifies that at 31 March 2011 it was in compliance with paragraph 3.1 of condition K.

Independent auditors' report

To the Water Services Regulation Authority and Directors of Veolia Water East Limited

We have audited the Regulatory Accounts of Veolia Water East Limited for the year ended 31 March 2011 on pages 72 to 92, 95 and 96 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.

These Regulatory Accounts have been prepared in accordance with the basis of preparation and accounting policies set out in the Statement of Accounting Policies.

This report is made, on terms that have been agreed, solely to the Company and the WSRA in order to meet the requirements of Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water and sewerage undertaker under the Water Industry Act 1991. 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 Condition F 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.

Respective responsibilities of the WSRA, the directors and auditors

As explained more fully in the Statement of Directors' Responsibilities set out on page 67, the directors are responsible for the preparation of the Regulatory Accounts and for their fair presentation in accordance with the basis of preparation and accounting policies. Our responsibility is to audit and express an opinion on the Regulatory Accounts in accordance with International Standards on Auditing (UK and Ireland), except as stated in the 'Scope of the audit of the Regulatory Accounts' below, and having regard to the guidance contained in Audit 05/03 'Reporting to Regulators of Regulated Entities' issued by the Institute of Chartered Accountants in England and Wales. Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the Regulatory Accounts

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

We have not assessed whether the accounting policies are appropriate to the circumstances of the Company where these are laid down by Condition F. Where Condition F does not give specific guidance on the accounting policies to be followed, our audit includes an assessment of whether the accounting policies adopted in respect of the transactions and balances required to be included in the Regulatory Accounts are consistent with those used in the preparation of the statutory financial statements of the company. Furthermore, 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 International Standards on Auditing (UK & Ireland).

Opinion on Regulatory Accounts

In our opinion, the Regulatory Accounts:

- fairly present in accordance with Condition F, the Regulatory Accounting Guidelines issued by the WSRA and the accounting policies set out on page 81, the state of the Company's affairs at 31 March 2011 on an historical cost and current cost basis, and its historical cost and current cost profit and its current cost cash flow for the year then ended; and
- have been properly prepared in accordance with Condition F, the Regulatory Accounting Guidelines and the accounting policies.

Basis of preparation

Without modifying our opinion, we draw attention to the fact that 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 and have not been prepared under the basis of United Kingdom Generally Accepted Accounting Practice ('UK GAAP'). Financial information other than that prepared on the basis of UK GAAP does not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in statutory financial statements prepared in accordance with the Companies Act 2006. Furthermore, the regulatory historical cost accounting statements on pages 72 to 74 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 Practice and a reconciliation of the balance sheet drawn up on this basis to the balance sheet drawn up under the Companies Act 2006 is given on page 91.

Opinion on other matters prescribed by Condition F

Under the terms of our contract, we have assumed responsibility to provide those additional opinions required by Condition F in relation to the accounting records. In our opinion:

- proper accounting records have been kept by the appointee as required by paragraph 3 of Condition F; and
- the Regulatory Accounts are in agreement with the accounting records and returns retained for the purpose of preparing the Regulatory Accounts.

Other matters

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

Our opinion on the Regulatory Accounts is separate from our opinion on the statutory financial statements of the Company for the year ended 31 March 2011 on which we report, which are prepared for a different purpose. Our audit report in relation to the statutory financial statements of the Company (our 'statutory audit') was made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 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 audit report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume responsibility for any other purpose or to any other person to whom our statutory audit report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Ernst & Young LLP

Steven Dobson (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London
29 June 2011

Veolia Water East Limited

Historical cost profit and loss account for the year ended 31 March 2011

	Year ended 31 March 2011			Year ended 31 March 2010		
	Appointed	**Non-Appointed**	**Total**	Appointed	Non-Appointed	Total
	£000	**£000**	**£000**	£000	£000	£000
Turnover	**14,353**	**-**	**14,353**	14,967	-	14,967
Operating costs (excluding HCD)	**(8,436)**	**(51)**	**(8,487)**	(8,547)	(59)	(8,606)
Historical cost depreciation	**(2,362)**	**-**	**(2,362)**	(1,387)	-	(1,387)
Operating income	**(372)**	**-**	**(372)**	835	-	835
Operating profit	**3,183**	**(51)**	**3,132**	5,868	(59)	5,809
Other income	**71**	**440**	**511**	1	534	535
Net interest receivable less payable	**(683)**	**-**	**(683)**	(716)	-	(716)
Profit on ordinary activities before taxation	**2,571**	**389**	**2,960**	5,153	475	5,628
Current tax	**(989)**	**(109)**	**(1,098)**	(1,126)	(133)	(1,259)
Deferred tax	**517**	**-**	**517**	(262)	-	(262)
Profit for the year	**2,099**	**280**	**2,379**	3,765	342	4,107

Turnover and Operating profit relate entirely to continuing operations.

