

Notes to the company financial statements

1 Accounting policies

a) Basis of accounting

The financial statements have been prepared under the historical cost convention as modified by the revaluation of financial assets and liabilities (including derivative instruments) at fair value through profit or loss and in accordance with applicable United Kingdom Accounting Standards and comply with the requirements of the United Kingdom Companies Act 2006 (the Act).

b) Tangible fixed assets and depreciation

Tangible fixed assets are included at cost less accumulated depreciation. Freehold land is not depreciated. Other assets are depreciated on a straight line basis over their estimated economic lives, which are principally as follows:

	Years
Buildings	30 – 60
Vehicles, computers and software	2 – 15

c) Leased assets

Where assets are financed by leasing arrangements which transfer substantially all the risks and rewards of ownership of an asset to the lessee (finance leases), the assets are accounted for as if they had been purchased and the fair values of minimum lease payments are shown as an obligation to the lessor. Lease payments are treated as consisting of a capital element and a finance charge, the capital element reducing the obligation to the lessor and the finance charge being written off to the profit and loss account over the period of the lease in proportion to the capital amount outstanding. Depreciation is charged over the shorter of the estimated useful life and the lease period. All other leases are accounted for as operating leases. Rental costs arising under operating leases are charged to the profit and loss account on a straight line basis over the life of the lease.

d) Impairment of fixed assets and investments

Impairments of fixed assets and investments are calculated as the difference between the carrying values of net assets of income generating units, including where appropriate investments and goodwill, and their recoverable amounts. Recoverable amount is defined as the higher of net realisable value or estimated value in use at the date the impairment review is undertaken. Net realisable value represents the net amount that can be generated through sale of assets. Value in use represents the present value of expected future cash flows discounted on a pre-tax basis, using the estimated cost of capital of the income generating unit. Impairment reviews are carried out if there is some indication that an impairment may have occurred, or, where otherwise required, to ensure that goodwill and fixed assets are not carried above their estimated recoverable amounts. Impairments are recognised in the profit and loss account and, where material, are disclosed as exceptional.

e) Financial instruments

The company has taken advantage of the exemption in FRS29: "Financial Instruments: Disclosures" not to provide the detailed disclosures of financial instruments set out in that standard since these are provided on a consolidated basis in the group financial statements.

i) Debt instruments

All loans and borrowings are initially recognised at cost, being the net fair value of the consideration received. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest rate method. Where a loan or borrowing is in a fair value hedging relationship it is remeasured for changes in fair value of the hedged risk at the balance sheet date with gains or losses being recognised in the profit and loss account (see below).

Gains and losses are recognised in the profit and loss account when the liabilities are derecognised or impaired, as well as through the amortisation process.

ii) Derivative financial instruments and hedging activities

The company uses derivative financial instruments such as cross currency swaps, forward currency contracts and interest rate swaps to hedge its risks associated with foreign currency and interest rate fluctuations. Such derivative instruments are initially recorded at cost and subsequently remeasured at fair value for the reported balance sheet. The fair value of cross currency swaps, interest rate swaps and forward currency contracts is calculated by reference to market exchange rates and interest rates at the period end.

In relation to fair value hedges which meet the conditions for hedge accounting, the gain or loss on the hedging instrument is taken to the profit and loss account where the effective portion of the hedge will offset the gain or loss on the hedged item (see above).

In relation to cash flow hedges which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in reserves, and the ineffective portion in the profit and loss account. The gains or losses deferred in reserves in this way are recycled through the profit and loss account in the same period in which the hedged underlying transaction or firm commitment is recognised in the profit and loss account.

For derivatives that do not qualify for hedge accounting, gains or losses are taken directly to the profit and loss account in the period.

Hedge accounting is discontinued when the hedging instrument expires, is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that date any cumulative gain or loss on the hedging instrument recognised in reserves is kept in reserves until the forecast transaction occurs, or transferred to the profit and loss account if the forecast transaction is no longer expected to occur.

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contract or the host contract is not carried at fair value with gains and losses reported in the profit and loss account.

1 Accounting policies (continued)

f) Investments

Investments in subsidiary undertakings are held at historical cost.

After initial recognition at cost (being the fair value of the consideration paid), investments which are classified as held for trading or available for sale are measured at fair value, with gains or losses recognised in income or equity respectively. When an available for sale investment is disposed of, or impaired, the gain or loss previously recognised in reserves is taken to the profit and loss account.

