Company Registration No. 2366949

UNITED UTILITIES ELECTRICITY PLC

Annual Report and Consolidated Financial Statements

31 March 2007

ANNUAL REPORT AND FINANCIAL STATEMENTS 2007

MANAGING DIRECTOR'S STATEMENT

Performance

The board is pleased to report another good set of financial results Revenue increased by 11 8 per cent to £315 6 million, reflecting allowed price increases of 2 6 per cent and adjustments to tariffs resulting from underecoveries of allowed revenue in previous years Operating profit before the impact of restructuring credit of £0 6 million increased to £175 5 million, up 18 9 per cent on last year, primarily reflecting the increase in revenue

United Utilities Electricity PLC continued to focus on maintaining the integrity, security and safety of its electricity distribution network and outputs are in line with its five year delivery plan During the year the business replaced or refurbished 293 kilometres of overhead lines and replaced 91 kilometres of underground cables It also replaced or refurbished 579 switchgear units and replaced 280 transformers

Electricity supplies were available for 99 99 per cent of the time during the financial year ended 31 March 2007, sustaining the business's high level of performance in managing the network to maintain constant supplies for consumers Under the regulatory interruptions incentive scheme, United Utilities Electricity PLC ('UUE') has been set network performance targets for the number and duration of customer supply interruptions The average number of interruptions per 100 consumers per annum was 53 89*, out-performing the regulatory target for the year of 57 1 The average number of minutes for which consumers were without supply was 56 68*, beating the regulatory target for the year of 58 1 minutes (Figures denoted by * have not yet been audited by Ofgem at the date of this report)

Stakeholders

We are committed to listening and responding to the needs of our different stakeholders employees, customers, investors, regulators and our commercial partners Understanding their requirements and then managing and reporting our performance is central to how we run our business The cornerstone of this approach is our employees and I would like to thank them for their continuing commitment and hard work

The board places great importance on the quality, accuracy and reliability of information on both financial and non-financial matters that we provide to our regulators Such information is subject to rigorous internal checks, review and sign off before it is submitted

Strategy

United Utilities Electricity PLC maintains its strategic focus on enhancing the value of the business by increasing investment, improving efficiency and quality of service and we are well placed to build on our current successes We are on track to deliver better performance for all our stakeholders during the period to 2010

The future

We have updated our operating model to formally separate asset ownership from asset operations and maintenance This has been done through the creation of a new operating subsidiary, United Utilities Electricity Services Ltd, which has operated since 1 April 2007 with clearly defined cost targets and performance incentives The aim is to increase our focus on performance management and support the sharing of best practice and knowledge across the business

The formal legal split between asset ownership and asset operations will enhance the performance and value of UUE in a number of ways The creation of an ownership team, distinct from the service provider, enables a specific, senior management focus on the commercial, regulatory and financial strategy of UUE and connects this with the strategy for the long-term development of the asset base The operational management team of the service provider is able to focus on cost control, performance, customer service, and delivery Furthermore, the contractual discipline and reporting regimes that have been put in place to separate the two businesses have increased the awareness of, and incentives to improve, performance, customer service, and cost efficiency United Utilities PLC announced on 5 June 2007 its decision to initiate a sale process for United Utilities Electricity PLC's distribution assets

Eóin Cooke
Managing Director

OPERATING AND FINANCIAL REVIEW

NATURE OF THE BUSINESS

Business overview

United Utilities Electricity PLC ('the Company') is a public limited company registered in England and Wales The principal activity of the Company and of United Utilities Electricity PLC Group ('the Group') is the operation of electricity distribution assets

United Utilities Electricity PLC is a subsidiary of United Utilities PLC The activities of United Utilities Electricity PLC are controlled through the United Utilities North West division This division also controls the water and wastewater assets owned by United Utilities Water PLC in north west England Besides the operation of electricity distribution assets, United Utilities PLC ('the UU Group') is one of the largest operators of water and wastewater systems in the UK The UU Group also operates a gas network and provides multi-utility metering and connections services

Business description

The electricity industry in the UK consists of four distinct components generation, transmission, distribution and supply (see figure 1 – UK electricity market components) The majority of electricity distribution services are provided by regional distribution companies, each with its own service area These are broadly based on the former electricity board areas (see figure 2 – UK electricity distribution companies in England, Scotland and Wales) The electricity market is regulated by the Gas and Electricity Markets Authority (the Authority), which governs and acts through the Office of Gas and Electricity Markets ('Ofgem') In the electricity market, suppliers contract with generators (for wholesale power) and with transmission and distribution network businesses (for delivery services), in order that they can provide energy to final consumers

OPERATING AND FINANCIAL REVIEW

Electricity distribution

The Group owns the distribution network which carries electricity from the National Grid along power lines to consumers' premises on behalf of the electricity supply companies who are United Utilities Electricity PLC's main customers Annual revenue is driven, in part, by the volume of electricity distributed The income derived from the distribution business therefore depends in part on changes in the demand for electricity by consumers in north west England, and also from generators who have been connected to United Utilities Electricity PLC's network under contracts agreed since 1 April 2005 Demand for electricity is affected by such factors as growth and movements in population, social trends, economic and business growth or decline, changes in the mix of energy sources used by consumers, weather conditions and energy efficiency measures The electricity distribution business is a regulated business in which the average revenue from charges, which a company may collect in any year, is capped by the electricity regulator (as described in more detail below) Accordingly, profit derived from the distribution business of United Utilities Electricity PLC also depends upon efficiency, achieved by reducing and controlling costs, and providing high standards of service

Key non- financial performance measures for the business relate to quality of supply Electricity supplies were available for 99 99 per cent of the time during the financial year ended 31 March 2007, sustaining the business's high level of performance in managing the network to maintain constant supplies for consumers Under the regulatory Interruptions Incentive Scheme, United Utilities Electricity PLC has been set network performance targets for the number and duration of customer supply interruptions Although we have still outperformed regulatory targets, performance in the past year has been adversely affected by a few high impact events on the grid and primary distribution systems, including third party damage to 33,000 volt cables The average number of interruptions per 100 consumers per annum was 53 89*, out-performing the regulatory target for the year of 57 1 The average number of minutes for which consumers were without supply was 56 68*, just out-performing the regulatory target for the year of 58 1 minutes (Figures in this paragraph denoted by * are still to be audited by Ofgem at the date of this report)

Economic regulation

The electricity industry in Great Britain is regulated under the Electricity Act 1989 (the 'Electricity Act'), the Utilities Act 2000 (the 'Utilities Act') and the Energy Act 2004 (the 'Energy Act') The Electricity Act, as amended by the Utilities Act, requires all companies distributing electricity to be licensed unless they are covered by an exemption Economic regulation pursuant to these licences is the responsibility of Ofgem Ofgem also exercises powers under UK competition legislation, most significantly the Competition Act 1998 and the Enterprise Act 2002

The UK government awarded electricity distribution licences in 2001 The licences continue in force for an indefinite period, subject to potential termination rights as set out below United Utilities Electricity PLC holds an electricity distribution licence that authorises it to distribute electricity anywhere in Great Britain Under that licence, United Utilities distributes electricity across its distribution system covering an area in north west England comprising 2 4 million consumer premises Restrictions included within the electricity distribution licence include

- a non-discrimination obligation,
- restrictions on the payment of dividends The board of directors must provide a certificate of compliance before declaring dividends, affirming they are satisfied that the business is complying with relevant licence obligations including that it has sufficient resources and that the making of the distribution will not cause it to be in material breach of any of the obligations in the future,
- restrictions on dealing with associated companies The consent of Ofgem is required before lending any funds to an associated company and all transactions with associated companies must be on an arm's length basis, without cross subsidy,
- ring-fencing of financial and management resources of the licensed business, and
- restriction on the disposal of any asset forming part of the distribution system