No government grants or assistance were received by the company during the reported period.

Veolia Water East Limited

Statement of historical recognised gains and losses for the year ended 31 March 2011

	At 31 March 2011			At 31 March 2010		
	Appointed	**Non-Appointed**	**Total**	Appointed	Non-Appointed	Total
	£000	**£000**	**£000**	£000	£000	£000
Profit for the year	**2,099**	**280**	**2,379**	3,765	342	4,107
Actuarial gain / (loss) recognised in pension scheme	**2,062**	**-**	**2,062**	(1,786)	-	(1,786)
Movement on deferred tax relating to pension scheme	**(535)**	**-**	**(535)**	500	-	500
Revaluation of fixed assets	**-**	**-**	**-**	31,235	-	31,235
Total gains recognised for the year	**3,626**	**280**	**3,906**	33,714	342	34,056

Veolia Water East Limited

Historical cost balance sheet
as at 31 March 2011

	2010/11			2009/10		
	Appointed	**Non-Appointed**	**Total**	Appointed	Non-Appointed	Total
	£000	**£000**	**£000**	£000	£000	£000
Fixed assets						
Tangible fixed assets	**65,254**	**-**	**65,254**	68,010	-	68,010
Investments	**1**	**-**	**1**	1	-	1
	65,255	**-**	**65,255**	68,011	-	68,011
Current assets						
Stocks	**267**	**-**	**267**	314	-	314
Debtors	**4,493**	**-**	**4,493**	4,710	6	4,716
Cash at bank and in hand	**151**	**-**	**151**	87	-	87
Infrastructure renewals prepayment	**873**	**-**	**873**	1,405	-	1,405
Total current assets	**5,784**	**-**	**5,784**	6,516	6	6, 522
Creditors - amounts falling due within one year	**(5,392)**	**-**	**(5,392)**	(6,136)	(6)	(6,142)
Net current assets	**392**	**-**	**392**	380	-	380
Creditors – amounts falling due after more than one year						
Borrowings	**(14,301)**	**-**	**(14,301)**	(14,601)	-	(14,601)
Other creditors	**(283)**	**-**	**(283)**	(1,892)	-	(1,892)
Total Creditors – amounts falling due after more than one year	**(14,584)**	**-**	**(14,584)**	(16,493)	-	(16,493)
Provisions for liabilities and charges						
Deferred tax provisions	**(2,255)**	**-**	**(2,255)**	(2,772)	-	(2,772)
Deferred income	**(61)**	**-**	**(61)**	(74)	-	(74)
Net assets employed	**48,747**	**-**	**48,747**	49,052	-	49,052
Capital and reserves						
Called up share capital	**1,174**	**-**	**1,174**	1,174	-	1,174
Profit and loss account	**46,073**	**-**	**46,073**	46,378	-	46,378
Other reserves	**1,500**	**-**	**1,500**	1,500	-	1,500
Capital and reserves	**48,747**	**-**	**48,747**	49,052	-	49,052

Veolia Water East Limited

Current cost profit and loss account for appointed business for the year ended 31 March 2011

	Note	**2011** **£000**	2010 £000
Turnover	2(i), (ii)	**14,353**	14,967
Current cost operating costs (including CCD and IRC)	3	**(10,808)**	(10,628)
Total operating income	2(iii)	**467**	846
Working capital adjustment	4	**(49)**	(32)
Current cost operating profit		**3,963**	5,153
Other income		**71**	-
Net interest receivable less payable	5	**(683)**	(715)
Financing adjustment	6	**776**	591
Current cost profit before taxation		**4,127**	5,029
Current tax		**(989)**	(1,126)
Deferred tax		**517**	(262)
Current cost profit attributable to shareholders		**3,655**	3,641

The Turnover and Operating Profit relate entirely to continuing operations.

No government grants or assistance were received by the company during the stated period.