Other investments are classified as held to maturity when the company has the positive intention and ability to hold to maturity. Investments held for an undefined period are excluded from this classification. Such investments (and those held to maturity) are subsequently measured at amortised cost using the effective interest rate method, with any gains or losses being recognised in the profit and loss account.

g) Share based payments

The company operates a number of equity settled, share based compensation plans for employees. The fair value of the employee services received in exchange for the grant is recognised as an expense over the vesting period of the grant.

The fair value of employee services is determined by reference to the fair value of the awards granted calculated using a pricing model, excluding the impact of any non-market conditions. The number of awards expected to vest takes into

account non-market vesting conditions including, where appropriate, continuing employment by the group. The charge is adjusted to reflect shares that do not vest as a result of failing to meet a non-market based condition.

h) Cash flow statement

The company has taken advantage of the exemption under Financial Reporting Statement 1 'Cash flow statements' and not produced a cash flow statement.

i) Deferred taxation

Deferred taxation is fully provided for in respect of timing differences between the treatment of certain items for taxation and accounting purposes only to the extent that the group has an obligation to pay more tax in the future or a right to pay less tax in the future. Deferred tax assets are only recognised to the extent that taxable profits are expected to arise in the future. Material deferred taxation balances arising are discounted by applying an appropriate risk free discount rate.

j) Pensions

The company participates in the group's defined benefit and defined contribution pension schemes, details of which are set out in note 28 to the group financial statements. However, the company is currently unable to identify its share of assets and liabilities relating to the defined benefit schemes. The pension costs charged against the operating profit are the contributions payable to the scheme in respect of the accounting period in respect of the defined benefit and defined contribution schemes.

2 Tangible fixed assets

	Land and buildings £m	Plant and equipment £m	Total £m
Cost			
At 1 April 2009	0.7	0.5	1.2
Additions	–	0.1	0.1
At 31 March 2010	0.7	0.6	1.3
Depreciation			
At 1 April 2009	(0.7)	–	(0.7)
Charge for year	–	(0.2)	(0.2)
At 31 March 2010	(0.7)	(0.2)	(0.9)
Net book value			
At 31 March 2010	–	0.4	0.4
At 31 March 2009	–	0.5	0.5

3 Investments

	Subsidiary undertakings		
	Shares £m	Loans £m	Total £m
At 1 April 2009	3,225.2	165.5	3,390.7
Additions/loans advanced	62.9	155.7	218.6
At 31 March 2010	3,288.1	321.2	3,609.3

Details of the principal subsidiaries of the company are given in note 40 of the group financial statements.

Notes to the company financial statements (continued)

4 Debtors

	2010 £m	2009 £m
Amounts owed by group undertakings	3.5	31.6
Deferred tax	10.1	11.8
Corporation tax recoverable	38.3	15.4
Other debtors	0.1	–
Prepayments and accrued income	4.3	–
	56.3	58.8

5 Creditors: amounts falling due within one year

	2010 £m	2009 £m
Bank overdrafts	91.4	24.7
Other loans	10.6	65.3
Borrowings (note 7)	102.0	90.0
Derivative financial instruments	2.0	–
Trade creditors	0.2	–
Amounts due to group undertakings	635.5	936.5
Other creditors	5.6	6.0
Taxation and social security	–	–
Accrued expenses	0.8	8.8
	746.1	1,041.3

6 Creditors: amounts falling due after more than one year

	2010 £m	2009 £m
Borrowings – other loans (note 7)	77.8	86.9
Amounts due to group undertakings	350.2	10.4
Derivative financial instruments	38.6	45.8
	466.6	143.1

7 Borrowings

Borrowings analysed by maturity date

	2010 £m	2009 £m
Borrowings due within one year	102.0	90.0
Borrowings due after one year:		
Between one and two years	–	10.6
Between two and five years	55.8	21.5
After more than five years	22.0	54.8
Total borrowings due after one year	77.8	86.9
	179.8	176.9

7 Borrowings (continued)

Financial liabilities analysed by interest rate after taking into account of interest rate swaps entered into by the company

2010	Non-interest bearing liabilities £m	Floating interest rate £m	Fixed interest rate £m	Total
Bank loans and overdrafts	–	91.4	–	91.4
Other loans	–	88.4	–	88.4
Other financial liabilities	0.2	–	–	0.2
	0.2	179.8	–	180.0
Impact of interest rate swaps not matched against specific debt instruments	–	(300.0)	300.0	–
	0.2	120.2	300.0	180.0
Weighted average interest rate		6.3%		
Weighted average period for which interest is fixed (years)		4.2		