Licence conditions can be modified by Ofgem either with the agreement of the licensee (or, in the case of standard conditions, with the agreement of the requisite proportion of licensees) or following reference to the Competition Commission for a decision on public interest grounds The licence can be terminated on 25 years' notice given by the Secretary of State

OPERATING AND FINANCIAL REVIEW

Ofgem regulates electricity distribution charges by capping the average charges that a company can impose in any year Ofgem conducts a periodic review and sets price caps every five years This price cap is set by reference to inflation as measured by the retail price index in the UK plus an adjustment factor known as 'X' which is specific to each company The size of a company's X factor (which can be positive, negative or zero) and the change at the start of a price control period to the opening revenue value (defined as P_0 change) reflect the scale of its capital investment programme, its cost of capital and its operational and environmental obligations, together with scope for it to improve its efficiency The last periodic review was completed at the end of 2004 and covers the period from 1 April 2005 to 31 March 2010 For the 2005-10 review period, United Utilities Electricity PLC was allowed a real (excluding inflation) P0 price increase of 8 2 per cent in 2005/06 followed by constant real prices thereafter (i e the X factor = zero) Ofgem published its first scoping letter and timetable for the 2010 price review on 17 May 2007

Price cap regulation as operated in the UK is performance based Companies are incentivised to be efficient, both in terms of their operating costs and in the implementation of their capital expenditure programme The benefit of any efficiency savings achieved through effective management is retained by the companies for a period of up to five years, after which time the benefit is passed to customers via the price setting process The cost of any under performance due to poor management is borne by the companies An incentive scheme was introduced by Ofgem in April 2002 which provided greater focus on three specific service areas number of interruptions to customers' supplies, length of those interruptions, and quality of the telephone response to customers Ofgem consulted on its approach to the incentive scheme as part of the price control review and again in 2006, including the form of the scheme, targets and associated costs It has been agreed that the distribution network operators' performance in those areas will continue to be incentivised until the end of the next price control period (31 March 2015) Under the scheme, United Utilities Electricity PLC is subject to annual rewards and penalties depending upon its performance against pre-specified targets Both rewards and penalties under the incentive scheme are capped at 3 0 per cent of annual revenues

Under the terms of their licences, electricity distribution network operators ('DNOs') must produce and implement charging methodologies for both connection to and use of their distribution systems The methodologies are required to set out the principles and methods by which charges will be calculated The methodologies must be approved by Ofgem.

Use of system agreements

Following a review by Ofgem, in 2006 the former bilateral agreements governing the commercial contractual arrangements relating to the connection to and use of distribution networks were replaced by a single multilateral contract, the Distribution Connection and Use of System Agreement ('DCUSA'), as Ofgem felt that it would improve transparency

Electricity metering services

In 2006/07 Ofgem consulted on licence modifications that are intended to clarify the obligations on DNOs with respect to electricity metering services after the price controls on the provision of new and replacement meters and meter operation services expire on 31 March 2007 The effect of the modifications is to make clear that from 1 April 2007, the regulatory price cap will be retained only for the rental of electricity meters installed prior to 31 March 2007 Other metering services will no longer form part of the definition of a distribution business and DNOs that wish to provide new or replacement meters or meter operation services must do so through a separate subsidiary As a result of this change, United Utilities Electricity PLC will cease to provide meter operation services from 30 June 2007 and the provision of new or replacement meters will be carried out by a fellow subsidiary of United Utilities PLC

Environmental regulation

Underground cabling

All electricity companies have a general duty under the Electricity Act to have regard to the desirability of environmental preservation and conservation and the protection of Sites of Special Scientific Interest when they formulate proposals for development United Utilities Electricity PLC may be required to carry out an environmental assessment when it intends to lay cables, construct overhead lines or carry out any other development in connection with its licensed activities In response to discussions with environmental organisations in United Utilities Electricity PLC's operating area, and with the backing of Ofgem, the company has embarked on a

OPERATING AND FINANCIAL REVIEW

programme of converting from overhead cables to underground cables in designated areas on aesthetic grounds There is an allowance of £5 million provided by Ofgem for such work over the period 2005-10 The first of these schemes was completed recently and five more are now in progress

High voltage cables
United Utilities Electricity PLC, in common with all other UK electricity companies, owns and operates pressure-assisted high voltage cables These operate at voltages of 33,000 and 132,000 volts These cables are either filled with nitrogen gas or a light 'oil' type fluid United Utilities operate both types, having 620 kilometres of the latter type of cable In the main the fluid is biodegradable, although some older cables are pressured with a variety of fluid that is not The potential for loss into the environment of the fluid, due to leaks or third party damage, is recognised nationally by all electricity companies and the Environment Agency ('EA') and is an issue concerning waste disposal and pollution law In order to mitigate the effects of any losses, United Utilities Electricity PLC is party to a national code of practice agreement with the EA Over the last six years, the company has worked to minimise losses into the environment and has reduced annual loss to around $25m^3$ in 2005/06 from a high of $74m^3$ in 2001/02 However 2006/07 has been a particularly disappointing year, with losses of $49m^3$ A significant contribution to this figure is damage caused to United Utilities Electricity PLC's 33,000 volts cables by third parties, although there is a contribution from some particularly poorly performing cables that have been replaced during 2006/07

Sulphur hexafluoride (SF6) management
SF6 is a gas with excellent electrical insulation and other properties, which has led to its widespread use in electrical switchgear However, there is concern over the SF6 that escapes into the atmosphere since it is a potent greenhouse gas, with a greenhouse warming potential of 22,200 times that of carbon dioxide The Kyoto Protocol to the Climate Change Convention has recognised the need to curb emissions of all greenhouse gases, including SF6

United Utilities Electricity PLC's strategy is accurately to record levels of leaks, to replace high leak rate sites and to review and develop future targets The company is working with the electricity industry and manufacturers to continue developing vacuum and solid insulation for switchgear, and so work towards eliminating the use of SF6 switchgear

The annual leakage of SF6, as recorded at 1 April 2006 and reported to the Environment Agency, equates to 254kg, or 2% of the total mass of SF6 controlled by UUNW of 12,984kg Management are not currently aware of any requirements or proposals that will result in the company being required to reduce leakage or otherwise increase costs, although we are monitoring the situation closely through the Energy Networks Association

Microgeneration
The Climate Change and Sustainable Energy Act was adopted in June 2006 with the primary aim of encouraging the production of energy through microgeneration and community energy schemes, improving energy efficiency and alleviating fuel poverty The act seeks to cut the emission of carbon dioxide in the UK and introduces new powers to modify the conditions of electricity distribution and supply licences to ensure that energy companies pay a fair price for electricity produced from microgeneration These are uncertain dependent on technology, market and regulatory issues A possible significant effect could be a reduction of units distributed in the long-term We are working to influence Ofgem through the price control mechanism so that this does not have a negative effect on the Company's revenue

Electric and magnetic fields
The possibility that electric and magnetic fields ('EMFs') may cause adverse health effects has been a topic of debate and research for many years Over the last 20 years, major research programmes throughout the world have explored whether EMFs have an adverse impact on health A large epidemiological study – the UK Childhood Cancer Study – reported in December 1999 that there was "no evidence that exposure to magnetic fields associated with the electricity supply in the UK increases risk for childhood leukaemia, cancers of the nervous system, or any childhood cancer" International bodies such as the World Health Organisation ('WHO') and the International Agency for Research on Cancer and, in the UK, the Health Protection Agency ('HPA') (which has subsumed the former National Radiological Protection Board) continue to investigate this issue and have concluded that there is no established causal link between EMFs and ill health

