Portsmouth water

150 years of quality service

REGULATORY ACCOUNTS 2008

CONTENTS

OUR BUSINESS

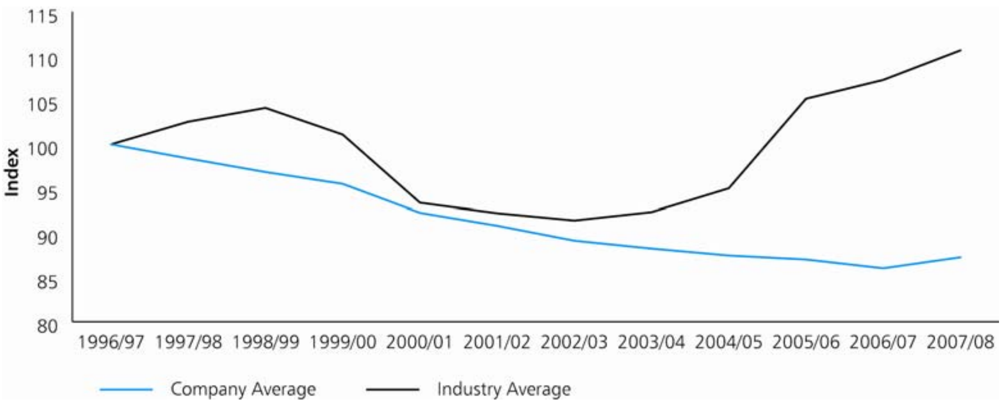
Portsmouth Water provides water to 299,000 homes and businesses in an area covering 868 square kilometres from the River Meon in Hampshire to the River Arun in West Sussex. The Company serves the cities and towns of Portsmouth, Chichester, Fareham, Gosport, Havant and Bognor Regis. On average, each day it supplies approximately 178 million litres of water through a network of over 3,200 kilometres of underground mains. Water supplied, which is generally of high quality, is derived from the chalk of the South Downs and is abstracted from wells, boreholes, springs and the River Itchen. The table below shows the major sources used by the Company during the year. The springs at Havant and Bedhampton, which provide between 30% and 35% of the total supply, are thought to be the largest group of springs used for public supplies in Europe.

Source	Actual 2007/08 Abstraction (Million Litres)	% of Supply 2007/08	% of Supply 2006/07
Springs at Havant & Bedhampton	20,003	30	31
River Itchen	8,567	13	9
Boreholes, Wells & Adits	38,665	57	60
Totals	**67,235**	**100**	**100**

Water from the springs at Havant and Bedhampton is treated at the Farlington treatment works and there are also treatment works at the River Itchen and Lovedean, which accounts for approximately 3% of supplies. Water from the remaining sources requires less sophisticated treatment.

Portsmouth Water's charges are the lowest in England and Wales, the average annual bill for water being £85 per household, the equivalent of 23p per day. In real terms, the price of water for household customers has fallen by 13% over the last 11 years. This compares with a real increase of 10.6% for the industry as a whole, as illustrated in the chart below, where the 1996/97 prices are indexed at 100:

Comparison of Average Household Bills with Average Industry Tariffs



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

Ofwat is the water industry's economic regulator, and its principal duties are exercised through the price-setting process. Ofwat sets price limits for Portsmouth Water every five years. The last determination of prices was in December 2004 for the period 2005 to 2010. The price setting process is known as the Periodic Review and involves a series of consultations between water companies, Ofwat and the other regulators over a two year period. The review examines all aspects of the business and requires the Company to submit a detailed Business Plan to Ofwat. Water companies are allowed to increase prices to customers annually by inflation (RPI) plus or minus the price limit set by Ofwat. The price limits for Portsmouth Water are shown in the table on page 10 and reflect the revenue, which the regulator believes an efficient company needs in order to finance its operations and capital programme, after making an assessment of potential future efficiency gains.

Water companies are largely natural monopolies and, in recognition, the Government, following Ofwat's advice and wide consultation, is cautiously opening up to competition the market for provision of water to large industrial and commercial customers. Although these customers have been able to switch supplier since December 2005, none have done so to date.

Portsmouth Water is recognised as one of the most efficient water companies in England and Wales (Source - Water and Sewerage Service Unit Costs and Relative Efficiency 2006/07 Report - published by Ofwat), and this has benefited customers through lower bills over many years, as shown above.

Over the last twenty years, the Company has experienced falling demand for water, particularly from commercial customers. The future, however, is expected to see rising demand from domestic customers, with a significant house building programme planned in the Company's area of supply. A twenty five year Water Resources Plan is also produced at each Periodic Review. The plan is reviewed annually and enables the Company to balance supplies with forecast demand even at times of dry conditions. Future plans incorporate a twin-track approach of demand management and additional sources of supply.

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

BUSINESS STRATEGY

Mission Statement

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

The Company has a well developed, focused strategy which will meet the demands of all its stakeholders. The key objectives are:

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

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

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

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

CURRENT DEVELOPMENT AND PERFORMANCE

Financial Performance

Profit Before Tax - Historical Accounts

Turnover for the year increased by 2.6% to £33.9m. This reflected the 5.37% overall tariff increase implemented in July 2007, which was partially offset by a reduction of £0.4m of income from the bulk supply to Southern Water and £0.5m in income from new connections, and other non-tariff work. The income from the bulk supply was very high in 2006/07 as the extent of the drought conditions in 2006 meant that it was operating for most of that year.

Operating costs, excluding depreciation and the FRS17 pension charge rose by £0.6m (3.7%). This was largely due to salary pay awards and electricity price increases. The current service cost for the pension scheme was increased by £1.2m to £2.3m. This was as a result of a one-off credit to the charge in 2006/07 following a change in the rules of the scheme allowing retirees to commute more of their pension to a lump sum, which has the effect of reducing the ongoing pension liability.

There was a loss on disposal of fixed assets of £0.2m compared to a profit of £0.9m in 2006/07 when the Company sold three properties.

Interest receivable at £4.3m (2007 - £3.6m) relates mainly to interest received from group companies and is based on Libor plus 1%.

An increase in other finance income of £0.2m represents an increase in the expected return on Pension Fund assets.

Interest payable at £6.2m (2007 - £5.3m) includes a £2.9m indexation of the loan provided by Artesian Finance plc (2007 - £2.4m). Interest on the capital sum amounted to £2.8m (2007 - £2.7m). Total borrowing was higher during the year as a result of the level and timing of the capital expenditure programme and interest on short term borrowing was £0.3m higher.

As a result primarily of the increased pension charge and lower income from property sales, profit before tax reduced to £8.4m (2007 - £10.7m).

Profit Before Tax - Current Cost Accounts

The current cost profit before tax reduced to £6.6m (2007 - £9.1m), principally due to the increased pension charge and lower income from property sales, as covered above. Current cost depreciation was also £0.6m higher than the previous year, reflecting the high level of capital expenditure in the year, particularly on the membrane plants.

Taxation

The taxation charge was £2.4m lower due to a reduction in deferred tax which was the result of the effect of the removal of industrial buildings allowances and changes to corporation tax and capital allowance rates.

Dividends

The dividends paid during the year amounted to £4.209m (2007 - £4.471m). In 2006/07 a special dividend of £0.3m was paid which represented an element of the profit on the sale of property. Dividends are paid up to the parent company and largely used to service debt held by the group.

Cashflow and Balance Sheet

Net cashflow from operations at £16.0m (2007 - £16.1m) reduced marginally as a result of a reduction in trade creditors. Net cash outlay on fixed assets at £12.2m (2007 - £11.8m) reflected a large outlay on the construction of the three membrane plants and further progress on the mains renewal programme.

Net debt at £79.0m (2007 - £73.6m) increased during the year as a result of the indexation of the £66.5m Index Linked Loan and the relatively high capital programme. At the year end, net debt to regulatory capital value was 72.3% (2007 - 71.3%).

Interest Rate, Liquidity, Capital and Credit Risk

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

The Company's exposure to interest rate fluctuations is now limited by the fixed interest rate applicable to the index-linked loan drawn in 2002, with inflation risks on the cost of the loan being effectively hedged against regulated revenues which are also linked to the Retail Prices Index. Interest is charged at a fixed rate of 3.635% on the indexed amount of the loan. The indexed value of the loan at 31 March 2008 was £78.6m (2007 - £75.7m).

The Company seeks to manage financial risk, to ensure sufficient liquidity is available to meet foreseeable needs through an appropriate borrowing structure and to invest cash assets safely and profitably on the short term market. Short term liquidity is achieved through a £15m working capital facility and an overdraft arrangement. At the end of the year, £4.0m of this facility had been drawn (2007 - £1.5m), while the overdraft arrangement remained unutilised.

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

The capital structure is set at a level which provides an appropriate risk profile to ensure the Company can obtain finance at competitive levels. As is common in the water industry the Company monitors capital in the ratio of debt to Regulatory Capital Value (RCV). RCV is a measure of the Company's asset value used in the setting of prices in the water industry. The level of RCV is published by the regulator (Ofwat) on an annual basis. The ratio achieved for 2007/08 is shown on page 4, and the details of the calculation are shown on page 42.

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

Accounting Policies

The historical cost accounts have been prepared in accordance with the accounting policies described in note 1 to the historical cost accounts on pages 17 to 18, and with UK GAAP, with the exception of certain sections of FRS 12 and FRS 15 that are not applied in the preparation of regulatory accounts, as required by Ofwat. The current cost accounts have been prepared in accordance with the accounting policies described in note 1 to the current cost accounts on page 32. There was a change in accounting policy in respect of unbilled measured income as at the year end date, which is described more fully on page 18 of the accounts.

