

**Statutory Accounts and Supplementary
Regulatory Accounting Statements**
for the year ended 31 March 2002



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Preface

for the year ended 31 March 2002

This document includes the statutory Accounts of Southern Water Services Limited to be filed with the Registrar of Companies as required under the Companies Act 1985, together with a set of supplementary regulatory accounting statements required by the Instrument of Appointment (the "Licence") issued to the company by the Secretary of State for the Environment.

The Director General of Water Services ("the Director General") has a duty under the Water Industry Act 1991 to ensure compliance with the conditions of this Licence.

A particular point of definition is worth noting. The "Appointee" is Southern Water Services Limited, appointed in the Licence to be the undertaker. Southern Water Services Limited has other functions and activities which are not regulated by the Licence. These activities are termed the "Non-Appointed Business".

Ring fencing statement

Under Condition K of its Licence, the company is at all times required to ensure, so far as is reasonably practicable, that if a special administration order were made, the company would have available to it sufficient rights and assets (other than financial resources) to enable the special administrator to manage the affairs, business and property of the company.

In the opinion of the directors, the company was in compliance with that requirement as at 31 March 2002.

Protection of the core business (Licence Condition F6A)

The directors state that the company will have available to it sufficient financial resources and facilities to enable it to carry out, for at least 12 months, its regulated activities and sufficient management resources to enable it to carry out its functions.

Directors' responsibilities for the preparation of the supplementary regulatory accounting statements

In addition to their responsibilities to prepare Accounts in accordance with the Companies Act 1985, described on page 2, the directors are also responsible under Condition F of the Licence issued to the company by the Secretary of State for the Environment as a water and sewerage undertaker under the Water Industry Act 1991 for:

- (a) ensuring that proper accounting records are maintained by the Appointee to enable compliance with the requirements of Condition F and having regard also to the terms of guidelines notified by the Director General to the Appointee from time to time;
- (b) preparing on a consistent basis for each financial year accounting statements in accordance with Condition F, having regard also to the terms of guidelines notified by the Director General from time to time, which so far as is reasonably practicable have the same content as the annual Accounts of the Appointee prepared under the Companies Act 1985 and which are prepared in accordance with the formats, accounting policies and principles which apply to those accounts;
- (c) preparing accounting statements on a current cost basis in respect of the same accounting period in accordance with guidelines issued by the Director General from time to time;
- (d) preparing such other accounting and related information as is required by Condition F having regard also to the terms of guidelines issued by the Director General from time to time.

The directors approved the statutory Accounts on pages 4 to 12 on 28 June 2002. They approved the supplementary regulatory accounting statements on pages 14 to 26 and pages 28 to 29 on 28 June 2002.

By order of the Board



Eric Hutchinson
Finance Director
28 June 2002

Report of the Directors

The directors present their report and the audited Accounts for the year ended 31 March 2002.

Results and dividend

The profit after taxation for the financial year amounted to £93.0 million (2001: £126.7 million). The directors recommend a final dividend of £nil per ordinary share (2001: £568.56) together with an interim dividend of £nil per ordinary share (2001: £284.28), making a total dividend of £nil per ordinary share for the year (2001: £852.84). The balance of the profit for the year of £93.0 million (2001: £78.9 million) has been transferred to reserves.

Activities and review

The principal activities of the company are the provision of water supply and wastewater services in the south-east of England.

Research and development

The improvement of existing services and processes, together with the identification and development of new technology and solutions, are key aspects of the company's strategy to enhance the quality of service to customers and improve methods of working. Research and development expenditure for the year amounted to £2.0 million (2001: £2.2 million).

Directors and their interests

The directors who held office at 31 March 2002 were as follows:

Martin Baggs (Appointed: 14 May 2001)
Christopher Chapman
Barrie Delacour
Stuart Derwent
Anthony Fegan
John Harris
Eric Hutchinson
David Stainthorpe

Mr A Nelson was appointed a director and elected Chairman of the Board on 23 April 2002.

None of the directors who held office at the end of the financial year had any disclosable interests in the shares of the company. Nor did any director have any disclosable interests in the shares of Scottish Power plc.

As permitted by Statutory Instrument, the Register of Directors' Interests maintained under Section 325 of the Companies Act 1985 does not contain the interests of directors who are also directors of a company of which the company is a wholly owned subsidiary. Accordingly, the interests of the following directors are disclosed in the Annual Report and Accounts for the year ended 31 March 2002 of Southern Water plc:

Martin Baggs
Barrie Delacour
Stuart Derwent
Anthony Fegan
Eric Hutchinson
David Stainthorpe

Directors' responsibilities

The directors are required by UK company law to prepare Accounts for each financial year which give a true and fair view of the state of affairs of the company as at the end of the financial year and of the profit or loss of the company for that year.

The directors confirm that suitable accounting policies have been used and applied consistently and that reasonable and prudent judgements and estimates have been made in the preparation of the Accounts for the year ended 31 March 2002. The directors also confirm that applicable accounting standards have been followed and that the Accounts have been prepared on the going concern basis.

The directors are responsible for maintaining proper accounting records and sufficient internal controls to safeguard the assets of the company and to prevent and detect fraud or any other irregularities.

Employees

Employee involvement and participation

The company has developed its communications processes with its employees to ensure greater understanding of and involvement in the business. This has been achieved through the "Waterline" staff magazine, produced to complement "Southern Water News", and by staff briefings. The influence of ScottishPower is seen through the extension of the values-based leadership development programme to Southern Water. The ScottishPower Learning business is now firmly established in Southern Water with programmes for school leavers and the long-term unemployed to work alongside and learn from our employees. The Open Learning facilities at all the main company locations reinforce the commitment of the company to providing learning opportunities.

The company continues to work actively with the trade unions and meets with them at senior management level on a regular basis. Key issues for consideration include business reorganisations, consultation on employment policy and discussion of key health and safety issues. As a result of recent changes in the business structure, the company is currently carrying out a review of the consultation arrangements. The objective of this review will be to ensure that all areas of the new organisation are adequately represented for consultation purposes.

Equal opportunity

Southern Water Services policy is to promote equality of opportunity in recruitment, employment continuity, training and career development. The policy is designed to ensure that equal opportunity in these areas extends as far as practicable to people with disabilities. The company is a member of the Employer's Forum on Disability, which supports the efforts to meet the needs of the disabled for employment and access to the company and its buildings.

Health and safety

Every employee receives a copy of the corporate policy statement on health and safety. There are regular meetings of employee representatives and managers to consider all aspects of health and safety, and there is a health and safety management review group which ensures that there is an adequate system for meeting the company's responsibilities for health and safety to its staff, customers and members of the public. Southern Water has its own internal occupational health service, including the provision of physiotherapy. These services are being developed to meet the needs of the business and our employees at work.

Creditor payment policy and practice

The company's current policy and practice concerning the payment of its trade creditors is to follow the Better Payment Practice Code to which it is a signatory. Copies of the Code may be obtained from the Department of Trade and Industry or from the website www.payontime.co.uk.

The company's policy and practice is to settle terms of payment when agreeing the terms of the transaction, to include the terms in contracts and to pay in accordance with its contractual and legal obligations. The company's creditor days at 31 March 2002 were 56 days (2001: 58 days).