In March 2001, the HPA published a review of the state of the science and concluded "for the vast majority of children in the UK there is now considerable evidence that the EMF levels to which they are exposed do not increase the risk of leukaemia or other malignant disease" However, it also noted that the possibility remains that intense and

OPERATING AND FINANCIAL REVIEW

prolonged exposure to magnetic fields can increase the risk of leukaemia in children but the epidemiological evidence is currently not strong enough to justify a firm conclusion that such fields cause leukaemia in children

In the spirit of the precautionary approach, the HPA published in May 2003 a consultation document on how to limit exposure to EMFs and, in particular, on whether the UK should adopt the more stringent exposure guidelines of the International Commission for Non-Ionising Radiation Protection ('ICNIRP') In March 2004, the HPA recommended that the ICNIRP guidelines should be adopted A report published by the Childhood Cancer Research Group ('CCRG') in 2005 strengthened the evidence that childhood leukaemia rates are slightly higher near power lines, but leaves the question of what causes this more confused than before, stating that "There is no accepted biological mechanism to explain the epidemiological results, indeed, the relation may be due to chance "

The independent Advisory Group on Non-Ionising Radiation ('AGNIR'), which reports to the HPA, has issued several reports relating to EMFs, considering their possible link with an increased risk of cancer The most recent AGNIR report on EMFs published in February 2006 concluded that the evidence does not support the hypothesis that exposure to EMFs is associated with an increased risk of breast cancer and that, although it is inconclusive, it does not appear that EMFs affect the hormone melatonin (a reduction in which can lead to breast cancer) The report gave recommendations for further research to be carried out

In spite of the official view of bodies like the HPA and the WHO, there continues to be significant lobbying by pressure groups concerned about the alleged effects of public electricity infrastructure on health In 2005, a cross industry all stakeholder group on the issue was set up in the UK It is known as the Stakeholder Advisory Group on Extra Low Frequency EMFs ('SAGE') Although SAGE was initiated by National Grid plc, it has now been taken up by the Department of Health, and essentially will undertake a report to the Department of Health and the government on EMF issues in relation to health The industry is represented on SAGE by the National Grid and by the Energy Networks Association of which United Utilities Electricity PLC is a member The work of SAGE is not complete, although it is expected that a report will be delivered to the Department of Health during 2007/08 Currently the balance of advice in SAGE seems to support the status quo, although given the breadth of views necessarily aired in the process, other options which could drive significant costs for the industry (such as the maintenance of building-free corridors around power lines) have had their merits reviewed However it will be for government to decide on the appropriate response to stakeholder concerns, and United Utilities Electricity PLC does not currently expect any real shift from the status quo to emerge

United Utilities Electricity PLC, in line with other Energy Networks Association ('ENA') member companies, carries out its activities in accordance with HPA guidance The ENA is the trade association for electricity companies in the UK The ENA and its member companies are committed to responsible behaviour in the light of the scientific evidence, including considering any appropriate precautionary actions

RESOURCES

People

Industrial relations

Good industrial relations remain a priority for United Utilities Electricity PLC The Group continues to recognise and work in partnership with trade unions A statement of principles governs the approach to labour relations across the Group Around 99 per cent of employees within the Company are now represented by trade unions for collective bargaining purposes, a process which is underpinned by principles contained within a voluntary collective agreement entitled 'Together in Partnership' Following an independent and comprehensive review and re-evaluation of the agreement, a series of joint initiatives have been put in place to develop this collaborative approach to employee relations further

Health and safety

United Utilities Electricity PLC remains committed to maintaining high standards of health and safety in every area of its business and is in full alignment with the HSE 'Revitalising Health and Safety' strategy Key performance indicators are in place and progress is monitored regularly at all levels throughout the business As a utility business, the risk profile remains broad with both major construction projects and contractor management playing a key part There were 11 accidents in 2006/07 (representing a rate of 10 3 per 1,000 employees) which were reportable under the Reporting of Injuries, Diseases and Dangerous Occurrences Regulations, showing a reduction of over 5 7% to the previous year's rate of 10 9 per 1,000 employees In addition there were 10,361 working days lost, due to

OPERATING AND FINANCIAL REVIEW

accidents and ill health, a rate of 9,746 per 1,000 employees, showing a reduction of 1 2% on the previous rate of 9,868 days per 1,000 employees

Training and development

The Group encourages employees to work to their full potential and is committed to improving its employees' skills through training and development and nurturing a culture in which employees feel valued

Dignity and equality

The Group respects the dignity and rights of every employee and supports them in performing various roles in society The Group also challenges prejudice and stereotyping October 2006 saw the introduction of the new Employment Equality (Age) Regulations Employees across the Company were briefed, making them aware of their rights under this new legislation

An equal pay audit was conducted during the year and no major disparities in pay between male and female employees were found when comparing like for like roles

Employees with disabilities

The Group is committed to fulfilling its obligations in accordance with the Disability Discrimination Act 1995 and best practice As an equal opportunities employer, the Group gives equal consideration to applicants with disabilities in its employment criteria and will modify equipment and working practices wherever it is safe and practical to do so, both for new employees and for those employees that are disabled during the course of their employment Additionally, the Group is committed to providing full support and appropriate training for employees who become disabled during the course of their employment so that they can continue to work in a position appropriate to their experience and abilities

Operating facilities

As at 31 March 2007, the Group's facilities included 13,128 kilometres of overhead lines, 43,149 kilometres of underground cables (operating at 132 kilovolts, 33 kilovolts, 25 kilovolts, 11 kilovolts, 6 6 kilovolts and 400/230 volts), 18,248 ground mounted substations and 17,021 pole mounted transformers United Utilities Electricity PLC holds wayleaves which entitle it to run lines and cables through and across private land and in some circumstances these can be terminated by the landowner or occupier upon notice pursuant to the Electricity Act However, United Utilities Electricity PLC has statutory rights to seek the compulsory retention of a wayleave if termination is sought by the landowner/occupier United Utilities Electricity PLC does not anticipate that any significant relocation of these facilities will be required, although any relocation of a major portion of these facilities would have a material adverse effect on its business and financial position Ground mounted substations are situated on properties either owned by United Utilities Electricity PLC or held under lease Pole mounted transformers are generally held under wayleave agreements United Utilities Electricity PLC anticipates that it will be able to negotiate lease renewals on satisfactory terms or relocate equipment so that the non-renewal of any such leases would not have a material adverse effect upon United Utilities Electricity PLC

In addition to the assets described above, the Group occupies various non-operational properties consisting primarily of offices, depots, warehouses and workshops These are either owned by the Company or leased It is anticipated that the Group will be able to negotiate renewals of any expiring leases, or relocate the relevant facilities, without having a material adverse impact on the Group

PRINCIPAL RISKS AND UNCERTAINTIES

The board considers the following risks to be the principal ones that might affect the Group's performance and results but cautions that the risks listed in this section do not address all the factors that could cause results to differ materially There may be additional risks that the Group does not currently know of, or that are deemed immaterial based on either information currently available or the Group's current assessment of the risk The Group's business, financial condition or results of operations could be materially affected by any of these risks, resulting in a decline in

OPERATING AND FINANCIAL REVIEW

the trading price of United Utilities PLC's ordinary shares The Group operates an internal control system to evaluate and manage risks as described immediately below

Internal control

The board is responsible for the company's system of internal controls and for reviewing its effectiveness Each year management reviews all controls including financial, operational and compliance controls and risk management procedures The internal control system is designed to manage, rather than to eliminate, the risk of failure to achieve the company's business objectives and can only provide reasonable, and not absolute, assurance against material misstatement or loss