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

Pensions

The Company accounts for the Brockhampton Pension Scheme in which it is a participating employer, in accordance with FRS17. The latest actuarial valuation carried out for the purposes of FRS17 showed a surplus after deferred tax of £21.6m (2007 - £15.3m).

Key Financial Performance Indicators

Gearing (net debt/regulatory capital value) and cash interest cover are recognised as key indicators for the Company. Performance in 2008 against the target ratios is shown in the table below.

***KPI - 1*[1]**	**Target**	**Performance 2007/08**	**Performance 2006/07**
Gearing - Debt/RCV[2]	<83%	72.3%	71.3%
Cash interest cover[2]	>2.2	2.53	2.75

[1] Each KPI is defined in the Appendix on page 42

[2] Definition of terms is contained in the Appendix on page 42

Customer Service

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

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

KPI - 2 The Overall Performance Assessment

Target	**Performance 2006/07**
To be in the upper quartile of performance for all water companies	Placed 4th out of 22 companies

The Overall Performance Assessment for 2007/08 will be published by Ofwat after the Report and Accounts have been completed and therefore the performance shown above is for 2006/07.

KPI - 3 DG Service Indicators

The DG service indicators data shown below is as recorded by the Company for 2007/08 and will be reported to Ofwat in the annual regulatory June Return.

DG Service Indicator	**Target**	**Performance 2007/08**	**Performance 2006/07**
DG2 No. of properties at risk of inadequate pressure	≤ 120	66	90
DG3 Unplanned interruptions to supply	≤ 0.3	0.14	0.23
DG4 Population subject to hosepipe bans	Nil	Nil	Nil
DG6 Billing contacts - answered within 5 days	100%	100%	100%
DG7 Written complaints - answered within 10 days	100%	100%	100%
DG8 Bills for metered customers - no. receiving bill based on meter reading	100%	100%	100%
DG9 Telephone contact - no. of calls abandoned	≤ 2.5%	4.2%	6.2%
- all lines busy	≤ 0.7%	0.3%	Nil

In all categories Ofwat assessed the Company as having good performance for 2006/07. The Ofwat assessments for 2007/08 will not be published until September, but the results recorded by the Company meet the criteria for being assessed as good.

KPI - 4 Water Quality

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

Water Quality	**Target**	**Performance 2007**	**Performance 2006**
Compliance samples passing standards	99.90%	99.97%	99.96%

The water quality performance indicator relates to the calendar year.

Operating Efficiency

Ofwat publishes a report each year which includes its assessment of the comparative operating efficiency of all water companies in England and Wales using econometric modelling. Companies are put in bands A to E according to their performance for both operating and capital maintenance efficiency, A being the top band. The latest report published is for the financial year 2006/07, which showed that Portsmouth Water was assessed as the top performing company and in the top bands for both operating and capital maintenance expenditure. In the medium term this benefits customers through relatively lower prices and the Company intends to maintain its position in the efficiency rankings.

KPI - 5 Efficiency

Target	**Performance 2006/07**
To be ranked in Band A for Operating Efficiency	Operating Efficiency Band A
To be ranked in Band A for Capital Maintenance Efficiency	Capital Maintenance Efficiency Band A

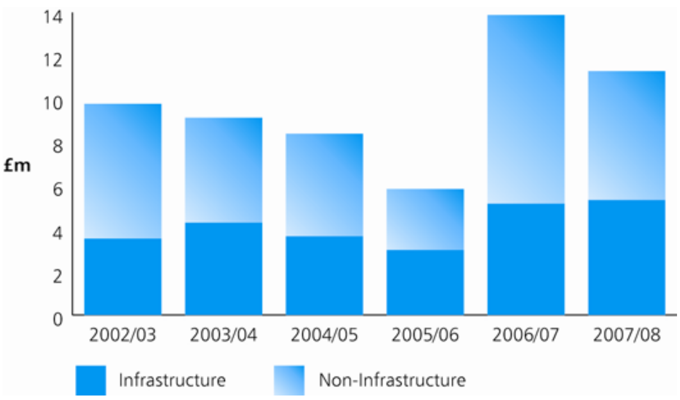
Capital Investment

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

Capital Programme Agreed	**Outcome**
Infrastructure Assets	
– Renewal of 25km of mains each year	Since April 2005, the Company has renewed an average of 24.6km per year
Water Quality Installation of membrane filtration plants to minimise the risk of cryptosporidium at	
– River Itchen	Completed Summer 2007
– Soberton	Will be completed in late Spring 2008
– Fishbourne	Will be completed in late Spring 2008
Remedial work on trunk mains in the Company's largest supply area to reduce the risk of discoloured water incidents	A small amount of work still to be carried out, but will be complete by the end of 2008
The installation of blending facilities at sources at risk from increasing nitrate levels	Will be completed in 2009
Optional Water Meters It was anticipated that 2,200 domestic customers would wish to switch from an unmeasured to a measured supply	In the 3 years to March 2008, over 13,000 customers had opted to switch, an average of 4,300 per year

Gross capital investment during the year was £12.0m (2007 - £14.8m) and included £4.8m (2007 - £4.1m) on infrastructure renewals. After receiving capital contributions and infrastructure charges of £0.8m, net capital expenditure was £11.2m (2007 - £13.9m). The chart below shows the level of net capital investment over a six year period in outturn prices.

Net Capital Expenditure



The major elements of expenditure in the year related to:

– Mains renewed - 27km (2007 - 26.0km) were renewed at a cost of £4.8m. The programme allowed for at the last Determination is now close to being met

- Membrane plants - work is nearing completion at two sites. The expenditure during the year was £4.0m and the full cost of the two plants will be £6.9m
- Havant Thicket Winter Storage Reservoir - the Company has started planning for a winter storage reservoir, which should help ensure security of water supplies well into the future. In order to obtain planning permission for this scheme, considerable environmental studies and public consultation has to be undertaken, which requires a range of design options and impact assessments. In 2007/08 this work resulted in expenditure of £0.6m

Water Resources - Outlook for 2008

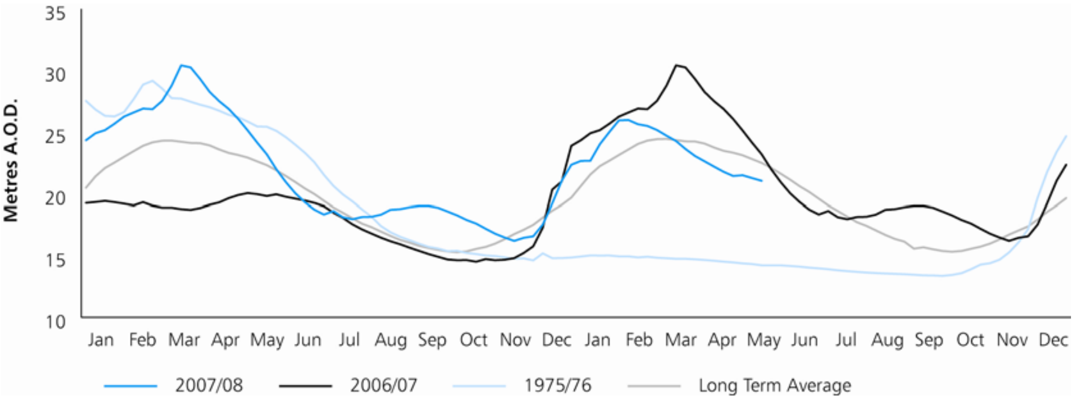
As detailed on page 1, nearly 90% of water supplied to customers is from groundwater springs, boreholes and wells which abstract from the underground chalk of the South Downs. Groundwater levels are therefore critical to maintaining supplies to customers. The Company has for many years monitored the groundwater level at Idsworth Well, Rowlands Castle, which is unaffected by abstraction and is representative of groundwater conditions in the South Downs chalk.

The rainfall for the year 2007/08 is as shown in the chart below.

Rainfall at Havant 2007/08

Despite the rainfall in the winter of 2008 being less than the long term average, the groundwater of the South Downs chalk, as measured at Idsworth Well, received recharge during the winter and, by May, was close to the long term average. This is outlined on the two year graph below, which includes the thirty year long term average and the drought year of 1976, when the Company last imposed a hosepipe ban.

Idsworth Well



Water resources are therefore expected to be sufficient to meet peak demands in the summer of 2008 and a hosepipe ban is not expected in our area of supply. However, the Company has used its newsletter, website and press releases to stress to customers the need to be conservative in their use of water.

Long Term Resource Planning

The Company has recently published its Draft Water Resources Management Plan for public consultation. The plan examines the likely key influences on the demand for water from customers and on the Company's ability to meet that demand. The plan also identifies the actions required to ensure that the supply/demand balance is met. A number of key assumptions were made:

- The number of domestic households in the Company's area of supply will grow from 281,600 in 2007 to over 348,000 by 2035 (Source - Experian)

- There will be a rise in average year per capita consumption from 160 litres/head/day in 2007 to 174 litres/head/day in 2035. The principal driver behind this movement will be the reduction of occupancy levels in households caused by a number of demographic factors
- The peak demand during a dry summer is 1.4 times that of average demand

Projections show that, whilst at average demand the Company has sufficient resources and treatment capacity until 2030, there may be insufficient capacity to meet summer peak demand by approximately 2015. To address this shortfall, the Company has developed a twin track approach of demand management and additional sources of supply consisting of:

- The development of a Farlington Washwater Recovery Plant in the AMP5 period by 2011/12.
- Initiating a Leakage Savings Programme which will reduce leakage levels from the current target of 29.7 Ml/d to a new target of 26.7 Ml/d by 2014/15.
- Instigating a promotional Water Efficiency Programme which will include sending cistern devices to all customers starting in 2010/11. The programme will be repeated on a five-yearly basis as the devices only have a short life expectancy.
- Beginning a 25 year programme of compulsory metering for all domestic households, where practicable, beginning in 2010/11. The Company plans a targeted programme which will minimise the overall costs of meter installation.
- Developing additional boreholes at Lavant and Brickkiln Water Treatment Works within the currently licensed abstraction limits by 2014/15.
- Promoting a programme of retrofit fitting of dual flush devices in toilets from 2015/16.
- Continuing the development of Havant Thicket Winter Storage Reservoir for completion by 2021.