Auditors

The auditors, PricewaterhouseCoopers, have indicated their willingness to continue in office, and a resolution concerning their reappointment will be proposed at the Annual General Meeting.

By order of the Board



Kevin Hall
Secretary
28 June 2002

Registered office
Southern House, Yeoman Road,
Worthing, West Sussex BN13 3NX

Profit and Loss Account

for the year ended 31 March 2002

	Notes	2002 £m	2001 £m
Turnover	2	429.9	421.6
Cost of sales	2	(195.9)	(182.1)
Gross profit		234.0	239.5
Administrative expenses	2	(23.4)	(21.9)
Other operating income	2	2.2	2.1
Exceptional item	4	(9.6)	–
Operating profit and profit on ordinary activities before interest and taxation	3	203.2	219.7
Net interest and similar charges	6	(71.9)	(66.3)
Profit on ordinary activities before taxation		131.3	153.4
Tax on profit on ordinary activities	7	(38.3)	(26.7)
Profit on ordinary activities after taxation		93.0	126.7
Dividends	8	–	(47.8)
Retained profit for the financial year	18	93.0	78.9

All items dealt with in the profit and loss account relate to continuing operations.

A statement of total recognised gains and losses and a reconciliation to historical cost profits and losses are not shown as all gains and losses for 2001 and 2002 are recognised in the profit and loss account under the historical cost convention.

The notes on pages 6 to 12 form part of these Accounts.

Balance Sheet

as at 31 March 2002

	Notes	2002 £m	2001 £m
Fixed assets			
Tangible assets	9	2,504.8	2,340.6
Investments	10	–	–
		2,504.8	2,340.6
Current assets			
Stocks	11	4.1	3.6
Debtors: amounts falling due within one year	12	111.8	93.0
		115.9	96.6
Creditors: amounts falling due within one year	13	(939.5)	(714.9)
Net current liabilities		(823.6)	(618.3)
Total assets less current liabilities		1,681.2	1,722.3
Creditors: amounts falling due after more than one year	14	(482.1)	(637.9)
Provision for liabilities and charges			
Other	15(a)	(3.1)	(3.1)
Deferred tax	15(b)	(352.1)	(331.7)
		(355.2)	(334.8)
Grants and contributions	16	(37.4)	(36.1)
Net assets		806.5	713.5
Capital and reserves			
Called up share capital	17	0.1	0.1
Share premium	18	46.3	46.3
Profit and loss account	18	760.1	667.1
Total equity shareholders' funds		806.5	713.5

The notes on pages 6 to 12 form part of these Accounts.

Approved by the Board on 28 June 2002 and signed on its behalf by:



Eric Hutchinson
Finance Director

1 Accounting policies

Basis of accounting

The Accounts have been prepared under the historical cost convention and in accordance with applicable accounting standards in the UK and, subject to the treatment of infrastructure grants and contributions described below, with the requirements of the Companies Act 1985.

Basis of preparation

The Accounts contain information about Southern Water Services Limited as an individual company and do not contain consolidated financial information as the parent of subsidiary companies. The company is exempt under section 228 of the Companies Act 1985 from the requirement to prepare consolidated Accounts as it and its subsidiary undertaking are included by full consolidation in the consolidated Accounts of the ultimate holding company Scottish Power plc, a company registered in Scotland.

Statement of cash flows

The company is exempt from including a Statement of Cash Flows in its Accounts as it was a wholly owned subsidiary of Scottish Power plc, which has included a consolidated Statement of Cash Flows in its consolidated Accounts.

Turnover

Turnover represents the invoiced value of goods and services provided, excluding value added tax.

Research and development

Expenditure on research and development is charged to the profit and loss account as it is incurred.

Tangible fixed assets

Tangible fixed assets are stated at cost and are depreciated on the straight-line method over their estimated operational lives. The main depreciation periods used by the company are set out below:

	Years
Buildings	10 – 60
Operational structures	15 – 80
Fixed plant	10 – 40
Vehicles, computers and mobile plant	3 – 10

Freehold land and infrastructure assets, being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls comprise a network of systems. Expenditure on infrastructure assets relating to increases in capacity or enhancement of the network and on maintaining the operating capability of the network in accordance with defined standards of service is treated as an addition to fixed assets.

The depreciation charge for infrastructure assets is the estimated level of annualised expenditure required to maintain the operating capability of the network and is based on the asset management plan determined by the water industry regulator as part of the price regulation process. The asset management plan is developed from historical experience combined with a rolling programme of reviews of the condition of the infrastructure assets.

Grants and contributions

Capital grants and customer contributions in respect of additions to non-infrastructure fixed assets are treated as deferred income and released to the profit and loss account over the estimated operational lives of the related assets. Grants and contributions receivable relating to infrastructure assets have been deducted from the costs of those assets. While this treatment is in accordance with the Statement of Standard Accounting Practice (SSAP) 4, it is not in accordance with the Companies Act 1985. The Act requires capital grants and contributions to be shown as deferred income rather than offset against the cost of tangible fixed assets. This departure from the requirements of the Act is, in the opinion of the directors, necessary for the Accounts to give a true and fair view as, while provision is made for depreciation of infrastructure assets, these assets do not have determinable finite lives and therefore no basis exists on which to recognise grants and contributions as deferred income. The effect of this treatment on tangible fixed assets is disclosed in note 9.

Leased assets

Fixed assets leased to the company under finance leases are capitalised and depreciated in line with the company's depreciation policy. The interest element of

finance lease repayments is charged to the profit and loss account in proportion to the balance of the capital repayments outstanding.

Rentals payable under operating leases are charged to the profit and loss account as incurred.

Stocks

Stocks are valued at the lower of cost and net realisable value.

Taxation

The charge for ordinary taxation is based on the profits for the year and takes into account full provision for deferred taxation, using the approach set out in Financial Reporting Standard 19 "Deferred tax", in respect of timing differences on a non-discounted basis. Such timing differences arise primarily from the differing treatment for taxation and accounting purposes of provisions and the depreciation of fixed assets.

Pensions

Southern Water plc operates pension schemes which cover the majority of the employees of Southern Water Services Limited. A valuation of the defined benefits pension schemes is normally conducted by an independent actuary every three years. The regular cost of providing pensions and related benefits and any variations from regular cost arising from the actuarial valuations are charged to the profit and loss account over the expected remaining service lives of current employees following consultations with the actuary. Any difference between the charge to the profit and loss account and the actual contributions paid to the pension schemes is included as an asset or liability in the balance sheet. Payments to defined contribution schemes are charged against profit as incurred.

2 Classification of turnover and revenue costs

Turnover represents the income receivable for providing water supply and wastewater services and is generated wholly in the United Kingdom.

Cost of sales reflects the direct costs of providing water supply and wastewater services. Administrative expenses comprise the indirect costs of the business. Other operating income refers to rents receivable and the profit on disposal of fixed assets.