Veolia Water East Limited

Current cost balance sheet for appointed business as at 31 March 2011

	Note	**2011 £000**	2010 £000
Fixed assets			
Tangible assets	8(i)	**252,452**	236,216
Third party contributions since 1989-90	8(ii)	**(10,148)**	(9,460)
		242,304	226,756
Working capital	9	**(13)**	(482)
Net operating assets		**242,291**	226,274
Cash and investments		**151**	87
Infrastructure prepayment		**873**	1,405
Corporation tax payable		**(619)**	(629)
Creditors due after one year		**(14,584)**	(16,493)
Deferred tax provision		**(2,255)**	(2,772)
Net assets employed		**225,857**	207,872
Capital and reserves			
Called up share capital		**1,174**	1,174
Profit and loss account	10	**10,161**	8,819
Current cost reserve at 31 March	11	**213,022**	196,379
Other reserves		**1,500**	1,500
		225,857	207,872

Veolia Water East Limited

Current cost statement of cash flows for the year ended 31 March 2011

	2010/11			2009/10		
	Appointed	**Non-Appointed**	**Total**	Appointed	Non-Appointed	Total
	£000	**£000**	**£000**	£000	£000	£000
Net cash inflow from operating activities	**6,851**	**398**	**7,249**	8,017	408	8,425
Returns on investments and servicing of finance						
Interest paid	**(620)**	**-**	**(620)**	(640)	-	(640)
Net cash flow from returns on investments and servicing of finance	**(620)**	**-**	**(620)**	(640)	-	(640)
Taxation paid	**(1,000)**	**(118)**	**(1,118)**	(704)	(67)	(771)
Capital expenditure and financing of investment						
Gross cost of purchase of fixed assets	**(802)**	-	**(802)**	(2,457)	-	(2,457)
Receipts of grants and contributions	**185**	-	**185**	262	-	262
Infrastructure renewals expenditure	**(1,084)**	-	**(1,084)**	(2,029)	-	(2,029)
Receipts from sales of fixed assets	**639**	-	**639**	844	-	844
Net cash flow from investing activities	**(1,062)**	**-**	**(1,062)**	(3,380)	-	(3,380)
Dividends paid	(3,840)	**(280)**	**(4,120)**	(4,092)	(341)	(4,433)
Net cash inflow / (outflow) before financing	**329**	**-**	**329**	(799)	-	(799)
Financing						
Short term group financing	**35**	**-**	**35**	(442)	-	(442)
Loan (repaid) / received	**(300)**	**-**	**(300)**	1,100	-	1,100
Net cash (outflow)/inflow from financing	**(265)**	**-**	**(265)**	658	-	658
Increase/(decrease) in cash in the year	**64**	**-**	**64**	(141)	-	(141)

Veolia Water East Limited

Notes to the current cost statement of cash flows for the year ended 31 March 2011

Reconciliation of current cost operating profit to net cash flow from operating activities

	2010/11			2009/10		
	Appointed	**Non-Appointed**	**Total**	Appointed	Non-Appointed	Total
	£000	**£000**	**£000**	£000	£000	£000
Current cost operating profit	**3,963**	**389**	**4,352**	5,153	475	5,628
Working capital adjustment	**49**	**-**	**49**	32	-	32
Decrease / (increase) in working capital	**108**	**9**	**117**	32	(67)	(35)
Current cost depreciation	**2,372**	**-**	**2,372**	2,083	-	2,083
Current cost profit on sales of fixed assets	**(467)**	**-**	**(467)**	(846)	-	(846)
Infrastructure renewals charge	**1,616**	**-**	**1,616**	1,375	-	1,375
Other non-cash items	**(790)**	**-**	**(790)**	188	-	188
Net cash flow from operating activities	**6,851**	**398**	**7,249**	8,017	408	8,425

Veolia Water East Limited

Notes to the current cost statement of cash flows for the year ended 31 March 2011 (continued)

Reconciliation of net cash flow to movement in net debt

	2010/11			2009/10		
	Appointed	**Non-Appointed**	**Total**	Appointed	Non-Appointed	Total
	£000	**£000**	**£000**	£000	£000	£000
Increase / (decrease) in cash in the period	**64**	**-**	**64**	(141)	-	(141)
Short term group financing	**(35)**	**-**	**(35)**	442	-	442
Loan repaid / (received)	**300**	**-**	**300**	(1,100)	-	(1,100)
Movement in net debt in the period	**329**	**-**	**329**	(799)	-	(799)
Net debt at the beginning of the period	**(13,794)**	**31**	**(13,763)**	(12,995)	31	(12,964)
Net debt at the end of the period	**(13,465)**	**31**	**(13,434)**	(13,794)	31	(13,763)

Notes to the current cost statement of cash flows for the year ended 31 March 2011 (continued)

Analysis of net debt

	Fixed rate	Floating rate	Index linked	Total
Maturity profile				
Less than 1 year	-	-	-	**-**
Between 1 and 2 years	-	-	-	**-**
Between 2 and 5 years [1]	(1)	(7,800)	-	**(7,801)**
Between 5 and 20 years	(6,500)	-	-	**(6,500)**
In more than 20 years	-	-	-	**-**
Borrowings (excluding preference shares)				**(14,301)**
Preference share capital				**-**
Total borrowings				**(14,301)**
Cash				**151**
Short term deposits				**716**
Net debt				(13,434)

[1] Although the loan expires in one year from 31st March 2011 it will be immediately renewed and therefore in these accounts it has been classified as a long-term liability thereby not distorting the level of debt.