Leakage

Leakage for the year was recorded at an average of 29.6Ml/d, which was within the leakage target of 29.7Ml/d. The leakage targets were set out in the Company's Business Plan for the last Periodic Review and agreed by Ofwat as part of the Final Determination in 2004.

KPI - 6 Leakage

Target	**Performance 2007/08**
Average leakage of 29.7Ml/d	Average leakage of 29.6Ml/d

Employees

The Company employs 222 people and believes it recruits and retains the right people which is key to the successful performance of the business.

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

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

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

Staff turnover, excluding retirees was 8.1% in 2008 (2007: 8.2%), which compares favourably with the national average which was 15.5% in 2006 (Source – EEF Absence and Rehabilitation Survey 2007).

Total absence (days per employee per year) has remained at just under 4.5. The figure of 4.48 compares with 4.38 for last year and is below the average for private companies of the same size at 7.2 (Source: CIPD: Annual Survey Report 2007).

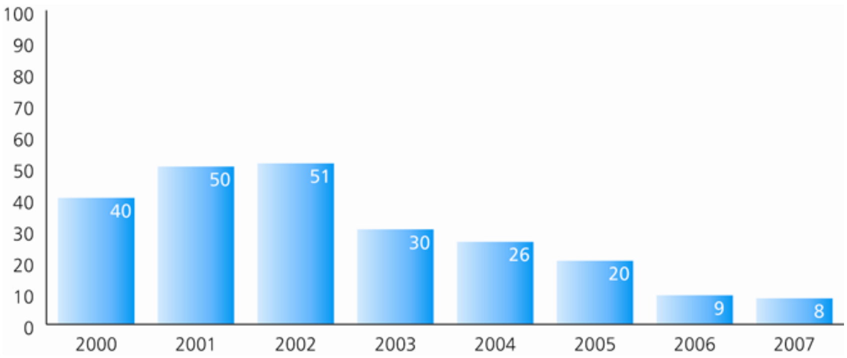
Health and Safety

Health and safety of employees is fundamental to the success of the business and the Company is committed to achieving high standards across the organisation. It has been 5 years since the Company embarked on a mission to improve its health and safety culture and therefore the record in this area. To achieve the initial step change the Company put health and safety at the top of the agenda and from the Board down has made it a high priority.

Last year saw the Company implement a number of campaigns and initiatives, aimed at increasing staff awareness of health and safety issues. These included vibration and audio assessments, poster campaigns, tool box talks along with training in safety awareness and manual handling.

The graph below portrays a positive picture in respect of the improvement in the Company's health and safety performance, notably a fall in total accidents to a third of what they were in 2003. The improvement since 2003 reinforces the Company's decision to revitalise health and safety and the commitment of time and resources into that area.

Total Accidents



The efforts of all employees were rewarded in March 2008, when the Company received a Gold Award for occupational health and safety from RoSPA for the third consecutive year.

CORPORATE RESPONSIBILITY

Environmental Performance

Environmental Performance

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

Conservation

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

Biodiversity Action Plan

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

Sustainable Procurement

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

Specific Environmental Projects

The Company has been involved in three environmental investigations into the impact of water abstraction on species identified by the Habitats Directive. The investigations at the River Itchen, Chichester Harbour and Langstone Harbour are covered in more detail on page 10.

Prosecution

In early 2007, an incident occurred at the River Itchen Treatment Works which resulted in polyaluminium chloride being distributed into a tributary of the River Itchen. None of the chemical reached the main river but some fish died. In 2007/08 the Company received a fine of £10,000. The Company has taken action to avoid this happening in the future.

Water Efficiency

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

Cistern Devices

Approximately 10,000 'Save-a-Flush' bags were issued to customers during the year.

Measured Customers

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

Commercial Water Audits

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

In-House Efficiency Study

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

Work in the Community

Amenities and Recreation

The Company's education partnership with Staunton Country Park has continued to grow. As well as providing the 'Water Is Life' themed education programme for local schools a 'Water is Life Trail' for visitors to the park was launched. The water trail is designed to help educate children and parents visiting the Park about the importance of water as a resource and encourage them to be more water efficient. The trail takes the form of a walk within the park searching for water information boards which help to answer simple questions.

Charitable Trust Fund

Since 2004 the Company has been supporting a Charitable Trust Fund, which aims to provide assistance for customers who have difficulty paying their bills.

Drinking Water Bottles

The Company has continued to promote the benefits to children of drinking water and as part of our 'Water for Health' initiative we have offered a drinking water bottle at the subsidised cost of 15p per bottle for every child in a local primary, infant and junior school.

The Water Bottles for Schools offer has gone from strength to strength with over 20,000 delivered last year and which has seen nearly 160,000 water bottles being delivered through the schools to our local children over the last five years.

Community Talks

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

Festivals and Fairs

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

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

The Company also played an active part in the Water Festivals of Hampshire and West Sussex. This involved a tour of the River Itchen Treatment works, a week of water experiments for visitors at Staunton Country Park and a stand at Arundel promoting water efficiency.

FUTURE DEVELOPMENT AND PERFORMANCE

Cautionary statement regarding forward-looking statements

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

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

The Company will continue to focus on service delivery to customers. It will aim to remain at the efficiency frontier for operating and capital maintenance expenditure and complete its AMP4 investment programme.

Financial Performance will be influenced by the price limits set by the Regulator in 2004, which, for the five year period to 2010, are as follows:

	2005/06	2006/07	2007/08	2008/09	2009/10
% increase above inflation	-0.7	-0.6	1.5	2.5	1.0

Capital expenditure in 2008/09 will be £14.3m (2008 - £12.0m), and will include £2.9m for blending facilities to deal with nitrates. Expenditure will reduce to £8.4m in 2009/10.

Energy costs represent almost 10% of total operating costs. The current electricity contract comes to an end in October 2008, and there remains great uncertainty as to the movement of prices and the impact on the business.

As a result of these factors, the Company anticipates that debt will rise from the March 2008 level of £79.0m to £85.0m in 2009 before falling to £84.7m in 2010. The increase in debt will be met by existing loan facilities. It is anticipated that, by 2010, net debt to RCV will be approximately 77.7%.

RISKS AND UNCERTAINTIES

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

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

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

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

Water quality is monitored by a comprehensive sampling regime in accordance with DWI standards. Furthermore, a telemetry system linked to all treatment works provides an alarm if there is a failure of equipment. The Company also maintains two days' storage of treated water in service reservoirs to provide sufficient time for any water quality issues at treatment works to be rectified before supply to customers. In addition, it has membrane filtration at three treatment works considered most at risk from cryptosporidium being present in the raw water and will commission additional plants at two more works by the summer of 2008.

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

The major environmental risk faced by the Company at the present time is a potential loss of abstraction licence resulting from measures that may be required by the EA to allow the UK to comply with the European Habitats Directive. Investigations have been carried out into the impact of abstraction by the Company at a number of sites covered by the Habitats Directive.

A study into the sustainability of abstraction from the River Itchen is complete and options have been reviewed with the EA and Southern Water for minimising the potential impact of abstraction on salmon migration, southern damselfly and invertebrates. The EA have made their decisions on the changes they require in the abstraction of water by both Portsmouth Water and Southern Water who also have an abstraction upstream of the Portsmouth facility. The full implication of this decision has yet to be assessed but could result in some of the measures required to address the potential supply/demand imbalance in 2020 identified on page 7 being brought forward.

Chichester and Langstone Harbours are Special Protection Areas (SPA) under the Habitats Directive. A comprehensive ecological and hydrological study carried out by the Company examined the effects on Chichester Harbour and its wildlife of operating the Company's Fishbourne source within the existing abstraction licence. The study has focused particularly on the significance of an adequate freshwater flow into the Harbour for wading birds and on maintaining a habitat for the rare Desmoulins Whorl Snail. Another study conducted by the EA considered the importance of freshwater flows into Langstone Harbour from the Springs at Havant and Bedhampton. The EA has announced its conclusions on these licences and the Company believes the required changes will have little impact on its ability to match supply and demand.

The flooding in various parts of the UK during the summer of 2007 has prompted several national reports. Whilst the Company was not affected in 2007, it has put in hand a thorough review of company response and contingency plans together with a fresh look at the vulnerability of key assets.

Regulatory risk relates to decisions taken by Ofwat at the five yearly price review and the potential failure to meet the monitoring plan agreed with Ofwat, containing targets for the period 2005 to 2010 for the capital programme, customer service and leakage. Failure to meet the monitoring plan targets could result in Ofwat taking action, including financial penalties. The last price review was completed in 2004, for the period 2005 to 2010, and the next review will be in 2009, for the period 2010 to 2015. The price review is conducted in an open and transparent manner and the Company actively participates in the process. The performance against the monitoring plan is reviewed on a monthly basis by the Board or the Executive Directors. The performance against the measures in the monitoring plan are discussed on pages 4 to 5.

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

These include:

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

N. J. Roadnight	N. Smith
Managing Director	Finance Director

This report has been prepared in accordance with the Directors' Remuneration Report Regulations 2002 and the Listing Rules of the Financial Services Authority.