The key features of the internal control system are

- a control environment with clearly defined organisation structures operating within a framework of policies and procedures covering every aspect of the business,
- comprehensive business planning, risk assessment and financial reporting procedures, including the annual preparation of detailed operational budgets for the year ahead and projections for subsequent years,
- a bi-monthly board review of financial and non-financial performance to assess progress towards objectives,
- regular monitoring of risks and control systems throughout the year, supported by the use of risks and issues databases,
- a self-certification process, whereby management are required to confirm that the system of internal control is operating effectively,
- a UU Group internal audit function which provides independent scrutiny of internal control systems and risk management procedures,
- an annual risk assessment exercise involving self-assessment by management of all business risks in terms of impact, likelihood and control strength and an objective challenge of that assessment by the internal audit team,
- health and safety performance reviews carried out by our in-house safety professionals in addition to the normal health and safety risk assessment and management processes carried out within each of the operating businesses,
- centralised treasury operations operating within defined limits and subject to regular reporting requirements and internal audit reviews, and
- established procedures, set out in an internal control manual, for planning, approving and monitoring major capital expenditure, major projects which includes short and long-term project budgets, risk evaluation, detailed appraisal and review procedures, defined authority levels and post-investment performance reviews

Principle risks and uncertainties

The Group's revenue is substantially influenced by the regulator, which could adversely affect profitability

The revenue and profitability of the Group is substantially influenced by price controls established every five years by the regulator The price control review for the Group covering the five-year period commencing on 1 April 2005 was determined by the regulator in November 2004 The Group has accepted this determination and has not exercised its right to appeal adverse price determinations to the Competition Commission

An adverse price determination may occur as a result of a number of factors, including an inadequate allowed cost of capital or unrealistic regulatory assumptions concerning operating expenses, required capital expenditure and revenue forecasts Scope to re-open these price controls within the charging period is limited Specific re-opening provisions have been made, with effect from 1 April 2005, in relation to uncertain costs associated with specified provisions of the Electricity Safety, Quality and Continuity Regulations 2002 (or amending/replacement regulations), the New Roads and Street Works Act 1991 and the Traffic Management Act 2004

OPERATING AND FINANCIAL REVIEW

Failure to deliver the capital investment programmes could adversely affect profitability

The Group requires significant capital expenditure for additions to, or replacement of, plant and equipment for its facilities and networks The price controls set by Ofgem take into account the level of capital expenditure expected to be incurred during the relevant five-year price review period and the associated funding costs Historically, the Group has financed the expenditure from cashflows from operations and from debt financing There can be no assurance that cashflows from operations will not decline, or that additional debt financing or other sources of capital will be available to meet these requirements

Failure to deliver operational performance or cost savings implicit in the regulatory review could adversely affect profitability

Operating cost savings to be achieved during the current five-year regulatory period are implicit in the regulatory review To assist the achievement of these operating cost savings, a business change programme is underway If the operating cost savings are not achieved, or the business change programme is not delivered, then the Group's profitability would suffer Similarly, if operational performance were to deteriorate, this may be reflected in less favourable outcomes from future price control reviews and the Group's profitability would suffer

Environmental regulations could increase the Group's costs and adversely affect profitability

Various environmental protection and health and safety laws and regulations govern the electricity distribution business These laws and regulations establish, amongst other things, standards for quality of electricity supply, which affect the Group's operations In addition, the Group is required to obtain various environmental permissions from regulatory agencies for its operations The Group endeavours to comply with all regulatory standards Should the Group fail to comply, it would face fines imposed by the courts or otherwise face sanctions by the regulator

Service interruptions could adversely affect profitability

In addition to the capital investment programmes, the Group controls and operates the electricity distribution network and undertakes maintenance of the associated assets with the objective of providing a continuous service Historically, there have been interruptions to the supply of services, such as the incident in January 2005 affecting Cumbria and Lancashire, when a storm severely damaged the electricity network supply to 250,000 customers, but the majority of interruptions relate to minor issues that are rectified promptly.

During 2006/07, there were an unusually high number of interruptions in total, which led to a few long duration interruptions and a number of interruptions affecting a large number of customers However there were no instances of interruptions combining long duration and high numbers affected Nevertheless, the failure of a key asset could cause a more significant interruption to the supply of services (in terms of duration or number of customers affected), which may have an adverse effect on the Group's operating results or financial position

Pension scheme obligations may require the Group to make additional contributions to the schemes which would reduce profitability

The Group participates in a number of pension schemes The principal schemes are funded defined benefit schemes and the assets of the schemes are held in trust funds independent of Group finances

A one-off lump sum contribution of £8 6 million was made to UUPS and £71 0 million was made to ESPS on 31 March 2005 These contributions were calculated to equal the capitalised value of the Group's funding obligations to the schemes for the next five years (based on the actuarial valuation as at 31 March 2004) and paid in lieu of certain employer contributions which would have been made to the schemes during that period

The Group's proportion of the schemes was estimated to have a combined pre-tax surplus of £24 5 million as at 31 March 2007, compared to a pre-tax obligation of £1 8 million at 31 March 2006, as disclosed under IAS 19

It should be noted that the funding requirements of the schemes are set on the basis of a number of actuarial assumptions about the future and, to the extent that actual experience is less favourable than the assumptions made, additional contributions over and above those paid already/expected to be paid in the future may be required The profitability of the Group may therefore be affected

Currently expected further pension contributions and a proportion of the existing scheme deficits are recoverable through the price controls established by Ofgem

OPERATING AND FINANCIAL REVIEW

LONG TERM STRATEGY, BUSINESS OBJECTIVES AND PERFORMANCE

United Utilities Electricity PLC's strategy is to outperform its regulatory contract (effective April 2005) pursuant to which the Company operates the electricity distribution network

The key objectives of United Utilities Electricity PLC are to

- deliver improved customer service through more efficient processes, systems and higher first time resolution,
- deliver sustainable operating and capital expenditure efficiencies, and
- enable its people to achieve their full potential

Developing a high performance company

Our strategy is built upon the key enabler of a high performance culture and the achievement of a long-term sustainable operating model This requires significant transformational change of the business in the way it will enhance expenditure planning and manage its assets and workforce

Sale of electricity distribution assets

Since the end of the financial year, the Group has realigned its structure to encourage improved performance and to lead to more commercial behaviour As one of the first stages of realigning the existing businesses into the new structure, a new operating entity, United Utilities Electricity Services Limited, has been established This company will focus on the operation and maintenance of the group's electricity assets, currently owned by United Utilities Electricity PLC

The board of United Utilities PLC has taken a decision to initiate a sale process for United Utilities Electricity PLC, which owns the electricity distribution assets, but intends to retain the asset operator function (within United Utilities Electricity Services Limited), consistent with its core skills strategy

The Company has identified a number of measurements against which it assesses its performance

- **Customer minutes lost ('CMLs')** – to meet or out-perform regulatory targets during the regulatory period 2005-10

United Utilities Electricity PLC met the 2006/07 regulatory targets for CMLs set by Ofgem

- **Customer interruptions ('CIs')** – to meet or out-perform regulatory targets during the regulatory period 2005-10

United Utilities Electricity PLC met the 2006/07 regulatory targets for CIs set by Ofgem

- **Overall customer satisfaction** – 85% in the medium-term

Good progress has already been made in meeting the efficiency challenges set by Ofgem and 69 per cent of United Utilities Electricity PLC's customers, who had made an enquiry, were satisfied with the overall service they received Successful delivery of the capital investment programme is vital and the partnership framework approach that has been developed will help to optimise the Company's performance The current strategy is to target customer service and operational performance improvement Overall the Company's progress means that it has a strong platform from which to develop

Our progress on our strategic objectives is monitored by the board of directors by reference to key performance indicators Performance in 2006/07 against these measures is set out in the table below, together with the prior year performance data