Veolia Water East Limited

Notes to the current cost financial information for the year ended 31 March 2011

1 Statement of accounting policies

Basis of current cost accounting
These accounts have been prepared in accordance with relevant Regulatory Accounting guidelines (RAGs).

The current cost accounts have been prepared for the Appointed Business of the Company in accordance with guidance issued by the Director General of Water Services for modified real terms financial statements 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 certain assets acquired prior to 31 March 1990, the effective commencement of the new regulatory system.

The accounting policies used are the same as those adopted in the non-statutory historical cost accounts, except as set out below.

Use of estimates
The preparation of accounts in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the accounts and the reported amounts of revenues and expenses during the reporting period. Actual outcomes could differ from those estimates

Tangible Fixed Assets
An Asset Management Plan (AMP) survey was undertaken to produce Modern Equivalent Asset (MEA) values for all existing assets at 31 March 2008. The asset valuation arising from this exercise has been included in this year's accounts, after adjusting for inflation as measured by changes in the Retail Price Index (RPI) since that date.

Expenditure on maintaining the operating capability of the network in accordance with defined standards of service is charged as an operating cost. Costs relating to increases in capacity or enhancements to the network are capitalised. No depreciation is charged on mains because the network is required to be maintained in perpetuity and therefore has no finite economic life.

FRS 15, FRS 12 and FRS 5 application G have not been applied in preparing the regulatory accounts. This is in accordance with requirement of the Regulator where regulatory accounting guidelines have been used instead. Therefore, the treatment in the regulatory accounts differs from that in the non-statutory financial statements. However, non-compliance has no effect on the profit and loss account other than to reclassify infrastructure renewals charges as depreciation.

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 the RPI for the year and treated as deferred income.

Infrastructure charges received in respect of connections to the mains network are allocated to fixed assets, surface and infrastructure, in accordance with the basis on which the charges are calculated.

Contributions receivable relating to infrastructure assets, which are not depreciated, have been deducted from the cost of tangible fixed assets in order to show a true and fair view.

1 Statement of accounting policies (continued)

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:

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.

Working capital adjustment – this is calculated by applying the change in the RPI over the year to the opening total of trade debtors and stock less trade creditors.

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.

Disposal of fixed assets adjustment (as defined in RAG 1.02) is calculated by applying the difference between the net book value of the current cost and the net book value of the historical cost of disposed assets, to the profit from disposal of fixed assets as shown in the historical cost accounts.

Dividend policy
The dividend policy aims to remunerate the ordinary equity share holder with a return that is broadly in line with the equity return allowed by Ofwat in the cost of capital assumption from the final determination for the AMP.

The dividend reflects a yield and a real growth consistent with the return on equity allowed by Ofwat in the determination for the current AMP, where yield is defined as the return on equity less the level of real growth in annual dividends

Notes to the current cost financial information for the year ended 31 March 2011 (continued)

		2011 £000	2010 £000
2	**Analysis of turnover and operating income for the Appointed Business**		
(i)	**Turnover**		
	Unmeasured turnover – household	**3,866**	3,745
	Measured – household	**7,324**	7,771
	Measured – non-household	**2,517**	2,635
	Large user and special agreement	**610**	671
	Measured turnover	**10,451**	11,077
	Third party services	**36**	145
	Total Turnover	**14,353**	14,967

(ii) Revenue Recognition

Revenue is recognised in accordance with FRS 5, 'Reporting the substance of transactions', in the period in which it is earned. The company does not recognise revenue where payment is received in advance.

However, payments made in the previous period in respect of the current period will be recorded as revenue in the current period.

FRS 5 Application Note G of FRS 5 has not been applied in the regulatory accounts.

Definition of and billing process for "Unoccupied" properties

Empty Measured Premises

Charges are payable if Premises are empty unless the Company is asked to turn off the supply. No retrospective allowances will be given. If the premises do not have a separate supply pipe it may not be possible for the Company to turn off the supply. There is no charge for turning off the supply but a re-connection fee is payable.

Notice of Vacation of Property

Where charges are fixed in relation to any Premises by reference to volume, the person made chargeable in relation to those Premises as occupier, shall be liable to pay such charges after they has cease to be the occupier of the Premises where they fail to notify the Company of the ending of their occupation of the Premises, at least two working days before they cease to occupy them.