Information not subject to audit

Remuneration Committee

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

The Level and Make-up of Remuneration

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

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

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

No Director is involved in deciding his own remuneration.

Information subject to audit

Directors' remuneration:

	2008 **£000**	**2007** **£000**
Total remuneration	558	531
Highest paid Director	153	147

Remuneration is analysed by Director below:

	Salary/Fees **£000**	**Benefits** **£000**	**Total** **2008** **£000**	**Total** **2007** **£000**
Executive:				
J. E. Cogley	99	11	110	106
A. R. Neve	99	8	107	102
N. J. Roadnight	139	14	153	147
N. Smith	104	14	118	114
Non-executive:				
T. M. Lazenby (Chairman)	30	-	30	24
R. L. Sullivan	20	-	20	19
R. J. Tennant	20	-	20	19
	511	47	558	531

Fees paid in respect of Mr. T. M. Lazenby are paid to Seamab Consultancy Ltd.

Benefits comprise company cars and medical insurance.

Long-term incentive schemes

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

As noted below the Executive Directors each hold shares in South Downs Capital Limited, the ultimate parent undertaking, and will benefit from the long term success of the Group which includes Portsmouth Water Limited. The remuneration package of the executive Directors, as reported in the accounts, did not include a performance related element. From April 2009 it is intended that their salary will include a performance related element, which will be based upon the achievement of agreed financial and customer service targets, which are yet to be agreed.

Share options

The Company does not operate an Executive Share Option Scheme.

The Directors' holdings of shares in South Downs Capital Limited, the ultimate parent undertaking, are detailed below and, in total, represent 15% of the issued share capital of that Company. They have no interests in the shares of Portsmouth Water Limited.

	C' Ordinary Shares
J. E. Cogley	30
A. R. Neve	30
N. J. Roadnight	48
N. Smith	42

Pensions

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

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

The executive Directors have accrued pension benefits under the Brockhampton Pension Scheme during the year as detailed below:

	Increase in Accrued Pension During Year to 31 March 2008 £000	**Transfer Value of Increase £000**	**Accumulated Accrued Pension at 31 March 2008 £000**	**Accumulated Accrued Pension at 31 March 2007 £000**
J. E. Cogley	2	27	64	60
A. R. Neve	2	28	64	60
N. J. Roadnight	3	40	86	80
N. Smith	2	25	52	48

The accumulated accrued pension is the leaving service benefit to which the Director is entitled if he were to leave service at the end of the year.

The increase in accrued pension excludes any increase for inflation.

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

BY ORDER OF THE BOARD
T. M. LAZENBY
CHAIRMAN
HAVANT
26 JUNE 2008

For the year ended 31 March 2008

	Notes	Appointed 2008 £000	Non Appointed 2008 £000	Total 2008 £000	Appointed 2007 £000 restated	Non Appointed 2007 £000 restated	Total 2007 £000 restated
TURNOVER	2	33,852	54	33,906	32,973	69	33,042
Operating costs	3	(23,462)	(36)	(23,498)	(21,584)	(49)	(21,633)
Historical cost depreciation		(3,027)	-	(3,027)	(2,694)	-	(2,694)
Operating income	4	(183)	-	(183)	912	-	912
OPERATING PROFIT		7,180	18	7,198	9,607	20	9,627
Other income	5	-	204	204	-	127	127
Interest receivable	6	4,331	-	4,331	3,612	-	3,612
Other finance income	20	2,851	-	2,851	2,688	-	2,688
Interest payable and similar charges	7	(6,215)	-	(6,215)	(5,333)	-	(5,333)
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION		8,147	222	8,369	10,574	147	10,721
Taxation	8						
- Current Tax		(1,877)	(67)	(1,944)	(1,982)	(44)	(2,026)
- Deferred Tax		1,797	-	1,797	(570)	-	(570)
PROFIT FOR THE FINANCIAL YEAR		8,067	155	8,222	8,022	103	8,125
Dividends	9	(4,054)	(155)	(4,209)	(4,368)	(103)	(4,471)
RETAINED PROFIT FOR THE FINANCIAL YEAR		4,013	-	4,013	3,654	-	3,654

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

For the year ended 31 March 2008

	Notes	Appointed 2008 £000	Non Appointed 2008 £000	Total 2008 £000	Appointed 2007 £000 restated	Non Appointed 2007 £000 restated	Total 2007 £000 restated
Profit for the financial year		8,067	155	8,222	8,022	103	8,125
Actuarial gain/(loss) on pension scheme	20	7,602	-	7,602	(519)	-	(519)
Deferred tax relating to actuarial (gain)/loss on pension scheme	18	(2,129)	-	(2,129)	155	-	155
Effect of change to corporation tax rate on pension asset		(292)	-	(292)	-	-	-
Total recognised gains and losses relating to the year		13,248	155	13,403	7,658	103	7,761

As at 31 March 2008

	Notes	Appointed 2008 £000	Non Appointed 2008 £000	Total 2008 £000	Appointed 2007 £000 restated	Non Appointed 2007 £000 restated	Total 2007 £000 restated
FIXED ASSETS							
Tangible	10	85,564	-	85,564	82,301	-	82,301
Investments							
- Loan to group company	11	60,478	-	60,478	59,940	-	59,940
- Other	13	4	-	4	4	-	4
		146,046	-	146,046	142,245	-	142,245
CURRENT ASSETS							
Stores		468	-	468	462	-	462
Debtors	12	4,049	-	4,049	3,720	-	3,720
Cash and short-term deposits	14	2,427	67	2,494	2,416	44	2,460
Infrastructure renewals prepayment		272	-	272	-	-	-
		7,216	67	7,283	6,598	44	6,642
CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR							
Infrastructure renewals accrual		-	-	-	(870)	-	(870)
Borrowings	15	(4,284)	-	(4,284)	(1,784)	-	(1,784)
Corporation tax payable		(928)	(67)	(995)	(1,017)	(44)	(1,061)
Unpaid dividend		(2,290)	-	(2,290)	(3,027)	-	(3,027)
Other creditors	16	(10,447)	-	(10,447)	(11,458)	-	(11,458)
NET CURRENT LIABILITIES		(10,733)	-	(10,733)	(11,558)	-	(11,558)
TOTAL ASSETS LESS CURRENT LIABILITIES		135,313	-	135,313	130,687	-	130,687
CREDITORS: AMOUNTS FALLING DUE AFTER ONE YEAR							
Borrowings	17	(77,239)	-	(77,239)	(74,282)	-	(74,282)
PROVISIONS FOR LIABILITIES							
Deferred Taxation	18	(8,344)	-	(8,344)	(9,565)	-	(9,565)
NET ASSETS EXCLUDING PENSION ASSET		49,730	-	49,730	46,840	-	46,840
Pension asset	20	21,584	-	21,584	15,280	-	15,280
NET ASSETS INCLUDING PENSION ASSET		71,314	-	71,314	62,120	-	62,120
CAPITAL AND RESERVES							
Called up share capital		1,078	-	1,078	1,078	-	1,078
Share premium account	19	1,539	-	1,539	1,539	-	1,539
Capital redemption reserve	19	3,250	-	3,250	3,250	-	3,250
Profit and loss account	19	65,447	-	65,447	56,253	-	56,253
		71,314	-	71,314	62,120	-	62,120

For the year ended 31 March 2008

	Statutory UK GAAP £m	Regulatory £m	Commentaries
PROFIT AND LOSS ACCOUNT			
Operating profit	7,585	7,198	See a) below
BALANCE SHEET			
Tangible fixed assets (net book value)	87,308	85,564	See b) below

a) The difference relates to the way these figures have been presented in both sets of accounts. In the Statutory Accounts, this figure excludes the (£0.183m) for loss on sale of fixed assets as it is reported below the operating profit line in the profit and loss account, but includes other income of £0.204m. In the Regulatory Accounts the amount shown includes the (£0.183m) for loss on sale of fixed assets but reports the other income below the operating profit line.

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

1 ACCOUNTING POLICIES

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

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

The principal accounting policies are as follows:

(a) Turnover

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

(b) Fixed assets

(i) Infrastructure assets - mains

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

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

(ii) Other assets

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

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

(c) Capital contributions

(i) Mains contributions

In certain circumstances third parties make non-returnable contributions towards the cost of specific infrastructure assets. They are treated as capital contributions and the Directors consider it appropriate that, in order to present a true and fair view, they should be deducted from fixed assets, as shown in note 10 to the accounts on page 22. In accordance with the Companies Act 1985 requirement to include fixed assets at cost, such contributions would normally be treated as deferred income and released to the profit and loss account over the useful life of the corresponding assets. However, the assets to which they relate do not have determinable finite lives and, accordingly, no basis exists on which to recognise those contributions as deferred income.

(ii) Infrastructure charges

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

(d) Investments

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

(e) Stocks

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

(f) Deferred taxation

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

The deferred tax balances have been discounted using a post-tax yield to maturity that could be obtained at the balance sheet date on government bonds with maturity dates similar to those of the deferred tax liabilities.

(g) Leases

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

(h) Pension costs and other post retirement benefits

Portsmouth Water Limited is the participating employer in the Brockhampton Pension Scheme. This scheme is a defined benefit scheme. The assets of the scheme are held in a separate trustee administered fund.

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

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

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

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

(i) Financial instruments

The Company's financial instruments consist of loans and receivables, financial assets at fair value through profit or loss, available-for-sale financial assets and held-to-maturity investments.

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

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

Other financial assets consist of short term bank deposits and are classified as financial assets at fair value through the profit and loss account. They are measured at fair value.