OPERATING AND FINANCIAL REVIEW

Key performance indicators

	2007	2006
Fınancıal		
Revenue	£315 6m	£282 4m
Operatıng profit before restructurıng credıt of £0 6m (2006 £0 6m)	£175 5m	£147 6m
Profit before tax	£144 9m	£103 0m
RAV Gearıng [(1)]	44%	47%
Interest cover [(2)]	4 5 tımes	3 2 tımes
Capıtal expendıture on property, plant and equıpment (cashflow)	£175 4m	£142 0m
Non-financıal		
Average mınutes for whıch customers were wıthout supply [(3)]	56 68	51 52
Customer ınterruptıons per 100 customers [(4)]	53 89	47.50
Overall customer satısfactıon [(5)]	69%	70%
Electrıcıty supply avaılabılıty	99 99%	99 99%

[(1)] RAV Gearıng ıs measured as borrowıngs net of cash and short-term deposıts and loans from other Unıted Utılıtıes PLC group companıes dıvıded by the provısıonal Regulatory Asset Value (RAV) of £1,090 3 mıllıon (2006 £1,057 1 mıllıon) The RAV Gearıng ıs on a Company basıs whıch ıs consıstent wıth Ofgem's reportıng requırements

[(2)]Interest cover ıs the number of tımes the net underlyıng finance expense ıs covered by operatıng profit from contınuıng operatıons before restructurıng costs Net underlyıng ınterest expense ıs calculated as the underlyıng cost of borrowıngs excludıng any pensıon adjustment and movements ın the faır value of debt and derıvatıves but ıncludıng the £24 4 mıllıon (2006 £22 0 mıllıon) ınterest on swaps and debt under faır value optıon

[(3)] The mınutes of supply lost per customer ıs an Ofgem measure calculated by takıng the sum of the customer mınutes lost for all restoratıon stages for all ıncıdents and dıvıdıng by the number of connected customers as at 30 September each year The 2007 figure ıs stıll to be audıted by Ofgem

[(4)] Customer ınterruptıons per 100 customers ıs a standard measure of network relıabılıty used by Ofgem and ıs calculated as (total customers affected/total customers connected to the network) x 100 The 2007 figure ıs unaudıted by Ofgem at the date of thıs report

[(5)] Overall customer satısfactıon ın relatıon to the response receıved from an enquıry ıs measured by an ınternal overall customer experıence assessment mechanısm It ınvolves a serıes of ıntervıews wıth customers Sample ıntervıews are conducted monthly

Financıal review

Revenue ıncreased by 11 8 per cent to £315 6 mıllıon ın 2006/07, largely due to an allowed real prıce ıncrease of 2 6 per cent ın the year and adjustments to tarıffs resultıng from underrecoverıes of allowed revenue ın prevıous years Operatıng profit ıncreased by 18 8 per cent to £176 1 mıllıon ın 2006/07, prımarıly reflectıng the ıncrease ın revenue Capıtal ınvestment ın property, plant and equıpment for the year was £175 4 mıllıon (2005/06 £142 0 mıllıon) Thıs ıs wıthın the regulatory allowance for the year and reflects the re-phasıng of expendıture across the 2005-10 regulatory revıew perıod

OPERATING AND FINANCIAL REVIEW

The net finance expense for the year was £31 2 million compared with £45 2 million in 2005/06 This reduction reflects the full year effect of the equity injection in March 2006, fair value movements on debt and derivative financial instruments, and returns on pension scheme assets

Dividends and dividend policy

In 2006/07, United Utilities Electricity PLC dividends recognised in the period were £36 0 million This figure represents a dividend payment relating to the financial year 2005/06 of £24 0 million, and an interim payment in 2006/07 of £12 0 million

The Company's dividend policy is to distribute the theoretical maximum consistent with the 5-year regulatory contract The earnings available for distribution comprise the return on equity assumed by the regulatory contract plus or minus any out-performance or under-performance over the period of the contract

Business performance

United Utilities Electricity PLC places a strong focus on maintaining the integrity, security and safety of its electricity distribution network and ensuring outputs are in line with its five-year delivery plan During the year, the business replaced or refurbished 293 kilometres of overhead lines and replaced 91 kilometres of underground cables It also replaced or refurbished 579 switchgear units and replaced 280 transformers

Business impacts

- **Business restructuring**

Since the end of the financial year, the board of United Utilities PLC has realigned the structure of United Utilities Electricity PLC to encourage improved performance and to lead to more commercial behaviour From 1 April 2007, Utility Solutions will manage the operation of all wastewater and water, electricity and gas networks, whether that is on behalf of United Utilities' own businesses or for external clients The Asset Management and Regulation function will develop and deliver regulatory price review strategy and will engage with key opinion-formers, ministers, regulators and civil servants Finally, the Business Development function will develop a business growth strategy for the Group and deliver its international business' financial targets

- **Sale of electricity distribution assets**

As one of the first stages of realigning the existing businesses into the new structure, a new operating entity, United Utilities Electricity Services Limited, has been established This company will focus on the operation and maintenance of the group's electricity assets, which remain owned by United Utilities Electricity PLC The board has taken a decision to initiate a sale process for the electricity distribution assets but expects to retain the United Utilities Electricity asset operator function

LIQUIDITY AND CAPITAL RESOURCES

The Group's primary source of liquidity is cash generated from its ongoing business operations As reflected in the cashflow statement on page 26, in the financial year ended 31 March 2007, net cash generated from the Group's operating activities was £164 6 million, compared with £64 4 million in 2005/06 The electricity regulator has established price controls to 2010 which will provide certainty for a large majority of the Group's revenues from ongoing operations, providing both a stable and a predictable source of funds

Treasury policy

United Utilities PLC's treasury function operates with the delegated authority of, and under policies approved by, the United Utilities Electricity PLC board The treasury function does not act as a profit centre and does not undertake any speculative trading activity It seeks to ensure that sufficient funding is available to meet foreseeable needs and maintains reasonable headroom for contingencies Long-term borrowings are structured or hedged to match earnings, which are largely in sterling, indexed to inflation and subject to regulatory price reviews every five years Exposure to interest rate movements for the following 12 months, where necessary, are eliminated at the start of each financial year using short-term hedges The credit quality of counterparties and individual aggregate exposures are reviewed annually

OPERATING AND FINANCIAL REVIEW

Debt financing

Moody's Investor Service rates the credit of United Utilities Electricity PLC as A2 on a long-term basis with a stable outlook and P-1 on a short-term basis Equivalent ratings published by Standard and Poor's Rating Services are A- long-term with a stable outlook and A-2 short-term. Standard and Poor upgraded its rating on the 2 April 2007 to A long-term with a stable outlook and A1 short-term The Group's borrowings net of cash and short-term deposits of £481 9 million at 31 March 2007 comprised £642 6 million of bonds, £90 0 million of loans from the European Investment Bank (EIB – the Group's largest debt investor), £7 3 million of bank overdrafts and £0 4 million owed to parent undertaking, offset by £258 4 million of cash and short-term deposits

Shorter-term liquidity

Short-term liquidity requirements are met from the Group's normal operating cashflow Further liquidity is provided by cash and short-term deposit balances, the Group's US$1 5 billion euro-commercial paper programme, supported by committed bank facilities and committed but undrawn long-term credit facilities Cash and short-term deposit balances were £258 4 million at 31 March 2007, compared with £137 0 million at 31 March 2006