The charges for which he shall be liable shall be those for the period ending with whichever of the following first occurs after he ceases to occupy the Premises:

- the next scheduled meter reading date
- the date the Company is informed by a new Occupier
- 28 days from the date he informed the Company

Revenue recognition (continued)

Where the person chargeable is not the occupier of the metered Premises, they may be held liable until the expiry of twenty-eight days' notice in writing. The twenty-eight days commences from the date the notice is received at the Company's Office. This provision will apply when the Occupier vacates Premises, but remains the owner of the Premises without giving the Company notice of vacation.

Empty Unmeasured Premises

Charges are payable if Premises are furnished but unoccupied unless the Company is asked to turn off the supply. No retrospective allowances will be given. There is no charge for turning off the supply but a re-connection fee is payable. If the premises do not have a separate supply pipe it may not be possible for the Company to turn off the supply.

Where a property has been empty for longer than 12 months, the Company may choose to meter the property.

Definition of and billing process for "Occupier" properties

Occupier is defined as any person who for the time being occupies any Premises supplied or the owner of any Premises who, not being in actual occupation:

(a) Maintains Premises for multiple occupation with shared facilities
(b) Lets Premises for periods of less than six months
(c) Maintains any other Premises ready for occupation.
(d) Maintains any newly converted or converted Premises ready for sale or letting.
(e) The Landlord of a house in multiple occupation as defined in Sections 77 and 254 to 259 of the Housing Act 2004

No bills are issued where details of the occupier are not known. Once occupier is identified, bills are issued retrospectively to the date of last change in occupancy.

Recognition of new properties

All new water supplies will be charged for by means of a meter.

Where there is a change in use of Premises or a change in occupier the Company may elect to treat this as a new supply.

		2011	2010
		£000	£000
(iii)	**Operating Income**		
	Current cost profit on sale of fixed assets	**467**	846

Veolia Water East Limited

Notes to the current cost financial information for the year ended 31 March 2011 (continued)

		2011	2010
		£000	£000
3	**Current Cost Operating Adjustments**		
	These adjustments are made to historical cost profit in order to arrive at profit after the maintenance of financial capital in real terms:		
	Historic cost operating costs	**10,798**	9,932
	Historic cost depreciation/amortisation	**(2,362)**	(1,387)
	Current cost depreciation/amortisation	**2,372**	2,083
	Current cost operating costs	**10,808**	10,628
	Historic cost profit on disposal	**(372)**	835
	Current cost profit on disposal	**839**	11
	Current cost operating income	**467**	846
	Disposal of fixed asset adjustments		
	Current cost disposals	**320**	1,043
	Less current cost depreciation	**(180)**	(1,043)
		140	-
	Historic cost disposals	**1,059**	132
	Less historic cost depreciation	**(80)**	(121)
		979	11

		2011	2010
4	**Working capital adjustment**	**£000**	£000
	This is calculated by applying the change in RPI over the year to the opening total of trade debtors and stock less trade creditors.		
	Trade debtors at 1 April	**4,710**	4,231
	Stock at 1 April	**314**	227
	Less creditors at 1 April	**(5,506)**	(4,487)
	Infrastructure Renewals Prepayment at 1 April	**1,405**	751
		923	722
	RPI	**5.35%**	4.45%
	Working capital adjustment	**49**	32

Veolia Water East Limited

Notes to the current cost financial information for the year ended 31 March 2011 (continued)

5 Net interest

	2011 £000	2010 £000
Interest receivable	-	129
Interest payable	(613)	(653)
Other finance charges	(70)	(191)
Net interest	(683)	(715)

6 Financing Adjustment

This is calculated by applying the change in RPI over the year to the opening balance of net finance, which comprises all monetary assets and liabilities in the balance sheet apart from those included in working capital.

	2011 £000	2010 £000
Cash at 1 April	87	228
Creditors due after one year	(14,600)	(13,500)
	(14,513)	(13,272)
RPI	5.35%	4.45%
	(776)	(591)

7 Dividends

	2011 £000	2010 £000
Ordinary Dividends		
Veolia Water Capital Funds	4,036	4,321
Dividends relating to non-appointed business	(280)	(341)
Other Minorities	40	68
Preference Dividends		
Veolia Water Capital Funds	43	43
Other Minorities	1	1
	3,840	4,092

Notes to the current cost financial information for the year ended 31 March 2011 (continued)