3 Operating profit

	2002 £m	2001 £m
Operating profit is stated after charging/(crediting):		
Depreciation on		
– owned assets	75.1	68.7
– leased assets	0.4	0.4
	75.5	69.1
Rentals under other operating leases	5.3	5.5
Research and development expenditure	2.0	2.2
Release of grants and contributions	(1.6)	(1.5)
Profit on disposal of fixed assets	(1.6)	(1.6)
	2002	2001
	£000	£000
Auditors' remuneration for statutory audit	100	93
Auditors' remuneration for non-audit services to the company	53	61

4 Exceptional item

	2002 £m	2001 £m
Restructuring of debt	9.6	–

Net exceptional costs of £9.6m were incurred comprising legal and professional fees arising from the proposed refinancing of Southern Water.

5 Employee information

(a) Employee costs (including directors' emoluments):	2002 £m	2001 £m
Wages and salaries	49.4	49.4
Social security costs	3.6	3.9
Pension costs	4.7	4.5
Total employee costs	57.7	57.8
Less: charged as capital expenditure	(13.9)	(14.0)
Charged to the profit and loss account	43.8	43.8
	2002	2001
	No.	No.
(b) Average number of persons employed	2,033	2,062

6 Net interest and similar charges

	2002 £m	2001 £m
Interest payable on bank loans and overdraft	(2.2)	(2.7)
Interest payable on other loans	(69.9)	(63.7)
Total interest payable	(72.1)	(66.4)
Interest receivable	0.2	0.1
Net interest charge	(71.9)	(66.3)

Interest of £69.9 million (2001: £63.7 million) was payable to Group companies.

7 Tax on profit on ordinary activities

	2002 £m	2001 £m
Current tax		
UK corporation tax at 30% (2001: 30%)	20.2	23.1
Adjustment in respect of prior years	(2.3)	(2.0)
	17.9	21.1
Deferred tax		
Origination and reversal of timing differences	20.4	24.1
Adjustment in respect of prior years	–	(18.5)
Total deferred tax	20.4	5.6
Total tax on profit on ordinary activities	38.3	26.7

The rate of current tax charge on profit on ordinary activities varied from the standard rate of corporation tax due to the following factors:

	2002 £	2001 £
Current tax		
UK corporation tax rate at 30% on profit for the year	39.4	46.0
Adjustment in respect of prior years	(2.3)	(20.5)
Permanent differences	1.2	1.2
Tax charge on ordinary activities	38.3	26.7
Effect of deferred tax	(20.4)	(5.6)
Current tax charge for year	17.9	21.1

8 Dividends per ordinary share

	2002 £ per ordinary share	2001 £ per ordinary share	2002 £m	2001 £m
Interim dividend	–	284.28	–	15.9
Proposed final dividend	–	568.56	–	31.9
	–	852.84	–	47.8

9 Fixed assets and capital commitments

	Freehold land and buildings £m	Plant and machinery £m	Vehicles and equipment £m	Infrastructure assets £m	Other £m	Total £m
(a) Tangible assets						
Cost:						
At 1 April 2001	794.3	791.1	0.7	1,155.6	262.3	3,004.0
Additions and transfers	62.6	84.6	–	75.4	26.3	248.9
Grants and contributions	–	–	–	(9.2)	–	(9.2)
Disposals	(0.6)	(0.9)	–	(0.8)	(0.1)	(2.4)
At 31 March 2002	856.3	874.8	0.7	1,221.0	288.5	3,241.3
Depreciation:						
At 1 April 2001	153.7	171.8	0.7	209.1	128.1	663.4
Charge for the year	15.8	27.2	–	21.0	11.5	75.5
Disposals	(0.7)	(0.9)	–	(0.7)	(0.1)	(2.4)
At 31 March 2002	168.8	198.1	0.7	229.4	139.5	736.5
Net book value:						
At 31 March 2002	687.5	676.7	–	991.6	149.0	2,504.8
At 31 March 2001	640.6	619.3	–	946.5	134.2	2,340.6

Of the additions to infrastructure assets, the amount spent on infrastructure renewals during the year was £32.9 million and of the grants and contributions set against infrastructure assets, £6.5 million relates to infrastructure renewals.

Tangible fixed assets include £497.2 million (2001: £646.1 million) of assets in the course of construction which are not depreciated until commissioning.

The net book value of tangible fixed assets held under finance leases at 31 March 2002 was £5.0 million (2001: £5.4 million). The charge for depreciation against these assets during the year was £0.4 million (2001: £0.4 million).

The net book value of infrastructure assets is stated after deducting grants and contributions since privatisation of £115.1 million (2001: £105.9 million).

(b) Capital commitments

	2002 £m	2001 £m
In respect of contracts placed	179.2	73.5

10 Fixed asset investments

Southern Water Services Limited holds the entire issued share capital of Southern Water Services Finance plc, a company incorporated in the UK on 13 March 1998. The principal activity of the company is to raise debt finance. The investment is stated at cost of £50,000 (2001: £12,500).

Southern Water Services Limited has guaranteed the £100 million Variable Coupon Guaranteed Bonds issued by Southern Water Services Finance plc.

11 Stocks

	2002 £m	2001 £m
Raw materials	1.1	1.5
Work in progress	3.0	2.1
	4.1	3.6

12 Debtors: amounts falling due within one year

	2002 £m	2001 £m
Trade debtors	60.8	55.1
Unbilled income	32.5	28.9
Amounts owed by group undertakings	14.2	0.4
Prepayments	0.1	1.4
Other debtors	4.2	7.2
	111.8	93.0

13 Creditors: amounts falling due within one year

	2002 £m	2001 £m
Bank overdraft	54.5	46.8
Loans from parent company	666.0	341.8
Trade creditors	20.2	16.3
Capital creditors and capital accruals	89.0	105.8
Amounts owed to group undertakings	54.4	85.7
Corporation tax	7.4	22.1
Other taxation and social security	1.2	1.2
Other accruals and deferred revenue	46.8	47.4
Dividends	–	47.8
	939.5	714.9

14 Creditors: amounts falling due after more than one year

	2002 £m	2001 £m
Loans and other borrowings:		
Loans from parent company	382.5	538.3
Loans from subsidiary undertaking	99.6	99.6
	482.1	637.9
Repayments fall due as follows:		
Between one to two years	285.5	424.5
Between two and five years	51.8	53.4
After five years not by instalments	129.7	129.7
After five years by instalments	15.1	30.3
	482.1	637.9

The rates of interest payable on loans from the parent company due after five years range from 6.35% to 11.1%. The rate of interest on the loans from subsidiary undertakings is 6.9%.

15 Provision for liabilities and charges

(a) Other provisions

At 31 March 2001 and 31 March 2002

Total
£m

3.1

The above provision relates to environmental obligations.

15 Provision for liabilities and charges *continued*

(b) Deferred tax

Deferred tax provided in the accounts is as follows:

	2002 £m	2001 £m
Accelerated capital allowances	355.6	339.0
Other timing differences	(3.5)	(7.3)
Total	352.1	331.7

Movement in deferred tax provision

	2002 £m	2001 £m
Deferred tax provided at 1 April	331.7	326.1
Deferred tax charge in Profit and Loss Account	20.4	5.6
Deferred tax provided at 31 March	352.1	331.7

16 Grants and contributions

	£m
At 1 April 2001	36.1
Receivable in year	2.9
Released to profit and loss account	(1.6)
At 31 March 2002	37.4

Grants and contributions relate to non-infrastructure assets.