The Company's financial liabilities consist of fixed rate borrowings in the form of perpetual debentures and an index linked loan. These instruments are classified as financial liabilities and are measured at amortised cost. There are also variable rate loans which are measured at fair value.

Change in accounting policy

The Company has, for the first time, included a debtor for unbilled measured income as at the year end date in these financial statements, as more fully explained in note 1(a) above. This represents a change in accounting policy and comparative figures have been restated accordingly.

The effect of this change in accounting policy was to;
(i) Increase turnover by £0.329m (2007 - £0.226m).
(ii) Increase profits after taxation by £0.231m (2007 - £0.159m)
(iii) Increase accrued income in the balance sheet by £2.273m (2007 - £1.944m)
(iv) Increase net assets after provision for tax in the balance sheet by £1.591m (2007 - £1.361m)

2. TURNOVER

	Appointed 2008 £000	Non Appointed 2008 £000	Total 2008 £000	Appointed 2007 £000 restated	Non Appointed 2007 £000 restated	Total 2007 £000 restated
Unmeasured supplies	21,396	-	21,396	20,586	-	20,586
Measured supplies	8,530	-	8,530	7,594	-	7,594
Measured large users	2,106	-	2,106	2,122	-	2,122
SWS Bulk Supply	530	-	530	940	-	940
Third party services	1,140	54	1,194	1,597	69	1,666
Other sources	150	-	150	134	-	134
	33,852	54	33,906	32,973	69	32,042

3. ANALYSIS OF OPERATING COSTS

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

	Appointed 2008 £000	Non Appointed 2008 £000	Total 2008 £000	Appointed 2007 £000	Non Appointed 2007 £000	Total 2007 £000
Manpower costs	8,450	26	8,476	7,064	21	7,085
Other costs of employment	198	-	198	200	-	200
Power	1,734	-	1,734	1,485	-	1,485
Rates	2,287	-	2,287	2,235	-	2,235
Hired and contracted services	3,065	5	3,070	2,810	9	2,819
Materials and consumables	1,326	5	1,331	1,393	19	1,412
Service charges	1,718	-	1,718	1,668	-	1,668
Infrastructure renewals charge	3,633	-	3,633	3,527	-	3,527
Provision for bad and doubtful debts	396	-	396	352	-	352
Other operating costs	655	-	655	850	-	850
	23,462	36	23,498	21,584	49	21,633

Other operating costs include payments made to the EOS Foundation, which is a charitable trust used to assist customers in debt. Due to the fact that the Fund is in credit it was not necessary to make any donations this year (2007 - Nil).

4. OPERATING INCOME

	Appointed 2008 £000	Non Appointed 2008 £000	Total 2008 £000	Appointed 2007 £000	Non Appointed 2007 £000	Total 2007 £000
(Loss)/profit arising on disposal of fixed assets	(183)	-	(183)	912	-	912

5. OTHER INCOME

	Appointed 2008 £000	Non Appointed 2008 £000	Total 2008 £000	Appointed 2007 £000	Non Appointed 2007 £000	Total 2007 £000
Rents	-	72	72	-	75	75
Commission from Southern Water Services	-	126	126	-	34	34
Home Assistance Service	-	6	6	-	18	18
	-	204	204	-	127	127

6. INTEREST RECEIVABLE

	2008 £000	2007 £000
Loan to Group Company	4,223	3,532
Interest on short term deposits	78	61
Other interest receivable	30	19
	4,331	3,612

			2008	2007
7.	**INTEREST PAYABLE AND SIMILAR CHARGES**		**£000**	**£000**
	£66.5m loan	- interest	2,827	2,725
		- indexation	2,900	2,404
		- amortisation of fees	57	57
		- administration expenses	22	22
			5,806	5,208
	Other bank loans and overdraft		384	105
	Debenture stocks		10	10
	Other interest payable		15	10
			6,215	5,333

		2008	2007
8.	**TAXATION**	**£000**	**£000 restated**
	Current tax		
	United Kingdom corporation tax at 30% (2007 - 30%)	1,951	2,005
	Adjustment in respect of prior periods	(7)	21
		1,944	2,026
	Deferred tax		
	Origination and reversal of timing differences 664		915
	(Increase) in discount	(141)	(554)
	Effect of removal of IBA's	(1,403)	-
	Effect of changes to corporation tax and capital allowance rates	(592)	-
	Difference between pension cost charge and pension cost relief	153	460
	Effect of change to corporation tax rate on pension asset	(729)	-
		(1,797)	570
	Tax on profit on ordinary activities	147	2,596

The tax charge for the year is lower (2007 - lower) than the standard rate of corporation tax in the UK of 30%. The difference is explained as follows:

	2008	2007
Profit on ordinary activities before tax	8,369	10,721
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 30% (2007 - 30%)	2,511	3,216
Effect of:		
Expenses not deductible for tax purposes	69	12
Depreciation for the period in excess of capital allowances	(671)	477
Revenue items charged to capital	206	(966)
Rolled over chargeable gains	-	(274)
Difference between pension cost charge and pension cost relief	(164)	(460)
Adjustments to tax charge in respect of prior periods	(7)	21
Current tax charge for year	1,944	2,026

9. DIVIDENDS

	2008 £000	2007 £000
Equity: Ordinary/'A' Ordinary		
- interim paid	2,422	2,715
- final paid	1,640	1,418
- special paid	147	338
	4,209	4,471

The Directors are proposing the payment of a final dividend of £2.088m for the year ended 31 March 2008. This dividend has not been accounted for within the current year financial statements as it has yet to be approved.

Part of the total dividend paid by the Company is attributable to the income received from the inter-company loan to South Downs. This element should be excluded to show the dividend attributable to the ongoing operation of the business. The dividends therefore comprise:

	2008 £000	2007 £000
Dividend attributable to the operations of the business	1,699	1,909
Net benefit from interest received on the inter-company loan	2,518	2,327
Special dividend	147	338
	4,364	4,574
Less dividend attributable to non-appointed business	(155)	(103)
	4,209	4,471

The policy for the Company is to grow the dividend attributable to operations through to 2010 in real terms by 2.0% per annum subject to operating cost outperformance and the timing of the cashflow over the reporting year. This is consistent with the approach taken by Ofwat at the Final Determination. The interim dividend paid in December 2007 was based on the cashflow for the 6 months to September which was lower than normal. Hence the dividend approved and paid in the year was lower than the previous year, but over the whole 5 year period the trend will be for a 2% growth.

The special dividend represents 50% of the profit on sale of property concluded in the second half of 2006/07, for which the dividend was paid in the report year.

10. TANGIBLE FIXED ASSETS

	Operational Assets £000	Infrastructure Assets £000	Other Tangible Assets £000	Total £000
HISTORICAL COST				
At 1 April 2007	69,582	40,916	9,768	120,266
Additions	5,530	525	1,203	7,258
Disposals	(231)	-	(120)	(351)
At 31 March 2008	74,881	41,441	10,851	127,173
DEPRECIATION				
At 1 April 2007	14,553	-	6,277	20,830
Charge for year	2,110	-	917	3,027
Disposals during year	(39)	-	(97)	(136)
At 31 March 2008	16,624	-	7,097	23,721
NET BOOK VALUE				
At 31 March 2008	58,257	41,441	3,754	103,452
At 1 April 2007	55,029	40,916	3,491	99,436
CAPITAL CONTRIBUTIONS				
At 1 April 2007	-	17,135	-	17,135
Received during year	-	753	-	753
At 31 March 2008	-	17,888	-	17,888
NET BOOK VALUE AFTER DEDUCTING CAPITAL CONTRIBUTIONS				
At 31 March 2008	58,257	23,553	3,754	85,564
At 1 April 2007	55,029	23,781	3,491	82,301

In the preparation of its Statutory Accounts, the Company has followed common industry practice and adopted the infrastructure renewals accounting basis as set out in FRS 15 : Tangible Fixed Assets. However, for the purposes of the Regulatory Accounts, Ofwat has requested that FRS 15 is not applied for infrastructure renewals accounting, thereby providing a basis consistent with prior years. A reconciliation to the balance sheet shown in the Statutory Accounts is provided below:

	Infrastructure Assets £000
COST	
Cost at 31 March 2008 per Regulatory Accounts	41,441
Adjustment to opening balance	31,136
Infrastructure renewals expenditure capitalised since 1 April 1999	31,332
Disposals since 1 April 1999	(1,870)
Cost at 31 March 2008 per Statutory Accounts	102,039
DEPRECIATION	
At 31 March 2008 per Regulatory Accounts	-
Adjustment to opening balance	31,136
Depreciation charge for infrastructure renewals since 1 April 1999	29,588
Disposals	(1,870)
At 31 March 2008 per Statutory Accounts	58,854
NET BOOK VALUE	
At 31 March 2008 per Regulatory Accounts	41,441
Adjustments for infrastructure renewals accounting since 1 April 1999	1,744
At 31 March 2008 per Statutory Accounts	43,185

11. FIXED ASSET INVESTMENT

	Loan to Group Undertakings
At 1 April 2007	59,940
Addition	538
At 31 March 2008	60,478

12. DEBTORS

	2008 £000	2007 £000 restated
Trade debtors	1,064	1,095
Amounts owed by Group companies	66	51
Prepayments and accrued income	2,811	2,187
Other debtors	108	387
	4,049	3,720

All of the above amounts fall due within one year

As at 31 March 2008, trade debtors with a carrying value of £2.573m (2007 - £2.196m) were provided for. The amount of the provision was £1.794m as at 31 March 2008 (2007 - £1.607m).