8 Fixed assets

	Infra-structure Assets	Operational Assets	Other Assets	Total
	£000	£000	£000	£000
(i) Tangible assets				
Gross replacement cost				
Balance 1 April 2010	203,313	62,516	9,787	275,616
Reclassification	2	505	(507)	-
Restated balance 1 April 2010	203,315	63,021	9,280	275,616
AMP adjustment	2,307	7,794	(9,634)	467
Restated balance 1 April 2010	205,622	70,815	(354)	276,083
RPI adjustment	10,870	3,353	354	14,577
Disposals	-	(320)	-	(320)
Additions	320	554	-	874
Balance 31 March 2011	**216,812**	**74,402**	**-**	**291,214**
Depreciation				
Balance 1 April 2010	-	33,426	5,974	39,400
Reclassification		(1)	1	-
Restated balance 1 April 2010		33,425	5,975	39,400
AMP adjustment	-	1,345	(6,276)	(4,931)
Restated balance 1 April 2010	-	34,770	(301)	34,469
RPI adjustment	-	1,797	301	2,098
Disposals	-	(180)	-	(180)
Charge for the year	-	2,375	-	2,375
Depreciation 31 March 2011	**-**	**38,762**	**-**	**38,762**
Net book value				
Balance 1 April 2010	203,315	29,596	3,305	236,216
Balance 31 March 2011	**216,812**	**35,640**	**-**	**252,452**

8 Fixed assets (continued)

(ii) Third Party Capital Contributions

	Infra-structure Assets £000	Specialised Operational Assets £000	Other Assets £000	Total £000
Balance 1 April 2010	9,307	209	407	9,923
RPI adjustment	498	12	21	531
Additions	184	-	-	184
Balance 31 March 2011	**9,989**	**221**	**428**	**10,638**
Amortisation				
Balance 1 April 2010	-	56	407	463
RPI adjustment	-	3	21	24
Charge for the year	-	3	-	3
Amortisation 31 March 2011	**-**	**62**	**428**	**490**
Net value capital contributions				
Balance 1 April 2010	9,307	153	-	9,460
Balance 31 March 2011	**9,989**	**159**	**-**	**10,148**

9 Working Capital

	2011 £000	2010 £000
Stocks	**267**	314
Trade debtors – measured household	**496**	504
Trade debtors – unmeasured household	**234**	194
Trade debtors – measured non-household	**132**	142
Trade debtors – unmeasured non-household	**6**	6
Other trade debtors	**1,094**	1,168
Measured Income accrual	**2,443**	2,641
Short term capital creditors	**(135)**	(712)
Deferred income	**(1,440)**	(1,346)
Other accruals	**(221)**	(35)
Trade payments in advance	**88**	55
Trade creditors	**(2,977)**	(3,413)
	(13)	(482)

Veolia Water East Limited

Notes to the current cost financial information for the year ended 31 March 2011 (continued)

10 Current cost profit and loss account

	2011 £000	2010 £000
Reserves brought forward	**8,819**	10,556
Profit for the year	3,655	3,641
Dividends	(3,840)	(4,092)
Actuarial gain / (loss) on pension scheme	2,062	(1,786)
Movement on deferred tax relating to pension scheme	(535)	500
Balance at 31 March	10,161	8,819

11 Movement on current cost reserve

	2011 £000	2010 £000
Current cost reserve at 1 April	**196,379**	187,393
Reclassification	**-**	25
AMP adjustment	**5,398**	(1)
Restated balance 1 April 2010	**201,777**	187,417
RPI adjustments		
Fixed assets	**12,479**	9,913
Working capital adjustment	**49**	32
Financing adjustment	**(776)**	(591)
Grants and third party contributions	**(507)**	(392)
Current cost reserve at 31 March	**213,022**	196,379

12 Regulatory Capital Value (RCV) at 2009-10 prices

	2011 £000
Opening RCV for the year	60,725
Capital expenditure	1,589
Infrastructure renewals expenditure	1,303
Grants and contributions	(257)
Depreciation	(1,952)
Infrastructure renewals charge	(1,415)
Out-performance of Regulatory assumptions (5 years in arrears)	(386)
Closing RCV carried forward	**59,607**
Average RCV	**58,830**

This RCV reflects that used by Ofwat when setting price limits for the period 2010-15, at 2009-10 prices. The actual expenditure during the year, as recorded in the regulatory accounts, differs from the figures shown above. Differences in capital expenditure will not affect price limits in the current period but will be taken into account in the calculation of the RCV during the next price review period.

Veolia Water East Limited

Notes to the current cost financial information for the year ended 31 March 2011 (continued)

13 Reconciliation between statutory and regulatory accounts as at 31 March 2011

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. In addition, the Water Services Regulation Authority has decided to depart from UK GAAP and dis-apply the provisions of Note G of FRS 5, which states the turnover should not include amounts that the company does not expect to collect. Reconciliation to the balance sheet is shown in the statutory accounts set out below:

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Notes to the current cost financial information for the year ended 31 March 2011 (continued)