17 Share capital

	2002 £m	2001 £m
Authorised 46,050,000 ordinary shares of £1 each	46.1	46.1
Allotted, called up and fully paid 56,000 ordinary shares of £1 each	0.1	0.1

18 Reconciliation of movement in shareholders' funds

	Called up share capital £m	Share premium £m	Profit and loss account £m	Total £m
At 1 April 2000	0.1	46.3	588.2	634.6
Profit retained	–	–	78.9	78.9
At 31 March 2001	0.1	46.3	667.1	713.5
At 1 April 2001	0.1	46.3	667.1	713.5
Profit retained	–	–	93.0	93.0
At 31 March 2002	0.1	46.3	760.1	806.5

19 Pensions

The company's pension arrangements are administered through two schemes operated by Southern Water plc, the immediate holding company. The principal defined benefit scheme, which covers the majority of the company's employees, has eight Trustee Directors. The power of appointment of new Trustee Directors is vested in Southern Water plc. The assets of the schemes are held separately from those of the company. State Street Bank and Trust Company acts as custodian trustee for the defined benefit schemes and asset management is delegated to external fund managers.

19 Pensions *continued*

Members of the schemes receive an annual statement of their accrued benefits and a copy of the trustees' annual report. The Accounts of all schemes are audited annually by PricewaterhouseCoopers.

The defined benefit schemes are valued by independent consulting actuaries using the "projected unit" method. The last completed actuarial valuation of the principal scheme was carried out as at 31 March 2001. At that date, the market value of the scheme's assets was £296 million, and the actuarial value of these assets represented approximately 107% of the benefits accrued to members, after allowing for expected increases in earnings. The employer's average contribution is 14.9% of pensionable pay with members paying standard contributions of 6%, 5% or 3%.

The principal assumptions used in all actuarial valuations are those related to the differentials between the rates of return on investments and the rates of increases in earnings and pensions. In the main scheme, it has been assumed that the investment return per annum will be 2% higher than wage and salary increases and 4% higher than pension increases.

On 31 December 1998, the Southern Water pension schemes were closed to new entrants, who have the option of joining one of the ScottishPower schemes.

20 Contingent liabilities

	2002 £m	2001 £m
Contractors' claims	15.7	12.3

The company is party to mutual cross-guarantees for any monies owed by Southern Water plc group companies to National Westminster Bank plc.

21 Financial commitments

	2002 £m	2001 £m
Annual commitments under operating leases:		
Expiring within one year	0.9	0.5
Expiring between two and five years	1.9	1.5
Expiring after five years	0.1	0.2
	2.9	2.2

22 Directors' emoluments

	2002 £000	2001 £000
Aggregate emoluments (including benefits in kind)	611	744
Retirement benefits are accruing to five directors under a Southern Water defined benefit scheme.		
Aggregate highest paid director's emoluments and benefits (excluding gains made on exercise of share options)	147	209
Defined benefit scheme: Accrued annual pension at 31 March	71	34

23 Related party transactions

At 31 March 2002 Scottish Power plc had ultimate control over the company. The company has taken an exemption, as allowed by Financial Reporting Standard 8, not to disclose related party transactions with other group companies as the parent company publishes full statutory consolidated Accounts.

24 Ultimate holding company

The company is a wholly owned subsidiary of Southern Water plc, which at 31 March 2002 was itself wholly owned by Scottish Power plc.

Copies of Scottish Power plc's consolidated Accounts may be obtained from the Company Secretary at 1 Atlantic Quay, Glasgow G2 8SP.

25 Post balance sheet event

On 23 April 2002 the parent company, Southern Water plc, was acquired by First Aqua Limited.

Independent Auditor's Report

for the year ended 31 March 2002

Independent auditor's report to the members of Southern Water Services Limited.

We have audited the Accounts on pages 4 to 12 which have been prepared under the historical cost convention and the accounting policies set out on page 6.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the directors' report and Accounts in accordance with applicable United Kingdom law and accounting standards are set out in the statement of directors' responsibilities on page 2.

Our responsibility is to audit the Accounts in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board.

We report to you our opinion as to whether the Accounts give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' report is not consistent with the Accounts, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the report of the directors and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Accounts.

Basis of audit opinion

We conducted our audit in accordance with auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the 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 Accounts are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the Accounts.

Opinion

In our opinion, the Accounts give a true and fair view of the state of the company's affairs at 31 March 2002 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.



PricewaterhouseCoopers

Chartered Accountants and
Registered Auditors
London

28 June 2002

Supplementary Historical Cost Accounts – Profit and Loss Account

for the year ended 31 March 2002

	Appointed Business £m	2002 Non- Appointed Business £m	Total £m	Appointed Business £m	2001 Non- Appointed Business £m	Total £m
Turnover	423.9	6.0	429.9	416.1	5.5	421.6
Operating costs (excluding exceptional item)	(215.8)	(3.5)	(219.3)	(192.6)	(11.4)	(204.0)
Exceptional item	(9.6)	–	(9.6)	–	–	–
Operating income	1.6	–	1.6	1.6	–	1.6
Operating profit	200.1	2.5	202.6	225.1	(5.9)	219.2
Other income	0.6	–	0.6	0.5	–	0.5
Net interest	(71.9)	–	(71.9)	(66.3)	–	(66.3)
Profit on ordinary activities before taxation	128.8	2.5	131.3	159.3	(5.9)	153.4
Taxation	(38.3)	–	(38.3)	(26.7)	–	(26.7)
Profit on ordinary activities after taxation	90.5	2.5	93.0	132.6	(5.9)	126.7
Dividends	–	–	–	(47.8)	–	(47.8)
Retained profit/(loss)	90.5	2.5	93.0	84.8	(5.9)	78.9

No separate calculation or allocation of UK corporation tax or net interest charge has been performed for the non-appointed business.

Supplementary Historical Cost Accounts – Balance Sheet

as at 31 March 2002

	Appointed Business £m	2002 Non- Appointed Business £m	Total £m	Appointed Business £m	2001 Non- Appointed Business £m	Total £m
Fixed assets						
Tangible assets*	2,476.3	1.3	2,477.6	2,317.4	1.4	2,318.8
Investments	–	–	–	–	–	–
Current assets						
Stocks	3.9	0.2	4.1	3.4	0.2	3.6
Debtors*	138.4	0.6	139.0	113.3	1.5	114.8
	142.3	0.8	143.1	116.7	1.7	118.4
Creditors: amounts falling due within one year:						
Short-term borrowings	(720.5)	–	(720.5)	(388.6)	–	(388.6)
Dividends payable	–	–	–	(47.8)	–	(47.8)
Other creditors	(188.2)	(5.5)	(193.7)	(243.0)	(9.0)	(252.0)
	(908.7)	(5.5)	(914.2)	(679.4)	(9.0)	(688.4)
Net current liabilities	(766.4)	(4.7)	(771.1)	(562.7)	(7.3)	(570.0)
Total assets less current liabilities	1,709.9	(3.4)	1,706.5	1,754.7	(5.9)	1,748.8
Creditors: amounts falling due after one year:						
Borrowing	(482.1)	–	(482.1)	(637.9)	–	(637.9)
Other creditors	(37.4)	–	(37.4)	(36.1)	–	(36.1)
Total creditors	(519.5)	–	(519.5)	(674.0)	–	(674.0)
Deferred tax	(352.1)	–	(352.1)	(331.7)	–	(331.7)
Provisions for liabilities and charges	(3.1)	–	(3.1)	(3.1)	–	(3.1)
Deferred income	(25.3)	–	(25.3)	(26.5)	–	(26.5)
Net assets	809.9	(3.4)	806.5	719.4	(5.9)	713.5
Capital and reserves						
Called up share capital	0.1	–	0.1	0.1	–	0.1
Share premium account	46.3	–	46.3	46.3	–	46.3
Profit and loss account	763.5	(3.4)	760.1	673.0	(5.9)	667.1
Total equity shareholders' funds	809.9	(3.4)	806.5	719.4	(5.9)	713.5