The ageing of these debtors was as follows:

	2008 £000	2007 £000
Up to 12 months	976	750
Over 12 months	1,597	1,446
	2,573	2,196

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

Movement on the provision for bad debt are as follows:

	2008 £000	2007 £000
As at 1 April 2007	1,607	1,466
Provision for bad debt required in the year	396	352
Debt written off in the year as uncollectable	(209)	(211)
As at 31 March 2008	1,794	1,607

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

13. INVESTMENTS

	2008 £000	2007 £000
Unlisted investments	4	4

14. CASH AT BANK AND IN HAND

Of the total amount shown of £2.494m, £1.463m (2007 - £1.408m) is held specifically for the payment of the next half yearly loan interest charges.

15. BORROWINGS: DUE WITHIN ONE YEAR

	2008 £000	2007 £000
3% Perpetual debenture stock	60	60
3½% Perpetual debenture stock	185	185
4% Perpetual debenture stock	39	39
Bank loan	4,000	1,500
	4,284	1,784

The £4m bank loan is part of a five year £15m working capital facility, which is secured upon the assets of the Company and bears interest at London Interbank rates.

16. OTHER CREDITORS	Appointed 2008 £000	Non Appointed 2008 £000	Total 2008 £000	Appointed 2007 £000	Non Appointed 2007 £000	Total 2007 £000
Payments received on account	1,273	-	1,273	1,390	-	1,390
Trade creditors	714	-	714	2,143	-	2,143
Amounts owed to Group companies	725	-	725	619	-	619
Social security and other taxation	208	-	208	201	-	201
Other creditors	2,203	-	2,203	1,967	-	1,967
Accruals	463	-	463	403	-	403
Water rates in advance	4,861	-	4,861	4,735	-	4,735
	10,447	-	10,447	11,458	-	11,458

17. BORROWINGS: DUE AFTER ONE YEAR	2008 £000	2007 £000
Bank loan	78,633	75,733
Less: deferred arrangement costs	1,394	1,451
	77,239	74,282

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

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

18. PROVISIONS FOR LIABILITIES	2008 £000	2007 £000
DEFERRED TAXATION:		
At 1 April 2007	9,565	9,455
Provided during the year in profit and loss account	(1,221)	110
At 31 March 2008	8,344	9,565

The total deferred tax balance before the effect of discounting is £9.426m (2007 - £15.512m). The amount provided for deferred taxation represents timing differences caused by the excess of tax allowances over depreciation.

	2008 £000	2007 £000
Deferred tax excluding that relating to pension asset:		
Accelerated capital allowances	8,344	9,565
Pension asset (note 20)	8,394	6,549
Total provision for deferred tax	16,738	16,114
At 1 April 2007	16,114	15,699
Deferred tax charge in profit and loss account (note 8)	(1,797)	570
Deferred tax charged to the statement of total recognised gains and losses	2,421	(155)
At 31 March 2008	16,738	16,114

The 2007 Finance Act reduced the corporation tax rate from 30% to 28% with effect from 1 April 2008. The deferred tax balances have therefore been re-measured resulting in a credit to the profit and loss account of £0.992m.

The abolition of Industrial Buildings Allowances (IBA's) was announced in the 2007 Budget and as a consequence timing differences in respect of IBA's are no longer recognised. This has resulted in a credit to the profit and loss account of £1.403m.

No provision has been made for deferred tax on gains recognised on the sale of properties where potentially taxable gains have been rolled over into replacement assets. Such tax would become payable only if the property were sold without it being possible to claim rollover relief. The total amount unprovided for is £0.694m (2007 - £0.781m). At present it is not envisaged that any tax will become payable in the foreseeable future.

19. RESERVES

	Share Premium £000	Capital Redemption £000	Profit and Loss £000
As 1 April 2007 as previously reported	1,539	3,250	54,892
Prior year adjustment - unbilled measured income	-	-	1,361
As 1 April 2007 restated	1,539	3,250	56,253
Profit for financial year	-	-	8,222
Dividends	-	-	(4,209)
Actuarial gain on pension scheme	-	-	7,602
Movement on deferred tax relating to pension scheme	-	-	(2,129)
Effect of change to corporation tax rate in pension asset	-	-	(292)
As 31 March 2008	1,539	3,250	65,447

20. PENSIONS

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

The formal actuarial valuation as at 31 March 2005 was updated to the accounting date by an independent qualified actuary in accordance with FRS 17. As required by FRS 17, the value of the defined benefit liabilities has been measured using the projected unit method.

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

	2008 % per annum	2007 % per annum	2006 % per annum
Price inflation	3.7	3.2	3.0
Discount rate	6.7	5.2	4.9
Pension increases (RPI)	3.7	3.2	3.0
Salary growth	6.45	5.95	5.75

On the basis of the assumptions used for life expectancy, a male pensioner currently aged 60 would be expected to live for a further 26.8 years (2007 - 26.7 years). Allowance is made for future improvements in life expectancy.

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

	2008 Expected Return % per annum	2008 Fair Value £000	2007 Expected Return % per annum	2007 Fair Value £000	2006 Expected Return % per annum	2006 Fair Value £000
Equities	7.7	66,777	7.8	76,283	7.4	77,020
Bonds	4.5	33,139	4.5	27,670	4.2	23,583
Other	3.9	7,780	5.4	4,758	4.5	4,296
	6.4	107,696	6.9	108,711	6.6	104,899

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

	2008 £000	2007 £000
Total fair value of scheme assets	107,696	108,711
FRS 17 value of scheme liabilities	77,718	86,882
Gross pension asset	29,978	21,829
Related deferred tax liability	8,394	6,549
Net pension asset	21,584	15,280

Under FRS 17, the scheme is represented on the balance sheet at 31 March 2008 as an asset of £29.978m (2007 - £21.829m), which amounts to £21.584m net of deferred tax (2007 - £15.280m).

The Company remains on a contribution holiday at the present time. This position will be revisited in the light of the results of the 31 March 2008 actuarial valuation. Members were also on a contribution holiday until 1 October 2006 but have now restarted the payment of contributions (at a reduced rate for the first year and at the full rate since 1 October 2007).

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

	2008 £000	2007 £000
Opening scheme liabilities	86,882	84,086
Employer's part of current service cost	2,304	2,275
Interest cost	4,500	4,116
Contributions by scheme participants	177	51
Benefits paid	(3,161)	(2,508)
Past service credit	-	(1,122)
Actuarial gain	(12,984)	(16)
Closing scheme liabilities	77,718	86,882

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

Opening fair value of scheme assets	108,711	104,899
Expected return on assets	7,351	6,804
Contributions by scheme participants	177	51
Benefits paid	(3,161)	(2,508)
Actuarial loss	(5,382)	(535)
Closing fair value of scheme assets	107,696	108,711

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

Current service cost (employer's part only)	2,304	2,,275
Past service cost	-	(1,122)
Total operating charge	2,304	1,153

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

	2008 £000	2007 £000
Expected return on pension scheme assets	7,351	6,804
Interest on post retirement liabilities	(4,500)	(4,116)
Net return	2,851	2,688
Total credit recognised in the profit and loss account	547	1,535

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

	2008	2007
Actual return less expected return on scheme assets	(5,382)	(535)
Experience gains arising on scheme liabilities	-	-
Gain due to changes in assumptions underlying the FRS 17 value of scheme liabilities	12,984	16
Actuarial gain/(loss) recognised in the STRGL	7,602	(519)

The actual return on plan assets was £1.969m in the year to 31 March 2008 (2007 - £6.269m).

The history of experience gains and losses is:

	2008	2007	2006	2005	2004
Present value of scheme liabilities (£000)	(77,718)	(86,882)	(84,086)	(71,593)	(66,845)
Total fair value of scheme assets (£000)	107,696	108,711	104,899	87,984	81,058
Surplus (£000)	29,978	21,829	20,813	16,391	14,213
Actual return less expected return on scheme assets (£000)	(5,382)	(535)	13,587	3,565	14,123
Percentage of scheme's assets	(5)%	0%	13%	4%	17%
Experience gains arising on scheme's liabilities (£000)	-	-	65	61	207
Percentage of the FRS 17 value of the scheme's liabilities	-	-	-	-	-
Total amount recognised in the STRGL (£000)	7,602	(519)	4,527	2,237	(7,694)
Percentage of the FRS 17 value of the scheme's liabilities	10%	0%	5%	3%	(12%)

The cumulative amount recognised in the STRGL as at 31 March 2008 was a loss of £6.977m (2007 - loss of £14.579m).