	Statutory UK GAAP £m	Regulatory £m	Explanation of difference
Profit and loss account			
Turnover	14.678	14.353	Income from the Anglian Water Reservation fee is netted off against Ardleigh Reservoir costs (£0.325m).
Operating costs	(11.236)	(10.849)	Income from the Anglian Water Reservation fee is netted off against Ardleigh Reservoir costs (£0.325m). There is a variance of £0.062m in respect of a difference between the regulatory accounts and statutory accounts in the policy for the right down of the infrastructure renewal prepayment that existed at March 2011.
Operating profit	3.954	3.132	Statutory accounts include other operating income of £0.511m, however this is not included in the regulatory accounts operating profit. Loss on disposal of fixed assets of £0.372m, adjusted for £0.962m revaluation effect, is excluded in operating profit in statutory accounts, but included in regulatory accounts. There is a variance of £0.062m in respect of a difference between the regulatory accounts and statutory accounts in the policy for the right down of the infrastructure renewal prepayment that existed at March 2011.
Balance sheet			
Tangible fixed assets (net book value)	66.063	65.254	In the statutory accounts the tangible fixed assets figure includes the infrastructure renewal prepayment. For regulatory accounting figures Ofwat requests this amount of £0.873m is included in current assets. The remainder of the variance is in respect of the infrastructure renewal prepayment policy referred to above.
Debtors	3.274	4.493	The difference mainly relates to receipts in advance which is netted off in the statutory accounts (£1.219m)
Creditors	4.170	5.392	Mainly relates to receipts in advance treated as a creditor in the regulatory accounts (£1.219m). Liability in respect to NI on share options of £0.003m is treated as short-term creditors in regulatory accounts, and as long-term creditors in statutory accounts.

Veolia Water East Limited

Notes to the current cost financial information for the year ended 31 March 2011 (continued)

14 Activity Cost Analysis for the Year Ended 31 March 2011

	SERVICE ANALYSIS		
Appointed Business – Profit and Loss Account	Water Resources & Treatment £000	Water Distribution £000	Water Services Total £000
Direct costs			
Employment costs	239	142	381
Power	466	4	470
Hired and contracted services	101	47	148
Associated companies	56	31	87
Materials and consumables	152	96	248
Service charges – Abstraction charge	321	-	321
Other direct costs	(307)	11	(296)
Total direct costs	**1,028**	**331**	**1,359**
General and support expenditure	757	319	1,076
Functional expenditure	**1,785**	**650**	**2,435**
Operating Expenditure			
Customer Services			2,450
Scientific Services			175
Other Business Activities			193
Total Business Activities			**2,818**
Local Authority Rates			1,146
Doubtful Debts			387
Total Opex Less Third Party Services			**6,786**
Third Party Services – Opex			34
Total Operating Expenditure			**6,820**
Reactive & Planned Maint.			
(incl. in Opex)			
Reactive & Planned Maint. Infrast.	-	370	370
Reactive & Planned Maint. Non-Infrast.	173	53	226
Capital Maintenance			
Infrast. Renewals Expenditure REV	-	1,616	1,616
Movement in Infrast. Renewals			
Current cost depreciation	1,496	879	2,375
Amortisation of deferred credits			(3)
Business activities current cost depreciation (non-allocated)			-
Total Capital Maintenance			**3,988**
Total Operating Costs			**10,808**
CCA (MEA) Values			**291,208**

The apportionments of general and support activities required to complete the above statement have been made on a pro-rata basis to direct cost allocations, which is consistent with prior years.

Veolia Water East Limited

Notes to the current cost financial information for the year ended 31 March 2011 (continued)

15 Long Term Current Cost Profit & Loss Account (2010/11 prices)

	2011 £000	2010 £000	2009 £000	2008 £000	2007 £000
Turnover	**14,353**	15,768	15,851	15,333	15,757
Current Cost Operating Costs	**(10,808)**	(11,197)	(11,650)	(10,550)	(10,185)
Operating Income	**467**	891	10	814	21
Working Capital Adjustment	**(49)**	(34)	2	(75)	(44)
	3,963	5,429	4,213	5,522	5,572
Other Income	**71**	-	-	-	-
Net Interest	**(683)**	(753)	(768)	(492)	(472)
Financing Adjustment	**776**	623	(50)	392	428
Current Cost Profit Before Taxation	**4,127**	5,298	3,396	5,420	5,506
Taxation	**(472)**	(1,462)	(1,129)	(1,769)	(1,887)
Current Cost Profit Attributable to Shareholders	**3,655**	3,836	2,267	3,652	3,619
Infrastructure Renewal Charge	**(1,616)**	(1,449)	(1,676)	(1,590)	(1,483)
Current Cost Depreciation	**(2,375)**	(2,192)	(2,050)	(2,260)	(2,204)
Operating Costs	**(6,817)**	(7,556)	(7,924)	(6,700)	(6,498)