Bank overdrafts and temporary borrowings, which are repayable in less than one year, were £7 7 million at 31 March 2007, compared with £14 7 million at 31 March 2006 The Group had available unutilised committed bank facilities of £50 0 million (2006 £75 0 million), of which £20 0 million expires within one year (2006 £30 million), £nil million expires after one year but in less than two years (2006 £20 0 million), and the remaining £30 0 million expires in more than two years (2006 £25 0 million) Although unutilised during the financial year ended 31 March 2007, the US$1 5 billion euro-commercial paper programme still provides for the periodic issuance of notes by United Utilities Electricity PLC United Utilities Electricity PLC has entered into £50 0 million of credit facilities, as noted above, used primarily as support for the US$1 5 billion euro-commercial paper programme

Longer-term liquidity

The Group has effective access to the international debt capital markets through its €7 billion medium-term note programme which provides for the periodic issuance by United Utilities Electricity PLC of debt instruments on terms and conditions determined at the time that the instruments are issued The programme does not represent a funding commitment, with funding only becoming committed when debt securities have been successfully issued The currencies in which borrowings are held are disclosed in note 17 to the financial statements

The Group's term loans were £732 6 million at 31 March 2007, compared with £643 9 million at 31 March 2006 Amounts repayable after more than five years comprise bank and other loans repayable between 2012 and 2046 Fixed interest rates, for amounts after more than five years, are at 8 875 per cent on £539 6 million (2005/06 £553 8 million) and are at floating rates on £90 0 million (2005/06 £90 1 million) of these loans £103 0m of index linked debt was held at 31 March 2007 (2006 nil) at an interest rate of 1 4746% plus retail price index

Interest rate management

The Group manages interest rate exposure by seeking to match financing costs as closely as possible with the revenues generated by its assets The Group's exposure to interest rate fluctuations is periodically managed in the medium-term through the use of interest rate swaps and the use of financial futures contracts traded on the London International Financial Futures and Options Exchange The average interest rate for 2006/07 was 6 55 per cent, compared with 6 84 per cent in 2005/06 excluding fair value adjustments

The Group uses a combination of interest rate swaps, futures and funding instruments to hedge exposure to interest rate volatility The Group's use of derivative instruments relates directly to underlying indebtedness, no speculative or trading transactions are undertaken The proportion of borrowings at effective fixed rates of interest for a period greater than one year is set in conjunction with the level of floating rate borrowings and projected regulatory revenues that are exposed to inflationary adjustments (index linked) In addition, the Group aims to manage its short-term budgetary commitments by ensuring that the majority of floating rate interest is fixed for periods of less than one year through the use of exchange traded financial futures The Group has limited exposure to foreign currency exchange rate movements Interest rate management and funding policies are set by the board

In order to hedge the interest cost implicit in the regulatory contract, the Group fixes interest rates for the duration of each five-year review period by typically swapping fixed rate debt to floating at the time of issue and then swapping back to fixed rate at the outset of each five-year regulatory contract period IAS 39 'Financial Instruments Recognition and Measurement' limits the use of hedge accounting, thereby increasing the potential volatility of the income statement However, this has no cashflow impact and the effect of IAS 39 should broadly balance out over the 2005-10 period

OPERATING AND FINANCIAL REVIEW

Summary

The board has reviewed the business plan and considers that the Group has sufficient liquidity to meet the anticipated financial commitments for the next 12 months In total, at 31 March 2007, unutilised committed facilities of £30 0 million expiring in more than one year, together with cash and short-term deposits of £258 4 million provide substantial pre-funding for the Group

CRITICAL ACCOUNTING POLICIES

The Group prepares its consolidated financial statements in accordance with accounting principles consistent with International Financial Reporting Standards ('IFRS') as adopted for use in the European Union including International Accounting Standards ('IAS') and interpretations issued by the International Financial Reporting Interpretation Committee ('IFRIC') As such, the Group is required to make certain estimates, judgements and assumptions that it believes are reasonable based upon the information available These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the periods presented

On an ongoing basis, the Group evaluates its estimates using historical experience, consultation with experts and other methods considered reasonable in the particular circumstances Actual results may differ significantly from the estimates, the effect of which is recognised in the period in which the facts that give rise to the revision become known

The Group's accounting policies are detailed in the consolidated financial statements The following paragraphs detail the policies the Group believes to have the most significant impact on the annual results under IFRS

Carrying value of long-lived assets

The Group's accounting policy for property, plant and equipment ('PPE') is detailed in the accounting policies section of the consolidated financial statements The carrying value of PPE under IFRS as at 31 March 2007 was £1,831 6 million Additions to PPE totalled £176 7 million and the depreciation charge was £59 4 million in the year ended 31 March 2007 The estimated useful economic lives of PPE are based on management's judgement and experience When management identifies that actual useful lives differ materially from the estimates used to calculate depreciation, that charge is adjusted prospectively Due to the significance of PPE investment to the Group, variations between actual and estimated useful lives could impact operating results both positively and negatively, although historically, few changes to estimated useful lives have been required

In accordance with IFRS, the Group is required to evaluate the carrying values of PPE for impairment whenever circumstances indicate, in management's judgement, that the carrying value of such assets may not be recoverable An impairment review requires management to make subjective judgements concerning the cashflows, growth rates and discount rates of the cash-generating units under review

Revenue recognition

Under IFRS, the Group recognises revenue generally at the time of delivery and when collection of the resulting receivable is reasonably assured Should management consider that the criteria for revenue recognition are not met for a transaction, revenue recognition would be delayed until such time as the transaction becomes fully earned Payments received in advance of revenue recognition are recorded as deferred revenue The Group raises bills and recognises revenue in accordance with its entitlement to receive revenue in line with the limits established by the periodic regulatory price review processes The customers of the business are the electricity supply companies that utilise United Utilities Electricity PLC's distribution network to distribute electricity from generators to the end consumer The amount billed is dependent upon the volume of electricity distributed, including estimates of the units distributed to customers The estimated usage is based on historic data, judgement and assumptions Operating revenues are gradually adjusted to reflect actual usage in the period over which the meters are read

Accounting for provisions and contingencies

The Group is subject to a number of claims incidental to the normal conduct of its business, relating to and including commercial, contractual and employment matters, which are handled and defended in the ordinary course of business The Group routinely assesses the likelihood of any adverse judgements or outcomes to these matters as well as ranges of probable and reasonably estimated losses Reasonable estimates involve judgements made by management after considering information including notifications, settlements, estimates performed by independent

OPERATING AND FINANCIAL REVIEW

parties and legal counsel, available facts, identification of other potentially responsible parties and their ability to contribute and prior experience In accordance with IFRS, a provision is recognised when it is probable that an obligation exists for which a reliable estimate can be made of the obligation after careful analysis of the individual matter The required provision may change in the future due to new developments and as additional information becomes available Matters that either are possible obligations or do not meet the recognition criteria for a provision are disclosed, unless the possibility of transferring economic benefits is remote

Retirement benefits

United Utilities Electricity PLC participates in two defined benefit schemes, one of which has a defined contribution section, which are independent of the Group's finances Actuarial valuations of the schemes for funding purposes are carried out at intervals of not more than three years The pension cost under IAS 19 'Employee Benefits' is assessed in accordance with the advice of a firm of actuaries The assumptions are disclosed in note 20 of the financial statements Results are affected by the actuarial assumptions used These assumptions include those made for investment returns on the schemes' assets, discount rates, pay growth and increases to pensions in payment and deferred pensions Actual experience may differ from the assumptions made, for example, due to changing market and economic conditions and longer or shorter lives of participants