* In the preparation of its statutory Accounts, the company has followed common industry practice and adopted the infrastructure renewals accounting basis set out in FRS 15. Note 1 to the statutory Accounts sets out this basis of infrastructure renewals accounting.

However, for the purposes of the regulatory Accounts, OFWAT have requested that this FRS 15 basis is not applied, thereby providing a basis consistent with prior years. A reconciliation to the balance sheet shown in the statutory Accounts and the balance sheet shown above, is set out below:

	2002 £m	2001 £m
Fixed assets – Net book value		
Per statutory Accounts	2,504.8	2,340.6
Infrastructure renewals prepayments if FRS 15 is not applied	(27.2)	(21.8)
Per regulatory Accounts	2,477.6	2,318.8
Debtors		
Per statutory Accounts	111.8	93.0
Infrastructure renewals prepayments if FRS 15 is not applied	27.2	21.8
Per regulatory Accounts	139.0	114.8

Accounting Policies

The Appointed Business of Southern Water Services Limited – Current Cost Accounts

These supplementary current cost Accounts have been prepared in accordance with guidance issued by the Director General of Water Services for modified real terms Accounts 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 effective commencement of the new regulatory regime.

These Accounts have been prepared in accordance with Regulatory Accounting Guidelines (RAGs) 1 to 4. In respect of cost allocations the company has continued to allocate costs as in previous years on the basis suggested in RAG 4 (Analysis of Operating Costs and Assets). The accounting policies used are the same as those adopted in the statutory historical cost Accounts, except as set out below.

Periodic review

The Strategic Business Plan produced by the company for the Periodic Review re-assessed asset stock and valuations. The valuations used in the current cost statements have been based on data from the 1999 Strategic Business Plan.

Real financial capital maintenance adjustments

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

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

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

Disposal of fixed assets adjustment – the difference between the values of realised assets in these current cost Accounts and in the historical cost Accounts.

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.

Infrastructure renewals accounting

For the purposes of the Regulatory Accounts, infrastructure renewals accounting has been continued and the relevant sections of FRS 15 have been dis-applied. A reconciliation between the statutory and Regulatory Accounts has been provided below the Historical Cost Balance Sheet for the appointed business.

Valuation bases for determining depreciation and disposal adjustments

i) Tangible fixed assets

Assets acquired prior to 31 March 1993 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 amount.

Land and buildings: Non-specialised operational properties have been valued using existing current cost values at 31 March 1993 as an estimate of open market value for existing use at that date, as the directors believe that there is no material difference between these values. These values have been adjusted for inflation using RPI since that date.

Specialised operational properties are valued at the lower of depreciated replacement cost and recoverable amount, restated annually between Periodic Reviews by adjusting for inflation using the RPI. The unamortised portion of third party contributions received is deducted in arriving at net operating assets (as described below).

Infrastructure assets: Mains, sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls are valued at replacement cost, determined principally on the basis of data provided by the Asset Management Plan (AMP).

A process of continuing refinement of asset records is expected to produce adjustments to existing values when Periodic Reviews of the AMP take place. In intervening years, values are restated for inflation using the RPI.

Other operational fixed assets: All other operational fixed assets are valued periodically at depreciated replacement cost. Between Periodic Reviews, values are restated for inflation using the RPI.

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

ii) Grants and other third party contributions

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

Current Cost Profit and Loss Account for the Appointed Business

for the year ended 31 March 2002

	Notes	2002 £m	2001 £m
Turnover	1	423.9	416.1
Current cost operating costs	2, 3	(300.7)	(269.2)
Operating income	1	1.6	1.6
Working capital adjustment	1	2.0	2.8
Current cost operating profit		126.8	151.3
Other income		0.6	0.5
Net interest		(71.9)	(66.3)
Financing adjustment		18.2	30.1
Current cost profit before taxation		73.7	115.6
Taxation			
- Current tax		(20.4)	(21.1)
- Deferred tax		(17.9)	(5.6)
Current cost profit attributable to shareholders		35.4	88.9
Dividends		-	(47.8)
Current cost retained profit		35.4	41.1

Current Cost Balance Sheet for the Appointed Business

as at 31 March 2002

	Notes	2002 £m	2001 £m
Tangible fixed assets	4, 5, 6	12,472.8	12,227.6
Third party contributions since 1989-90		(138.7)	(133.1)
		12,334.1	12,094.5
Working capital	7	(73.9)	(157.3)
Net operating assets		12,260.2	11,937.2
Non-trade debtors		4.2	6.0
Non-trade creditors due within one year		(720.5)	(388.6)
Creditors due after one year		(482.1)	(637.9)
Deferred tax		(352.1)	(331.7)
Provisions for liabilities and charges		(3.1)	(3.1)
Dividends payable		-	(47.8)
Net assets employed		10,706.6	10,534.1
Capital and reserves			
Called up share capital		0.1	0.1
Share premium		46.3	46.3
Profit and loss account		(49.7)	(85.1)
Current cost reserve	8	10,709.9	10,572.8
Total capital employed		10,706.6	10,534.1

Current Cost Cash Flow Statement

for the year ended 31 March 2002

	Notes	Appointed Business £m	2002 Non- Appointed Business £m	Total £m	Appointed Business £m	2001 Non- Appointed Business £m	Total £m
Net cash inflow from operating activities	9	199.4	–	199.4	335.1	1.7	336.8
Returns on investments and servicing of finance							
Interest received		0.2	–	0.2	13.8	–	13.8
Interest paid		(42.9)	–	(42.9)	(80.8)	–	(80.8)
Net cash outflow from returns on investments and servicing of finance		(42.7)	–	(42.7)	(67.0)	–	(67.0)
Taxation							
UK corporation tax paid		(32.7)	–	(32.7)	(50.9)	–	(50.9)
Net cash outflow from taxation		(32.7)	–	(32.7)	(50.9)	–	(50.9)
Capital expenditure and financial investment							
Gross purchase of fixed assets		(239.6)	–	(239.6)	(272.5)	–	(272.5)
Receipts of grants and contributions		12.1	–	12.1	11.2	–	11.2
Infrastructure renewals expenditure		(26.4)	–	(26.4)	(22.0)	–	(22.0)
Disposal of fixed assets		1.6	–	1.6	1.6	–	1.6
Net cash outflow from capital expenditure and financial investment		(252.3)	–	(252.3)	(281.7)	–	(281.7)
Equity dividends paid		(47.8)	–	(47.8)	(45.8)	(1.7)	(47.5)
Net cash outflow before financing	10	(176.1)	–	(176.1)	(110.3)	–	(110.3)
Financing							
New loans		182.8	–	182.8	125.3	–	125.3
Repayment of loans		(14.4)	–	(14.4)	(11.8)	–	(11.8)
Net cash inflow from financing		168.4	–	168.4	113.5	–	113.5
(Decrease)/increase in cash		(7.7)	–	(7.7)	3.2	–	3.2