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

CURRENT COST PROFIT AND LOSS ACCOUNT
FOR THE APPOINTED BUSINESS

For the year ended 31 March 2008

	Notes	2008 £000	2007 £000 restated
TURNOVER		33,852	32,973
Current cost operating costs	2	(28,011)	(25,521)
Operating income	3	(631)	332
		5,210	7,784
Working capital adjustment	4	330	237
CURRENT COST OPERATING PROFIT		5,540	8,021
Interest receivable		4,331	3,612
Other finance income		2,851	2,688
Interest payable and similar charges		(6,215)	(5,333)
Financing adjustment	4	68	77
CURRENT COST PROFIT BEFORE TAXATION		6,575	9,065
Taxation			
- Current Tax		(1,877)	(1,982)
- Deferred Tax		1,797	(570)
CURRENT COST PROFIT FOR THE FINANCIAL YEAR		6,495	6,513
Dividends		(4,054)	(4,368)
CURRENT COST PROFIT RETAINED		2,441	2,145

CURRENT COST BALANCE SHEET
FOR THE APPOINTED BUSINESS

As at 31 March 2008

	Notes	2008 £000	2007 £000 Restated
FIXED ASSETS			
Tangible fixed assets	5	720,014	691,927
Third party contributions since 1989/90		(19,390)	(17,955)
		700,624	673,972
Working capital	6	(5,302)	(6,735)
Cash		967	1,016
Short term deposits		1,460	1,400
Infrastructure renewals accrual		272	(870)
NET OPERATING ASSETS		698,021	668,783
NON OPERATING ASSETS AND LIABILITIES			
Borrowings		(4,284)	(1,784)
Non-trade debtors		58	44
Non-trade creditors: amounts falling due within one year		(687)	(585)
Investment - loan to group company		60,478	59,940
- other		4	4
Corporation tax payable		(928)	(1,017)
Dividends		(2,290)	(3,027)
TOTAL NON OPERATING ASSETS AND LIABILITIES		750,372	722,358
CREDITORS: AMOUNTS FALLING DUE AFTER ONE YEAR			
Borrowings		(77,239)	(74,282)
PROVISIONS FOR LIABILITIES AND CHARGES		673,133	648,076
Deferred tax provision		(8,344)	(9,565)
NET ASSETS EXCLUDING PENSION ASSET		664,789	638,511
Pension asset		21,584	15,280
NET ASSETS INCLUDING PENSION ASSET		686,373	653,791
CAPITAL AND RESERVES			
Called up share capital		1,078	1,078
Share premium account		1,539	1,539
Capital redemption reserve		3,250	3,250
Profit and loss account	7	32,250	24,628
Current cost reserve	8	648,256	623,296
		686,373	653,791

CURRENT COST CASH FLOW STATEMENT

For the year ended 31 March 2008

	Notes	Appointed 2008 £000	Non Appointed 2008 £000	Total 2008 £000	Appointed 2007 £000	Non Appointed 2007 £000	Total 2007 £000
NET CASH INFLOW FROM OPERATING ACTIVITIES	9	15,774	222	15,996	15,989	147	16,136
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE							
Interest received		3,780	-	3,780	3,156	-	3,156
Interest paid		(3,257)	-	(3,257)	(2,869)	-	(2,869)
NET CASHFLOW FROM RETURNS ON INVESTMENT AND SERVICING OF FINANCE		523	-	523	287	-	287
TAXATION							
UK corporation tax paid		(1,866)	(44)	(1,910)	(2,186)	(71)	(2,257)
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT							
Purchase of tangible fixed assets		(8,139)	-	(8,139)	(8,603)	-	(8,603)
Receipt of contributions		753	-	753	945	-	945
Infrastructure renewals expenditure		(4,775)	-	(4,775)	(4,145)	-	(4,145)
Sale of tangible fixed assets		32	-	32	1,167	-	1,167
NET CASH OUTFLOW FROM INVESTING ACTIVITIES		(12,129)	-	(12,129)	(10,636)	-	(10,636)
EQUITY DIVIDENDS PAID		(4,791)	(155)	(4,946)	(4,476)	(103)	(4,579)
CASH (OUTFLOW)/INFLOW BEFORE MANAGEMENT OF LIQUID RESOURCES AND FINANCING		(2,489)	23	(2,466)	(1,022)	(27)	(1,049)
MANAGEMENT OF LIQUID RESOURCES							
(Purchase) of short term deposits		(60)	-	(60)	(50)	-	(50)
NET CASHFLOW BEFORE FINANCING		(2,549)	23	(2,526)	(1,072)	(27)	(1,099)
FINANCING							
New loans		2,500	-	2,500	1,500	-	1,500
(DECREASE)/INCREASE IN CASH IN THE YEAR	10	(49)	23	(26)	428	(27)	401

1. ACCOUNTING POLICIES

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

The accounting policies used are the same as those adopted in the historical cost accounts as shown on pages 17 and 18, except as set out below:

Tangible Fixed Assets

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

Modern Equivalent Asset (MEA) Valuation

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

Land and buildings

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

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

Infrastructure assets

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

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

Other operational fixed assets

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

Surplus land

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

Third party contributions

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

Real Financial Capital Maintenance Adjustments

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

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

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

Other Current Cost Adjustments

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

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

2. CURRENT COST OPERATING COSTS

	2008 £000	2007 £000
Operating costs per historical cost accounts	26,489	24,278
Current cost depreciation adjustment (note 1)	1,522	1,243
	28,011	25,521

3. OPERATING INCOME

	2008 £000	2007 £000
Current cost (loss)/profit arising on disposal of fixed assets	(631)	332

4. WORKING CAPITAL AND FINANCING ADJUSTMENTS

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

5. TANGIBLE FIXED ASSETS

	Operational Assets £000	Infrastructure Assets £000	Other Tangible Assets £000	Total £000
GROSS CURRENT REPLACEMENT COST				
At 1 April 2007	172,188	573,841	11,866	757,895
RPI adjustment	6,421	21,617	442	28,480
Disposals	(1,734)	-	(144)	(1,878)
Additions	5,530	526	1,203	7,259
At 31 March 2008	182,405	595,984	13,367	791,756
DEPRECIATION				
At 1 April 2007	57,894	-	8,074	65,968
RPI adjustment	2,140	-	300	2,440
Disposals during year	(1,094)	-	(121)	(1,215)
Charge for year	3,552	-	997	4,549
At 31 March 2008	62,492	-	9,250	71,742
NET BOOK VALUE				
At 31 March 2008	119,913	595,984	4,117	720,014
At 1 April 2007	114,294	573,841	3,792	691,927

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

6. WORKING CAPITAL

		2008 £000	2007 £000
Stores		468	462
Trade debtors	- measured household	11	7
	- unmeasured household	1,137	889
	- measured non-household	280	208
	- unmeasured non-household	12	9
	- other	285	507
Measured income accrual		2,274	1,944
Prepayments and other debtors		538	243
Trade creditors		(714)	(1,047)
Deferred income - customer advance receipts		(1,936)	(1,915)
Capital creditors		(1,777)	(2,658)
Accruals and other creditors		(5,880)	(5,384)
TOTAL WORKING CAPITAL		(5,302)	(6,735)

7. PROFIT AND LOSS ACCOUNT

		£000
As 1 April 2007 as previously stated		23,325
Prior year adjustments	- unbilled measured income	1,361
	- working capital	(83)
	- finance adjustment	25
As 1 April 2007 restated		24,628
Profit for financial year		2,441
Actuarial gain on pension scheme		7,602
Movement on deferred tax relating to pension scheme		(2,129)
Effect of change to corporation tax rate on pension asset		(292)
As 31 March 2008		32,250

8. CURRENT COST RESERVE

		£000
At 1 April 2007 as previously stated		620,568
Prior year adjustments	- working capital	83
	- finance adjustment	(25)
Transfer of item previously classified as capital contributions		2,670
As 1 April 2007 restated		623,296
RPI adjustments:-		
Fixed assets		26,040
Working capital adjustment		(330)
Net finance adjustment		(68)
Third party contributions		(682)
At 31 March 2008		648,256

9. RECONCILIATION OF OPERATING PROFIT TO NET CASH INFLOW FROM OPERATING ACTIVITIES

	2008 £000	2007 £000
Current cost operating profit	5,540	8,021
Working capital adjustment	(330)	(237)
(Decrease) in working capital	(758)	(212)
Other finance income	2,304	1,153
Current cost depreciation	4,549	3,937
Current cost loss/(profit) on sale of fixed assets	631	(332)
Infrastructure renewals charge	3,633	3,527
Movement in provisions	205	132
NET CASHFLOW FROM OPERATING ACTIVITIES	15,774	15,989

10. ANALYSIS OF NET DEBT

	As at 1 April 2007 £000	Cash Flow £000	Non Cash Movements £000	As at 31 March 2008 £000
Cash at bank and in hand	1,016	(49)	-	967
Loans due after one year	(74,282)	-	(2,957)	(77,239)
Loans due within one year	(1,784)	(2,500)	-	(4,284)
	(76,066)	(2,500)	(2,957)	(81,523)
Short term deposits	1,400	60	-	1,460
Current asset equity investments	4	-	-	4
	1,404	60	-	1,464
	(73,646)	(2,489)	(2,957)	(79,092)

INTEREST RATE RISK PROFILE

	Fixed rate £000	Floating Rate £000	Index linked £000	Total £000
MATURITY PROFILE				
Less than one year	(1,784)	(2,500)	-	(4,284)
Between one and two years	-	-	-	-
Between two and five years	-	-	-	-
Between five and twenty years	-	-	-	-
In more than twenty years	-	-	(77,239)	(77,239)
TOTAL BORROWINGS	(1,784)	(2,500)	(77,239)	(81,523)
Cash and investments				971
Short term deposits				1,460
NET DEBT				(79,092)

CURRENT COST ACTIVITY COST TABLE

	Resources & Treatment £000	Distribution £000	Water Supply Subtotal £000
Direct Costs			
Employment costs	192	2,712	2,904
Power	874	782	1,656
Hired and contracted services	7	425	432
Materials and consumables	329	354	683
Service charges	1,718	-	1,718
Other direct costs	23	44	67
Total direct costs	3,143	4,317	7,460
General and support expenditure	2,210	3,555	5,765
Total functional expenditure	5,353	7,872	13,225
Business Activities			
Customer services			1,826
Scientific services			975
Other business activities			396
Business activities subtotal			3,197
Local authority rates			2,267
Doubtful debts			396
Total opex less third party services			19,085
Third party services - opex			744
Total operating expenditure			19,829
Capital Maintenance			
Infrastructure renewals charge		3,633	3,633
Current cost depreciation			
- service activities	1,875	2,623	4,498
- business activities			51
Total capital maintenance			8,182
Total operating costs			28,011
CCA (MEA) Values			
Service activities	48,126	670,594	718,720
Business activities			1,294
Service totals			720,014
Services for the third parties			-
Total			720,014

Regulatory Capital Value at 2007/08 prices

	£000
Opening Regulatory Capital Value as at 1 April 2007	109,309
Capital Expenditure (excluding infrastructure renewals)	10,091
Infrastructure renewals expenditure	4,520
Infrastructure renewals charge	(4,231)
Capital contributions	(1,326)
Current cost depreciation	(4,675)
Outperformance of regulatory assumptions (5 years in arrears)	(2,516)
Closing Regulatory Capital Value as at 31 March 2008	111,172
Average Regulatory Capital Value for the year	108,422

Explanatory Note

The Table shown above gives the build up of the Regulatory Capital Value for the financial year ended 31 March 2008 that was used by the Office of Water Services in setting price limits for the current period in the 2004 Final Determination of price limits.