Derivatives and borrowings

The Group's default treatment is for borrowings to be carried at amortised cost, whilst derivatives are recognised separately on the balance sheet at fair value with movements in those fair values reflected through the income statement This has the potential to introduce considerable volatility to both the income statement and balance sheet Therefore, for fair value hedges, changes in the recognised value of hedged debt that are attributable to the hedged risk are adjusted through the income statement In the case of cashflow hedges, movements in the fair value of derivatives are deferred within reserves until they can be recycled through the income statement to offset the future income statement effect of changes in the hedged risk In order to apply this treatment, it must be demonstrated that the derivative has been, and will continue to be, an effective hedge of the hedged risk within the debt item Changes in the fair value of all derivatives are recognised in the income statement, except for derivatives that are designated and effective in terms of cashflow hedging relationships, in which case the gains and losses are deferred in equity The Group applies the fair value option through profit or loss where the complexity of the swaps means that they are disallowed from being allocated in a hedge relationship despite there being significant fair value offset between the hedged item and the derivative itself This area is considered to be of significance due to the magnitude of the Group's level of borrowings

RESEARCH AND DEVELOPMENT

The Company undertakes research primarily to provide improved standards of service to customers, together with continuing improvements in business efficiency Research and development within the Group's electricity network aims to deliver financial, supply quality, environmental and safety improvements to customers and is supported under the Innovation Funding Incentive introduced by Ofgem The Group is a member of a number of collaborative research programmes including EA Technology Limited which addresses common issues that face the electricity industry The Group also undertakes specific projects with these and other research and development providers, manufacturers and with universities Research and development expenditure by the Group was £1 3 million in the year ended 31 March 2007 (2005/06 £0 7 million)

EVENTS AFTER THE BALANCE SHEET DATE

On 4 June 2007, the United Utilities PLC board took the decision to initiate a sale process for UUE's distribution assets United Utilities PLC intends to retain a contract for the operation of its electricity distribution assets

OPERATING AND FINANCIAL REVIEW

CAUTIONARY STATEMENT REGARDING FORWARD LOOKING STATEMENTS

Certain statements included or incorporated by reference within the annual report may constitute 'forward looking statements' Forward looking statements are based on expectations, forecasts and assumptions by our management and involve a number of risks, uncertainties and other factors that could cause actual results to differ materially from those stated

This report contains certain statements with respect to the financial condition, results of operations and business of the Group Some of these statements are not facts, including those about the board's beliefs and expectations Words such as 'expects', 'anticipates', 'intends', 'plans', 'believes', 'seeks', 'estimates', 'potential', 'reasonably possible', 'targets' and variations of these words and similar expressions reflect inherent risks and uncertainty Such statements are based on current plans, estimates and projections, and therefore investors should not rely on them Further, the company undertakes no obligation to update publicly any of them in light of new information or future events and they are relevant only as at the date made The company cautions investors that a number of important factors could cause actual results to differ materially from those anticipated or implied in any forward looking statements These factors include (i) the effect of, and changes in, regulation and government policy, (ii) the effects of competition and price pressures, (iii) the ability of the company to achieve cost savings and operational synergies, (iv) the ability of the company to service its future operations and capital requirements, (v) the timely development and acceptance of new products and services by the company, (vi) the effect of technological changes, and (vii) the company's success in managing the risks of the foregoing There may be additional risks that the Group does not currently know of, or that are deemed immaterial based on either information currently available or the group's current assessment of the risk The Group's business, financial condition or results of operations could be materially affected by any of these risks

The directors of United Utilities Electricity PLC advise that all the information supplied in the managing director's statement on page 3 and the operating and financial review on pages 4 to 18 form part of the directors' report as incorporated by reference Any liability for the information is restricted to the extent prescribed in the Companies Act 2006

DIRECTORS' REPORT

The directors present their report and the audited financial statements of the United Utilities Electricity PLC Group (the 'Group') for the year ended 31 March 2007

Profit and dividends

The results for the year, set out in the income statement on page 23, show that revenue for the year ended 31 March 2007 increased to £315 6 million (2006 £282 4 million), an increase of 11 8 per cent over the previous year Profit for the year after tax was £112 3 million (2006 £77 3 million)

An interim dividend of £12 0 million was paid in March 2007 for the year ended 31 March 2007 (2006 £11 7million), and a final dividend for the year ended 31 March 2006 of £24 0 million was paid in the year (2006 £39 1 million) The directors have recommended a final ordinary dividend for 2006/07 of £100 0 million

Business review and principal activities

The Company is a wholly owned subsidiary of United Utilities PLC The Company's principal activity is the operation of electricity distribution assets The distribution of electricity is regulated by the terms of the Company's Electricity Distribution Licence granted under the Electricity Act 1989 and monitored by the Gas and Electricity Markets Authority There have not been any significant changes in the Company's principal activities in the year under review The directors are not aware, at the date of this report, of any likely major changes in the Company's activities in the next year apart from the sale of the distribution assets as mentioned below

On 30 March 2007 the Company disposed of its interest in its non-trading subsidiary NB Generation Limited as detailed in note 29

On 4 June 2007, the United Utilities PLC board took the decision to initiate a sale process for United Utilities Electricity PLC's distribution assets United Utilities PLC intends to retain a contract for the operation of its electricity distribution assets

The managing director's statement and the operating and financial review on pages 3 to 18 report on the Company's activities during the year and on likely future developments A summary of key performance indicators can be found in the operating and financial review The directors, in preparing the operating and financial review, have not sought to comply with the ASB's 2006 Reporting Statement on operating and financial reviews All the information supplied in the managing director's statement on page 3 and the operating and financial review on pages 4 to 18 form part of the directors' report as incorporated by reference Any liability is restricted to the extent prescribed in the Companies Act 2006

Principal risks and uncertainties

Principal risks and uncertainties are discussed as part of the operating and financial review

Research and development

The Group is committed to developing innovative, cost-effective and practical solutions for providing high quality services and standards to our customers, and for the benefit of the wider community and the development of the business It seeks to take as part of this process maximum advantage of wide-ranging expertise, abilities and facilities within the Group

Employees

Employees are key to achieving the business strategy and enhancing shareholder value and as such the Group remains committed to maintaining high standards of health and safety in every area of its business

The Group is committed to improving its employees' skills through training and development and nurturing a culture in which employees feel valued The Group encourages employees to work to their full potential and respects the dignity and rights of every employee and supports them in performing various roles in society The Group also challenges prejudice and stereotyping

The Group is committed to fulfilling its obligations in accordance with the Disability Discrimination Act 1995 and best practice As an equal opportunities employer, the Group gives equal consideration to applicants with disabilities in its employment criteria and will modify equipment and working practices wherever it is safe and practical to do so, both for new employees, and for those employees that are disabled during the course of their employment Additionally, the Group is committed to providing full support and appropriate training for employees who become disabled during the course of their employment, so they can continue to work in a position appropriate to their experience and abilities

DIRECTORS' REPORT

The Group believes that share ownership is an effective way of strengthening employees' involvement in the development of the business and bringing together their interests and those of the shareholders A sharebuy scheme offers employees an opportunity to build up a shareholding in the ultimate parent company United Utilities PLC

Policy on the payment of creditors

The policy is to pay suppliers according to agreed terms of business These terms are agreed upon entering into binding contracts and the Group seeks to adhere to the payment terms, provided the relevant goods and services have been supplied in accordance with the contracts The Group and Company had 43 days of purchases outstanding at the end of the financial year (2006 49 days)

Directors

The directors of the Company during the year ended 31 March 2007 are set out below All were directors for the whole year except where otherwise indicated

S G Batey (resigned 26 July 2006)*

S Beaumont (resigned 5 July 2006)

M Beesley

M J Boxall

E Cooke

C Cornish*

A Cowan (appointed 1 February 2007)

G Dixon (resigned 30 November 2006)

T Weller (appointed 1 August 2006)*

*Director, United Utilities PLC

Details of directors' interests in the share capital of United Utilities PLC are set out in note 9 to the accounts or in the accounts of United Utilities PLC where appropriate

At no time during the year did any director have a material interest in any contract or arrangement which was significant in relation to the Group's business