2009	Non-interest bearing liabilities £m	Floating interest rate £m	Fixed interest rate £m	Total
Bank loans and overdrafts	–	24.7	–	24.7
Other loans	–	152.2	–	152.2
Finance leases	–	–	–	–
Other financial liabilities	–	–	–	–
	–	176.9	–	176.9
Impact of interest rate swaps not matched against specific debt instruments	–	(300.0)	300.0	–
	–	(123.1)	300.0	176.9
Weighted average interest rate		6.4%		
Weighted average period for which interest is fixed		5.2		

The company's borrowings are denominated in sterling, after taking into account cross currency swaps the company has entered into. There is no difference between the book value and the fair value of the company's borrowings.

The fair values are based on expected future cash flows discounted using zero coupon forward interest rates related to the expected timing of payments.

At the balance sheet dates the company had committed undrawn borrowing facilities of £41.7 million (2009: nil) expiring between one and two years and £458.3 million (2009: £500 million) expiring between two and five years (2009: two and five years).

Notes to the company financial statements (continued)

8 Share capital

	2010 £m	2009 £m
Total authorised share capital: 434,139,785 ordinary shares of 97 ¹⁷ / ₁₉ p (2009: 346,783,834 ordinary shares of 97 ¹⁷ / ₁₉ p)	425.0	339.5
Total issued and fully paid share capital: 236,585,205 ordinary shares of 97 ¹⁷ / ₁₉ p (2009: 235,938,946 ordinary shares of 97 ¹⁷ / ₁₉ p)	231.6	231.0

Changes in share capital were as follows:

	Number	£m
Ordinary shares of 97¹⁷/₁₉p	235,938,946	231.0
At 1 April 2009		
Shares issued at 536p, 548p, 592p, 759p, 823p, 862p, 1172p or 1221p under the group's Employee Sharesave Scheme	614,269	0.6
Shares issued at 720p and 738p under the group's Share Option Scheme	3,548	–
At 31 March 2010	236,556,763	231.6

9 Share premium

	2010 £m	2009 £m
At 1 April	71.9	64.3
Share premium arising on issue of shares for Employee Share Option Scheme	4.0	7.6
At 31 March	75.9	71.9

10 Other reserves

	Capital redemption reserve £m	Hedging reserve £m	Total other reserves £m
At 1 April 2008	156.1	(12.1)	144.0
Transfers to the profit and loss account on cash flow hedges	–	2.3	2.3
At 1 April 2009	156.1	(9.8)	146.3
Transfers to the profit and loss account on cash flow hedges	–	2.3	2.3
At 31 March 2010	156.1	(7.5)	148.6

The capital redemption reserve arose on the repurchase of B shares. This is not distributable.

11 Reconciliation of shareholders' equity

	Share capital £m	Share premium £m	Other reserves £m	Retained earnings £m	Equity attributable to the equity holders of Severn Trent Plc £m
At 1 April 2008	229.7	64.3	144.0	2,314.9	2,752.9
Cash flow hedges					
– Transfers to net profit	–	–	2.3	–	2.3
Share options and LTIPs					
– proceeds from shares issued	1.3	7.6	–	–	8.9
– value of employees' services	–	–	–	0.1	0.1
– awards granted by subsidiaries	–	–	–	5.2	5.2
– tax and social security paid on awards vesting	–	–	–	(0.2)	(0.2)
Net profit for the year	–	–	–	113.3	113.3
Dividends	–	–	–	(158.8)	(158.8)
At 1 April 2009	231.0	71.9	146.3	2,274.5	2,723.7
Cash flow hedges					
– Transfers to net profit	–	–	2.3	–	2.3
Share options and LTIPs					
– proceeds from shares issued	0.6	4.0	–	–	4.6
– awards granted by subsidiaries	–	–	–	5.2	5.2
Net profit for the year	–	–	–	140.0	140.0
Dividends	–	–	–	(159.7)	(159.7)
At 31 March 2010	231.6	75.9	148.6	2,260.0	2,716.1

In previous years £1,221.2 million of the company's retained profit arose as a result of group restructuring exercises, and is not considered likely to be distributable. As permitted by Section 408 of the Companies Act 2006, no profit or loss account is presented for the company.