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

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

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

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

The Directors are responsible, under Condition F of the Instrument of Appointment by the Secretary of State for the Environment, Food and Rural Affairs (Defra) and as a water undertaker under the Water Industry Act 1991, for preparing the financial statements for each financial year that give a true and fair view of the state of affairs of the Company at the end of the financial year and of the profit or loss of the Company for that period. In preparing those financial statements, the Directors are required to:

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

The Directors are responsible for:

- keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 1985;
- safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities; and
- the maintenance and integrity of the corporate and financial information included on the Company’s website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

In so far as the Directors are aware:

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

Certificate of Compliance with Licence Condition F6A

In arriving at the certificate provided below, the Board met on 26 June 2008 to consider the Appointee's financial and management requirements over the next 12 months and the available resources. The Directors reviewed the following information:

- the latest financial position of the Company through its latest Report and Accounts
- the Management Accounts for May 2008
- the current level of gearing
- the projected level of gearing through to 2010, based on its own internal budget projections
- the Company's available bank and overdraft facilities through to 2010
- the headroom between the projected key operating ratios (gearing and interest cover) and its loan covenants through to 2010

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

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

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

Signed by:

T. M. Lazenby ....

N. J. Roadnight ....

N. Smith ....

A. R. Neve ....

J. E. Cogley ....

R. L. Sullivan ....

R. J. Tennant ....

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

Borrowings or Sums Lent

There is a loan outstanding made to a Group Company, South Downs Limited, in June 2002. The balance of the loan, consisting of the principal amount and accrued interest to date, amounts to £60.478m. This loan was made as a part of the refinancing package which was carried out in the financial year 2002/03. The interest rate for the loan is based on LIBOR plus a margin.

Dividends paid to Associated Undertakings

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

Payments for Tax Losses

Payments relating to the surrender of tax losses to Portsmouth Water Limited, from Group Companies, made to South Downs Limited amounting to £1,223,381.

Supply of Services

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

Service	Associate Company	Turnover of Associate (£000's)	Terms of Supply	Value (£000's)
Rent of operational sites	Brockhampton Holdings Limited	197	Market Tested	57
Rent of operational sites	Brockhampton Property Investments Limited	201	Market Tested	6
Management Charge	South Downs Limited	-	Turnover	53

There is a recharge of Directors salaries amounting to £19,384, paid to Portsmouth Water Limited by Brockhampton Holdings Limited, which represents the time spent by Portsmouth Water Executive Directors on Group matters.

Statement by Board of Directors

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

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

We have audited the regulatory accounts of Portsmouth Water Ltd on pages 14 to 37 which comprise:

- the regulatory historical cost accounting statements comprising the regulatory historical cost profit and loss account, the regulatory historical cost balance sheet and the related notes to the historical cost financial statements; and

- the regulatory current cost accounting statements for the appointed business comprising the current cost profit and loss account, the current cost balance sheet, the current cost cash flow statement and the related notes to the current cost financial statements including the statement of accounting policies.

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

Basis of Preparation

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

The Regulatory Accounts are separate from the statutory financial statements of the Company. There are differences between United Kingdom Generally Accepted Accounting Principles (UK GAAP) and the basis of preparation of information provided in the regulatory accounts because the Regulatory Accounting Guidelines specify alternative treatment or disclosure in certain respects. Where the Regulatory Accounting Guidelines do not specifically address an accounting issue, then they require UK GAAP to be followed. Financial information other than that prepared wholly on the basis of UK GAAP may not necessarily represent a true and fair view of the financial performance or financial position of a company as shown in financial statements prepared in accordance with the Companies Act 1985.

Respective Responsibilities of the WSRA, Directors and Auditors

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

The Directors' responsibilities for preparing the Regulatory Accounts in accordance with Regulatory Accounting Guidelines are set out in the statement of directors' responsibilities for regulatory information on page 38.

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

We report to you our opinion as to whether the regulatory historical cost accounting statements present fairly, under the historical cost convention, the revenues and costs, assets and liabilities of the appointee and its appointed business in accordance with the Company's Instrument of Appointment and Regulatory Accounting Guideline 2.03 (Guideline for the classification of expenditure), Regulatory Accounting Guideline 3.06 (Guideline for the contents of regulatory accounts) and Regulatory Accounting Guideline 4.03 (Guideline for the analysis of operating costs and assets); and whether the regulatory current cost accounting statements on pages 29 to 37 have been properly prepared in accordance with Regulatory Accounting Guideline 1.04 (Guideline for accounting for current costs and regulatory capital values), Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03. We also report to you if, in our opinion, the Company has not kept proper accounting records as required by paragraph 3 of Condition F and whether the information is in agreement with the appointees' accounting records and has been properly prepared in accordance with the requirements of Condition F and, as appropriate, Regulatory Accounting Guideline 1.04, Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.06, and Regulatory Accounting Guideline 4.03.

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

Basis of Audit Opinion

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

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

Our opinion on the Regulatory Accounts is separate from our opinion on the statutory financial statements of the Company on which we report, which are prepared for a different purpose. Our audit report in relation to the statutory accounts of the Company (our "Statutory" audit) was made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our statutory audit work was undertaken so that we might state to the Company's members those matters we are required to state to them in a Statutory auditors' report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume any responsibility to anyone other than the Company and the Company's members as a body, for our Statutory audit work, for our Statutory audit report, or for the opinions we have formed in respect of that Statutory audit.

The regulatory historical cost accounting statements on pages 14 to 28 have been drawn up in accordance with Regulatory Accounting Guideline 3.06 in that infrastructure renewals accounting as applied in previous years should continue to be applied and accordingly that the relevant sections of Financial Reporting Standards 12 and 15 be disapplied. The effect of this departure from Generally Accepted Accounting Principles, and a reconciliation of the balance sheet drawn up on this basis with that drawn up under Companies Act 1985 is given on page 23.

Opinion

In our opinion the Regulatory Accounts of the Company for the year ended 31 March 2008 fairly present in accordance with Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment to the Company as a water undertaker under the Water Industry Act 1991, the Regulatory Accounting Guidelines issued by the WSRA and the accounting policies set out on pages 17 to 18 and page 32, the state of the Company's affairs at 31 March 2008 on an historical cost and current cost basis, the historical cost and current cost profit for the year and the current cost cash flow for the year and have been properly prepared in accordance with those conditions, guidelines and accounting policies.

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

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

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

(c) the regulatory historical cost accounting statements on pages 14 to 28 present fairly, under the historical cost convention, the revenues and costs, assets and liabilities of the Appointee and its Appointed Business in accordance with the Company's Instrument of Appointment and Regulatory Accounting Guideline 2.03, Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03 issued by the WSRA; and

(d) the regulatory current cost accounting statements on pages 29 to 37 have been properly prepared in accordance with Regulatory Accounting Guideline 1.04, Regulatory Accounting Guideline 3.06 and Regulatory Accounting Guideline 4.03 issued by the WSRA.

SAFFERY CHAMPNESS
CHARTERED ACCOUNTANTS
REGISTERED AUDITORS
LION HOUSE RED LION STREET
LONDON
26 JUNE 2008

	2008 £000	2007 £000
KPI - 1		
a) Gearing - Debt/RCV		
(i) Debt		
Bank loan (note 17, page 25)	78,633	75,733
Bank loan (note 15, page 24)	4,000	1,500
Debenture stock (note 15, page 24)	284	284
Cash at bank and in hand	(2,494)	(2,460)
	80,423	75,057

For the purposes of this ratio, debt excludes the deferred arrangement costs of £1.394m (note 17, on page 25) and the current asset investment of £0.004m (note 13, on page 24).

(ii) Regulatory Capital Value (RCV)

Value established by Ofwat in Final Determination in 2004

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

	2008 £000	2007 £000
Regulatory capital value indexed to 31 March	111,172	105,341
(iii) Gearing - Debt/RCV ratio (i) ÷ (ii)	72.3%	71.3%

b) Cash interest cover

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

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

	2008 £000	2007 £000
Net cashflow from operating activities	15,996	16,136
Interest received	3,780	3,156
Taxation	(1,910)	(2,257)
Capital expenditure	(12,129)	(10,636)
New borrowings	2,500	1,500
	8,237	7,899
(ii) Interest paid	3,257	2,869
(iii) Cash interest cover ratio (i) ÷ (ii)	2.53	2.75

KPI - 2 and 3 Customer Service Measures

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

KPI - 4 Water Quality

This indicator is based on figures reported to the DWI.

KPI - 5 Efficiency

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

KPI - 6 Leakage

This indicator is based on figures supplied to Ofwat and confirmed in its report ‘Security of Supply, Leakage and the Efficient Use of Water’. The figures for 2007/08 have been supplied to Ofwat, but will not be confirmed in the Ofwat document until later in 2008.