Notes to the Current Cost Accounts

for the year ended 31 March 2002

1 Analysis of turnover and operating income for the appointed business

	Water Supply £m	2002 Sewerage Services £m	Total £m	Water Supply £m	2001 Sewerage Services £m	Total £m
Turnover						
Measured	39.3	82.0	121.3	39.5	78.7	118.2
Unmeasured	67.5	209.9	277.4	68.7	205.8	274.5
Trade effluent	–	6.7	6.7	–	7.0	7.0
Large user revenues	4.5	3.2	7.7	4.7	–	4.7
Other sources (excluding third parties)	0.6	5.6	6.2	0.9	5.9	6.8
Third party services	4.6	–	4.6	4.9	–	4.9
Total turnover	116.5	307.4	423.9	118.7	297.4	416.1
Current cost profit on disposal of fixed assets	0.8	0.8	1.6	0.7	0.9	1.6
Working capital adjustment	0.5	1.5	2.0	0.8	2.0	2.8

2 Reconciliation of Historical to Current Cost operating costs

	2002 £m	2002 £m	2001 £m	2001 £m
Historical cost operating costs (including exceptional item)		225.4		192.6
Current cost depreciation	129.8		124.7	
Historical cost depreciation	(54.5)		(48.1)	
		75.3		76.6
Current cost operating costs		300.7		269.2

Notes to the Current Cost Accounts
for the year ended 31 March 2002

3 Analysis of current cost operating costs by activity

	Service analysis								Business services		
	Water supply			Sewerage					Customer services £m	Scientific services £m	Cost of regulation £m
	Resources and treatment £m	Distribution £m	Water supply sub total £m	Sewerage £m	Sewage treatment £m	Sludge treatment and disposal £m	Sewage treatment and disposal £m	Sewerage service sub total £m			
2002											
Direct costs											
Employment costs	1.0	3.2	4.2	2.6	3.9	3.1	7.0	9.6			
Power	3.0	2.0	5.0	3.1	5.7	1.3	7.0	10.1			
Hired & contracted services	0.3	3.1	3.4	1.6	1.2	1.4	2.6	4.2			
Materials & consumables	0.1	1.4	1.5	0.4	0.7	0.3	1.0	1.4			
Service charges, EA	3.7	–	3.7	0.6	2.1	–	2.1	2.7			
Other direct costs	1.0	0.4	1.4	0.2	0.5	10.2	10.7	10.9			
Total direct costs	9.1	10.1	19.2	8.5	14.1	16.3	30.4	38.9	11.6	2.6	1.3
General & support expenditure	6.4	7.9	14.3	5.9	10.8	7.7	18.5	24.4	4.4	1.2	0.5
Functional expenditure	15.5	18.0	33.5	14.4	24.9	24.0	48.9	63.3	16.0	3.8	1.8
Total Business Activities			9.1					12.5	(16.0)	(3.8)	(1.8)
Rates			6.5					7.7			
Doubtful debts			1.7					4.5			
Exceptional items			3.3					6.3			
Total opex less third party services			54.1					94.3			
Third party services – opex			3.1					–			
Total operating expenditure			57.2					94.3			
Capital costs											
Infrastructure renewal expenditure	0.1	14.3	14.4	12.0	–	–	–	12.0			
Movement in infrastructure renewal prepayment	–	(5.8)	(5.8)	0.4	–	–	–	0.4			
Current cost depreciation (allocated)	26.6	4.5	31.1	29.6	42.6	26.5	69.1	98.7			
Amortisation of deferred credits			(0.3)					(1.3)			
Capital maintenance excluding third party services			39.4					109.8			
Third party services – capital maintenance			–					–			
Total capital maintenance			39.4					109.8			
Total operating costs			96.6					204.1			
Reactive and Planned Maintenance (Inc. in Opex)											
Infrastructure	–	7.7	7.7	4.8	–	–	–	4.8			
Non-Infrastructure	0.3	1.0	1.3	3.7	3.6	3.5	7.1	10.8			
CCA (MEA) values											
Service activities	520.9	2,548.7	3,069.6	7,727.0	1,022.0	635.2	1,657.2	9,384.2			
Business activities			–					–			
Service totals	520.9	2,548.7	3,069.6	7,727.0	1,022.0	635.2	1,657.2	9,384.2			
Services for third parties			19.0					–			
Total CCA (MEA) values			3,088.6					9,384.2			

3 Analysis of current cost operating costs by activity continued

	Service analysis								Business services		
	Water supply			Sewerage					Customer services £m	Scientific services £m	Cost of regulation £m
	Resources and treatment £m	Distribution £m	Water supply sub total £m	Sewerage £m	Sewage treatment £m	Sludge treatment and disposal £m	Sewage treatment and disposal £m	Sewerage service sub total £m			
2001											
Direct costs											
Employment costs	1.0	2.5	3.5	3.6	3.9	2.2	6.1	9.7			
Power	3.9	0.8	4.7	3.1	4.1	1.4	5.5	8.6			
Hired & contracted services	0.3	3.0	3.3	2.3	1.3	0.9	2.2	4.5			
Materials & consumables	0.1	1.5	1.6	0.5	0.7	0.3	1.0	1.5			
Service charges, EA	3.6	–	3.6	0.6	2.1	–	2.1	2.7			
Other direct costs	1.1	0.4	1.5	0.3	0.5	9.6	10.1	10.4			
Total direct costs	10.0	8.2	18.2	10.4	12.6	14.4	27.0	37.4	11.4	2.8	1.3
General & support expenditure	5.7	5.7	11.4	5.7	6.7	5.3	12.0	17.7	1.7	0.6	0.2
Functional expenditure	15.7	13.9	29.6	16.1	19.3	19.7	39.0	55.1	13.1	3.4	1.5
Total Business Activities			7.8					10.2	(13.1)	(3.4)	(1.5)
Rates			6.3					6.9			
Doubtful debts			1.7					4.4			
Exceptional items			–					–			
Total opex less third party services			45.4					76.6			
Third party services – opex			3.3					–			
Total operating expenditure			48.7					76.6			
Capital costs											
Infrastructure renewal expenditure	0.8	12.1	12.9	9.1	–	–	–	9.1			
Movement in infrastructure renewal prepayment	–	(4.4)	(4.4)	3.1	–	–	–	3.1			
Current cost depreciation (allocated)	25.2	4.4	29.6	29.2	40.6	25.3	65.9	95.1			
Amortisation of deferred credits			(0.3)					(1.2)			
Capital maintenance excluding third party services			37.8					106.1			
Third party services – capital maintenance			–					–			
Total capital maintenance			37.8					106.1			
Total operating costs			86.5					182.7			
Reactive and Planned Maintenance (Inc. in Opex)											
Infrastructure	–	7.2	7.2	5.5	–	–	–	5.5			
Non-Infrastructure	0.6	0.6	1.2	2.9	3.4	3.5	6.9	9.8			
CCA (MEA) values											
Service activities	514.9	2,507.1	3,022.0	7,636.8	955.9	594.1	1,550.0	9,186.8			
Business activities			–					–			
Service totals	514.9	2,507.1	3,022.0	7,636.8	955.9	594.1	1,550.0	9,186.8			
Services for third parties			18.8					–			
Total CCA (MEA) values			3,040.8					9,186.8			