12 Employee costs and auditors' remuneration

	2010 £m	2009 £m
Wages and salaries	1.2	1.4
Social security costs	0.1	0.1
Pension costs	0.8	2.8
Total employee costs	2.1	4.3

For details of directors' remuneration see the Directors' remuneration report on pages 54 to 57.

Auditors' fees in respect of the company were £76,000 (2009: £77,000). For full details of the fees paid to the auditors by the group, see note 7 to the group financial statements.

Fees payable to Deloitte LLP and their associates for non-audit services to the company are not required to be disclosed because the consolidated financial statements are required to disclose such fees on a consolidated basis.

13 Employee numbers

Average number of employees of the company (including executive directors) during the year was 11 (2009: 10). All were based in the United Kingdom.

14 Employee share schemes

For details of employee share schemes and options granted over the shares of the company, see note 33 of the consolidated financial statements. Details of LTIP conditional awards and share options granted by the company to its employees are set out below.

The company has charged £nil (2009: £0.1 million) to the profit and loss account in respect of share based payments.

Notes to the company financial statements (continued)

14 Employee share schemes (continued)

At 31 March the number of options that were exercisable under each of the share based remuneration schemes was as follows:

	2010		2009	
	Number of exercisable options/awards	Weighted average exercise price	Number of exercisable options/awards	Weighted average exercise price
Long Term Incentive Plan	–	–	–	–
Employee Sharesave Scheme	161	1,172p	1,237	598p
	161		1,237	

i) Long Term Incentive Plan (LTIP)

Changes in the number of awards outstanding during the year:

	Number of awards
Outstanding at 1 April 2008	423,554
Granted during the year	3,566
Vested during the year	(50,770)
Lapsed during the year	(64,590)
Transferred to other group companies	(231,620)
Outstanding at 1 April 2009	80,140
Granted during the year	4,813
Vested during the year	–
Lapsed during the year	(76,574)
Transferred to other group companies	–
Outstanding at 31 March 2010	8,379

Awards outstanding at 31 March were:

Date of grant	Normal date of vesting	Number of shares	
		2010	2009
July 2006	2009	–	76,574
July 2007	2010	–	–
July 2008	2011	3,566	3,566
July 2009	2012	4,813	–
		8,379	80,140

ii) Employee Sharesave Scheme

Changes in the number of options outstanding during the year:

	Number of share options	Weighted average exercise price
Outstanding at 31 March 2008	3,083	780p
Cancelled during the year	(461)	1,172p
Exercised during the year	(1,146)	809p
Forfeited during the year	(239)	823p
Outstanding at 31 March 2009	1,237	598p
Cancelled during the year	449	806p
Exercised during the year	(1,237)	598p
Transferred from other companies	4,107	874p
Outstanding at 31 March 2010	4,556	867p

14 Employee share schemes (continued)

Options outstanding at 31 March were:

Date of grant	Normal date of vesting	Option price	Number of shares	
			2010	2009
January 2002	2009	548p	–	1,010
January 2006	2009, 2011 or 2013	823p	–	227
January 2007	2010, 2012 or 2014	1,172p	161	–
January 2009	2012 or 2014	862p	3,946	–
January 2010	2013 or 2015	808p	449	–
			4,556	1,237

15 Pensions

The company operates two defined benefit schemes (being the Severn Trent Pension Scheme and the Severn Trent Water Mirror Image Pension Scheme). In addition, the group operates an unfunded arrangement for certain employees whose earnings are above the pension cap.

Further details regarding the operation of these schemes are given in note 28 of the group financial statements.

The company is currently unable to identify its share of the underlying assets and liabilities from the group's defined benefit schemes, and hence it continues to account for the cost of contributions as if the scheme was a defined contribution scheme.

The pension charge for the year was £0.8 million (2009: £2.9 million).

16 Related party transactions

The company has taken advantage of the exemption under FRS 8 and not disclosed details of transactions with other undertakings within the Severn Trent group of companies.

17 Contingent liabilities

a) Bonds and guarantees

The company has entered into bonds and guarantees in the normal course of business. No liabilities are expected to arise in respect of either the bonds or guarantees.

b) Bank offset arrangements

The banking arrangements of the company operate on a pooled basis with certain of its subsidiary undertakings. Under these arrangements participating companies guarantee each others' overdrawn balances to the extent of their credit balances, which can be offset against balances of participating companies.

18 Post balance sheet events

On 27 May 2010 the board of directors proposed a final dividend of 45.61 pence per share.

19 Dividends

For details of the dividends paid in 2009/10 and 2008/09 see note 14 in the group financial statements.