Veolia Water East Limited

Notes to the current cost financial information for the year ended 31 March 2011 (continued)

16 Long Term Current Cost Balance Sheet (2010/11 prices)

	2011	2010	2009	2008	2007
	£000	£000	£000	£000	£000
Tangible Fixed Assets	**252,452**	248,854	248,144	247,958	236,861
Third Party Contributions Since 1989-90	**(10,148)**	(9,966)	(9,691)	(9,423)	(8,747)
Working Capital	**860**	972	831	604	1,945
Net Operating Assets	**243,164**	239,860	239,283	239,139	230,059
Cash & Investments	**151**	92	251	198	22
Creditors Due within One Year	**(619)**	(663)	(254)	(875)	(865)
Creditors Due After One Year	**(14,584)**	(17,375)	(15,699)	(14,095)	(10,653)
Provision for Liabilities & Charges	**(2,255)**	(2,920)	(2,793)	(2,398)	(2,783)
Net Assets Employed	**225,857**	218,993	220,788	222,026	215,780
Called up Share Capital	**1,174**	1,237	1,292	1,286	1,291
Capital Reserve	**1,500**	1,580	1,651	1,644	1,651
Profit & Loss Account	**10,161**	9,291	11,642	12,766	14,021
Current Cost Reserve	**213,022**	206,885	206,204	206,274	198,818
	225,857	218,993	220,788	221,971	215,780

Notes to the current cost financial information for the year ended 31 March 2011 (continued)

17 Disclosure of Transactions with Associates

(i) The Company complies with the objectives and principles of Regulatory Accounting Guideline 5.04 (Rag 5.04) as set by the Water Services Regulation Authority, namely that transactions with associated companies are at arms length and there has been no cross subsidy.

(ii) No director of the Company has acted as both purchaser and supplier. Procedures are in place covering the placing of orders and authorisation of invoices.

(iii) The materiality levels below which transactions are disclosed are consistent with the general requirement in Condition F, as set by the Water Services Regulation Authority. The non-appointed elements of the business relating mainly to billing commission and rental income have been separated from the appointed business.

(iv) The Company has continued to allocate costs as in previous years rather than on the full activity based method as described in RAG 5.

Services Provided by Associates – Profit and Loss Charges

Associate	**Service**	**Terms of Supply**	**Value £'m**
Ardleigh Reservoir Committee	Bulk purchase of treated water	No market exists	0.451
Veolia Water Southeast Ltd	Recharge for monitoring of telemetry/out of hours calls	Other market testing	0.064
Veolia Water Central Plc	Recharge for central services	Other market testing	0.008
Veolia Water Shared Services	Recharge for central services	Other market testing	0.691
Veolia Water UK PLC	Management fee	Other market testing	0.370
Veolia Water UK PLC	Recharge for insurance (Group policies)	Other market testing	0.084
Veolia Water UK PLC	Other recharges	Other market testing	0.162
Veolia Water Capital Funds	Interest on loan	Other transactions with Associated Companies	0.622
Veolia Environnement UK Ltd	Recharges	Other market testing	0.003
Veolia Water Trust Fund	Debt recovery	Other transactions with Associated Companies	0.012
Total	**Profit & Loss Charges**		**2.467**

Services Provided by Associates – Equity

Associate	**Service**	**Terms of Supply**	**Value £'m**
Veolia Water Capital Funds	Dividends (including those relating to non-appointed)	Other transactions with Associated Companies	4.079
Total	**Profit & Loss Charges**		**4.079**

17 Disclosure of Transactions with Associates (continued)

Services Provided by Associates – Balance Sheet Charges

Associate	Service	Terms of Supply	Value £'m
Balance Sheet			
Ardleigh Reservoir Committee	Various capital schemes	No market exists	0.053
Veolia Water Shared Services	IT related	Other market testing	0.100
Total	**Capital Expenditure**		**0.153**

Turnover of associated companies

	£m
Ardleigh Reservoir Committee	1.195
Veolia Water Southeast Ltd	18.646
Veolia Water Central Plc	239.647
Veolia Water Shared Services	25.846
Veolia Water UK PLC *	5.084
Veolia Environnement UK Ltd	Nil

* Veolia Water UK PLC turnover represents the turnover plus other operating income of the Company itself and does not include the turnover of the group subsidiaries.

Funding from Associate: Veolia Water Capital Funds PLC
A credit agreement exists with Veolia Water Capital Funds PLC to provide funding up to a maximum aggregate principal amount of £13.0m at an interest rate of LIBOR plus 200 basis points.

A 15-year fixed-term loan was entered into on 11 February 2005, providing £6.5m capital from Veolia Water Capital Funds PLC, at an interest rate of 5.407%.