4 Current cost analysis of fixed assets by asset type – Water Supply

	Specialised operational assets £m	Non- specialised operational assets £m	Infra- structure assets £m	Other tangible assets £m	Total £m
Gross replacement cost					
Balance at 1 April 2001	823.0	16.6	2,528.1	86.5	3,454.2
RPI adjustment	10.7	0.2	32.9	1.1	44.9
Disposals	(0.2)	–	–	–	(0.2)
Additions	19.7	0.2	9.1	10.4	39.4
Balance at 31 March 2002	853.2	17.0	2,570.1	98.0	3,538.3
Accumulated depreciation					
Balance at 1 April 2001	354.2	4.1	–	55.1	413.4
RPI adjustment	4.6	0.1	–	0.7	5.4
Disposals	(0.2)	–	–	–	(0.2)
Charge for year	22.1	0.3	–	8.7	31.1
Balance at 31 March 2002	380.7	4.5	–	64.5	449.7
Net book value at 31 March 2002	472.5	12.5	2,570.1	33.5	3,088.6
Net book value at 31 March 2001	468.8	12.5	2,528.1	31.4	3,040.8

5 Current cost analysis of fixed assets by service – Sewerage Services

	Specialised operational assets £m	Non- specialised operational assets £m	Infra- structure assets £m	Other tangible assets £m	Total £m
Gross replacement cost					
Balance at 1 April 2001	2,489.5	66.2	7,555.4	131.5	10,242.6
RPI adjustment	32.4	0.9	98.2	1.7	133.2
Disposals	(2.2)	–	(0.1)	–	(2.3)
Additions	130.5	0.9	33.4	11.8	176.6
Balance at 31 March 2002	2,650.2	68.0	7,686.9	145.0	10,550.1
Accumulated depreciation					
Balance at 1 April 2001	943.1	16.5	(0.4)	96.6	1,055.8
RPI adjustment	12.3	0.2	–	1.2	13.7
Disposals	(2.2)	–	(0.1)	–	(2.3)
Charge for year	82.6	1.2	–	14.9	98.7
Balance at 31 March 2002	1,035.8	17.9	(0.5)	112.7	1,165.9
Net book value at 31 March 2002	1,614.4	50.1	7,687.4	32.3	9,384.2
Net book value at 31 March 2001	1,546.4	49.7	7,555.8	34.9	9,186.8

6 Current cost analysis of fixed assets by asset type – Total

	Specialised operational assets £m	Non- specialised operational assets £m	Infra- structure assets £m	Other tangible assets £m	Total £m
Gross replacement cost					
Balance at 1 April 2001	3,312.5	82.8	10,083.5	218.0	13,696.8
RPI adjustment	43.1	1.1	131.1	2.8	178.1
Disposals	(2.4)	–	(0.1)	–	(2.5)
Additions	150.2	1.1	42.5	22.2	216.0
Balance at 31 March 2002	3,503.4	85.0	10,257.0	243.0	14,088.4
Accumulated depreciation					
Balance at 1 April 2001	1,297.3	20.6	(0.4)	151.7	1,469.2
RPI adjustment	16.9	0.3	–	1.9	19.1
Disposals	(2.4)	–	(0.1)	–	(2.5)
Charge for year	104.7	1.5	–	23.6	129.8
Balance at 31 March 2002	1,416.5	22.4	(0.5)	177.2	1,615.6
Net book value at 31 March 2002	2,086.9	62.6	10,257.5	65.8	12,472.8
Net book value at 31 March 2001	2,015.2	62.2	10,083.9	66.3	12,227.6

7 Working capital

	2002 £m	2001 £m
Stocks	3.9	3.4
Trade debtors	92.8	84.1
Trade creditors	(15.0)	(16.3)
Short-term capital creditors and accruals	(89.0)	(106.1)
Infrastructure renewals prepayment	28.6	23.3
Other trade accruals	(65.4)	(82.3)
Receipts in advance	(25.3)	(25.9)
Corporation tax	(7.3)	(22.1)
Payroll related tax and social security	(1.2)	(1.3)
Group trade debtors/(creditors)	3.9	(15.5)
Prepayments	0.1	1.4
	(73.9)	(157.3)

8 Movement on Current Cost Reserve

	2002 £m	2001 £m
Balance at 1 April	10,572.8	10,336.9
RPI Adjustments		
Fixed assets	159.0	271.7
Grants and third party contributions	(1.7)	(2.9)
Working capital	(2.0)	(2.8)
Financing	(18.2)	(30.1)
Balance at 31 March	10,709.9	10,572.8

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

	2002 £m	2001 £m
Current cost operating profit	126.8	151.3
Working capital adjustment	(2.0)	(2.8)
Increase in stocks	(0.5)	(1.6)
Receipt from other income	0.6	0.5
Current cost depreciation	129.8	124.7
Current cost profit on sale of assets	(1.6)	(1.6)
(Increase)/decrease in debtors and prepaid expenses	(19.8)	3.2
(Decrease)/increase in creditors and accrued expenses	(53.2)	42.1
Infrastructure renewals expenditure	26.4	22.0
Decrease of provisions	(5.4)	(1.2)
Amortisation of grants and contributions	(1.6)	(1.5)
Effect of other deferrals and accruals	(0.1)	–
Net cash flow from operating activities	199.4	335.1

10 Analysis of net debt

	At 31 March 2001 £m	Cash flows £m	Other changes £m	At 31 March 2002 £m
Overdrafts	(46.8)	(7.7)	–	(54.5)
Loans due after one year	(637.9)	(50.0)	205.8	(482.1)
Loans due within one year	(341.8)	(118.4)	(205.8)	(666.0)
Total	(1,026.5)	(176.1)	–	(1,202.6)

Five Year Rolling Summary

Current cost profit and loss account for appointed business

	2002 £m	2001 £m	2000 £m	1999 £m	1998 £m
Turnover	423.9	422.4	486.1	460.5	449.7
Current cost operating costs (including exceptional item)	(300.7)	(273.2)	(293.6)	(300.3)	(298.9)
Operating income	1.6	1.5	4.2	3.7	3.1
Working capital adjustment	2.0	2.8	4.3	4.6	4.1
Current cost operating profit	126.8	153.5	201.0	168.5	158.0
Other income	0.6	0.6	0.6	0.6	1.1
Net interest	(71.9)	(67.3)	(60.0)	(54.6)	(43.9)
Financing adjustment	18.2	30.6	21.7	13.3	19.6
Current cost profit before taxation	73.7	117.4	163.3	127.8	134.8
Taxation	(38.3)	(27.2)	(61.4)	(33.9)	(120.0)
Current cost profit attributable to shareholders	35.4	90.2	101.9	93.9	14.8
Dividends	–	(48.5)	(47.9)	(46.5)	(46.0)
Current cost profit/(loss) retained	35.4	41.7	54.0	47.4	(31.2)

Current cost balance sheet for appointed business

	2002 £m	2001 £m	2000 £m	1999 £m	1998 £m
Tangible fixed assets	12,472.8	12,390.9	12,240.8	13,972.0	13,768.8
Third party contributions since 1989-90	(138.7)	(134.9)	(130.6)	(125.5)	(118.6)
Working capital	(73.9)	(159.4)	(126.0)	(166.8)	(224.6)
Net operating assets	12,260.2	12,096.6	11,984.2	13,679.7	13,425.6
Non-trade debtors	4.2	6.1	3.7	40.6	151.4
Non-trade creditors due within one year	(720.5)	(393.8)	(757.0)	(282.8)	(31.9)
Creditors due after one year	(482.1)	(646.5)	(551.6)	(557.2)	(45.6)
Deferred tax	(352.1)	(336.1)	–	–	–
Provisions for liabilities and charges	(3.1)	(3.1)	(3.2)	(3.4)	(3.6)
Dividends payable	–	(48.4)	(47.5)	(46.6)	(719.0)
Net assets employed	10,706.6	10,674.8	10,628.6	12,830.3	12,776.9
Capital and reserves					
Called up share capital	0.1	0.1	0.1	0.1	0.1
Share premium	46.3	46.9	48.0	49.2	50.2
Profit and loss account	(49.7)	(86.2)	(130.8)	138.5	92.9
Current cost reserve	10,709.9	10,714.0	10,711.3	12,642.5	12,633.7
Total capital and reserves	10,706.6	10,674.8	10,628.6	12,830.3	12,776.9

The prior year figures above have been adjusted for subsequent inflation using the indexation procedures prescribed by the DG in RD 13/02. Accordingly the 2001 figures are different from the comparatives on pages 17 to 25 which have not been indexed.

Report of the Auditors to the Director General of Water Services

for the year ended 31 March 2002

We have audited the Accounts on pages 4 to 12 and the supplementary regulatory information on pages 14 to 26.

Respective responsibilities of directors and auditors

As described on pages 1 and 2 the company's directors are responsible for the preparation of Accounts and the supplementary regulatory information. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit for statutory Accounts purposes includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the 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 Accounts are free from material misstatement, whether caused by fraud or other irregularity or error.

In forming our opinion we also evaluated the overall adequacy of the presentation of information in the Accounts in terms of Generally Accepted Accounting Principles and Regulatory Accounting Guidelines as appropriate. With regard to the latter, the historical cost regulatory balance sheet on page 15 has been drawn up in accordance with Ofwat's instruction of 20 April 2001 that infrastructure renewals accounting as applied in previous years should be continued and the relevant sections of Financial Reporting Standards 12 and 15 dis-applied. The effect of this instruction and a reconciliation of the statutory to regulatory historic cost balance sheet is given on page 15.

Opinion

In our opinion the Accounts for the year to 31 March 2002 contain the information required to be published and submitted to you by Southern Water Services Limited to comply with Condition F of the Instrument of Appointment by the Secretary of State for the Environment of the company as a water (and sewerage) undertaker under the Water Industry Act 1991.

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 of the Instrument and the Regulatory Accounting Guidelines 1-4 issued by the Office of Water Services;
- (c) The Accounts on pages 4 to 12 give, under the historical cost convention, a true and fair view of the revenues, costs, assets and liabilities of the Appointee and its appointed business; and
- (d) The current cost financial information on pages 16 to 26 has been properly prepared in accordance with the Regulatory Accounting Guideline 1.02, Accounting for current costs, issued in May 1992 by the Office of Water Services.



PricewaterhouseCoopers

Chartered Accountants and Registered Auditors
London

28 June 2002

Additional Accounting Information

Services supplied to the appointee by associated companies

Company/Division	Turnover of associated company/division £m	Nature of transaction	Terms of supply	Value 2002 £000	Value 2001 £000
Scottish Power plc (Energy Supply)	1,700.5	Meter services	Other market testing	1,196	1,285
		Group charges	No market	5,800	5,900
Scottish Power plc (Other businesses)	67.2	Contracting	Other market testing	–	279
		ISD	Other market testing	1,063	4,749
Thus	257.8	Telecommunications	Other market testing	5,856	7,568
Scottish Power plc (Power Systems)	646.6	Vehicles leasing	Other market testing	1,583	1,676

Allocation of costs between regulated and non-regulated businesses

Each non-appointed activity is treated separately within the company's financial records. Examples of non-appointed activities include non-monopoly rechargeable works, sales from stores, recreation and amenity services etc. Revenues, costs, assets and liabilities are generally directly allocated to particular business activities. Administrative overheads have been apportioned from the appointed business to the non-appointed business on an activity cost basis.

Details of inter-company loans

Loans from Scottish Power plc by instalments (EIB)	£99.2 million
Loans from Scottish Power plc not by instalments (EIB)	£30.0 million
Loans from Scottish Power plc not by instalments	£460.2 million
Loans from Southern Water plc not by instalments	£459.1 million
Loans from Southern Water Services Finance plc not by instalments	£99.6 million

Dividends paid and comment on policy underlying the payment

In accordance with the terms of the sale of Southern Water to First Aqua Limited by ScottishPower no dividend is proposed to be paid for 2001/02.

Details of any guarantees or security provided

The company is party to mutual cross-guarantees for any monies owed by Southern Water plc group companies to National Westminster Bank plc.

Asset transfers

There were no asset transfers during the year.

Rental income from associated companies

Rental income received from the associated companies during the year:

	£000
Thus	73
ScottishPower Metering	11

Additional Commentary on Trends and Comparisons

Five year trend

In real terms current cost operating profit fell by £31.2 million over five years mainly reflecting the decrease in turnover relating to the Final Determination P-nought adjustment. Major cost efficiencies continue to be made in the implementation of the Way Ahead Plan through the use of new technology and new business processes. These efficiencies have offset cost increases due to inflation, additional operating costs arising from capital, new obligations and increased depreciation on schemes commissioned during the year.

Movements from prior year

Turnover

	£m
Turnover 2000/01	416.1
Price limits and inflation	13.0
Other	(5.2)
Turnover 2001/02	423.9

Operating costs (net of capital maintenance)

	£m
Operating costs 2000/01	125.3
Exceptional cost	9.6
Restructuring accrual release	7.1
Other cost increases, net of efficiencies	9.5
Operating costs 2001/02	151.5

Southern Water
Southern House
Yeoman Road
Worthing
West Sussex
BN13 3NX

www.southernwater.co.uk

Registered number 2366670