Directors' and officers' insurance

The Company maintains an appropriate level of directors' and officers' insurance whereby directors are indemnified against liabilities to third parties to the extent permitted by the Companies Act

Directors' responsibilities in respect of the preparation of the financial statements

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial year Under that law the directors have elected to prepare the financial statements in accordance with IFRSs as adopted by the European Union The financial statements are required by law to be properly prepared in accordance with IFRS as adopted by the European Union and the Companies Act 1985

IAS 1 ' Presentation of Financial Statements' requires that the financial statements present fairly for each financial year the company's financial position, financial performance and cashflows This requires the faithful representation of the effects of the transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's 'Framework for the Preparation and Presentation of Financial Statements' In virtually all circumstances, a fair presentation will be achieved by the compliance with all applicable IFRS

DIRECTORS' REPORT

In preparing the financial statements, the directors are required to

- properly select and apply accounting policies,
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information,
- provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial performance, 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 confirm that the financial statements comply with the above requirements The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy the financial position of the company and to enable them to ensure that the statutory financial statements comply with the Companies Act 1985 They have a general responsibility for the system of internal control and for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities

Information given to auditors

Each of the persons who is a director at the date of approval of this report confirms that

(1) so far as the director is aware, there is no relevant audit information of which the Company's auditors are unaware, and

(2) the director has taken all the steps that he/she ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information

This confirmation is given and should be interpreted in accordance with the provisions of s234ZA of the Companies Act 1985

Independent auditor

A resolution to reappoint Deloitte & Touche LLP as the auditor of the Company will be proposed at the forthcoming annual general meeting

Registered address

United Utilities Electricity PLC
Haweswater House
Lingley Mere Business Park
Lingley Green Avenue
Great Sankey
Warrington
WA5 3LP

Registered number 2366949

By order of the board

Mike Boxall

Mike Boxall
Director

25 July 2007

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF

UNITED UTILITIES ELECTRICITY PLC

We have audited the group and company financial statements of United Utilities Electricity PLC for the year ended 31 March 2007 which comprise the consolidated income statement, the consolidated and company balance sheets, the consolidated and company statements of recognised income and expense, the consolidated and company cashflow statements and the related notes 1 to 32 These financial statements have been prepared under the accounting policies set out therein

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985 Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland)

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985 We also report to you whether in our opinion the information given in the directors' report is consistent with the financial statements The information given in the directors' report includes that specific information presented in the managing director's statement and the operating and financial review that is cross-referenced from the "Business review and principal activities" section of the directors' report

In addition, we report to you if, in our opinion, 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 other transactions is not disclosed

We read the other information contained in the Annual Report as described in the contents section and consider whether it is consistent with the audited financial statements The other information comprises only the managing director's statement, the operating and financial review and the directors' report We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements Our responsibilities do not extend to any further information outside the Annual Report

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the company and the group, 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 financial statements 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 financial statements

Opinion

In our opinion

- the group and individual company financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the group's and company's affairs as at 31 March 2007 and of the profit of the group for the year then ended,
- the financial statements have been properly prepared in accordance with the Companies Act 1985, and
- the information given in the directors' report is consistent with the financial statements

Deloitte & Touche LLP Deloitte & Touche LLP
Chartered Accountants and Registered Auditors
Manchester, England
27 July 2007

CONSOLIDATED INCOME STATEMENT
For the year ended 31 March 2007

	Note	Group 2007 £m	Group 2006 £m
Revenue	2	315 6	282 4
Employee benefits expense	4	(18 3)	(21 2)
Depreciation and amortisation expense		(55 5)	(48 9)
Other operating costs		(66 3)	(64 7)
Restructuring credit		0 6	0 6
Total operating expenses		(139 5)	(134 2)
Operating profit	3	176 1	148 2
Investment income	5	19 7	8 8
Finance expense	6	(50 9)	(54 0)
Investment income and finance expense		(31 2)	(45 2)
Profit before taxation		144 9	103 0
Taxation	7	(32 6)	(25 7)
Profit for the year		112 3	77 3

All the results shown in the consolidated income statement derive from continuing operations

Operating profit and investment income for 2006 have been re-presented as the Group has changed its presentation of interest income and expenditure associated with its defined benefit pension schemes (see note 5)

BALANCE SHEETS
At 31 March 2007

	Note	Group 2007 £m	Company 2007 £m	Group 2006 £m	Company 2006 £m
ASSETS					
Non-current assets					
Intangible assets	10	24 2	24 2	28 1	28 1
Property, plant and equipment	11	1,831 6	1,831 6	1,714 3	1,714 3
Investment property	12	-	-	5 4	5 4
Other investments	13	-	-	1 0	35 7
Derivative financial instruments	18	2 1	2 1	-	-
Retirement benefit surplus	20	24 5	24 5	-	-
		1,882 4	1,882 4	1,748 8	1,783 5
Current assets					
Inventories	14	3 3	3 3	3 4	3 4
Trade and other receivables	15	106 8	106 5	54 4	50 8
Cash and cash equivalents	16	258 4	258 4	137 0	137 0
Derivative financial instruments	18	4 4	4 4	13 0	13 0
		372 9	372 6	207 8	204 2
Total assets		2,255 3	2,255 0	1,956 6	1,987 7
LIABILITIES					
Non-current liabilities					
Borrowings	17	(732 6)	(732 6)	(643 9)	(643 9)
Retirement benefit obligations	20	-	-	(1 8)	(1 8)
Deferred tax	21	(325 0)	(325 0)	(305 4)	(305 4)
Provisions	22	-	-	(1 3)	(1 3)
Consumer contributions	23	(300 5)	(300 5)	(245 9)	(245 9)
Refundable customer deposits	24	(10 6)	(10 6)	(6 1)	(6 1)
		(1,368 7)	(1,368 7)	(1,204 4)	(1,204 4)
Current liabilities					
Borrowings	17	(7 7)	(7 7)	(14 7)	(14 7)
Trade and other payables	19	(152 3)	(151 4)	(112 7)	(160 5)
Derivative financial instruments	18	(6 7)	(6 7)	(1 9)	(1 9)
Current income tax liabilities		(38 2)	(38 2)	(36 3)	(33 3)
		(204 9)	(204 0)	(165 6)	(210 4)
Total liabilities		(1,573 6)	(1,572 7)	(1,370 0)	(1,414 8)
Total net assets		681 7	682 3	586 6	572 9
EQUITY					
Called up share capital	25	238 4	238 4	238 4	238 4
Share premium account	26	4 4	4 4	4 4	4 4
Revaluation reserve	26	122 4	122 4	127 0	127 0
Capital redemption reserve	26	8 6	8 6	8 6	8 6
Retained earnings	26	307 9	308 5	208 2	194 5
Total equity		681 7	682 3	586 6	572 9

Approved by the board of directors on 25 July 2007 and signed on its behalf by

Eóin Cooke

Eóin Cooke
Director

STATEMENTS OF RECOGNISED INCOME AND EXPENSE
For the year ended 31 March 2007

	Note	Group 2007 £m	Company 2007 £m	Group 2006 £m	Company 2006 £m
Losses on wnte back of trade and other payables on adoption of IAS 39		-	-	(1 0)	(1 0)
Gains on debt and derivative instruments on adoption of IAS 39		-	-	11 2	11 2
Fair value gain/(loss) on cashflow hedges	18	2 1	2 1	(0 7)	(0 7)
Actuarial gains on defined benefit pension schemes	20	24 8	24 8	35 6	35 6
Deferred tax on items taken directly to equity	21	(8 2)	(8 2)	(13 7)	(13 7)
Net income recognised directly in equity		18 7	18 7	31 4	31 4
Profit for the year		112 3	126 6	77 3	78 3
Total recognised income and expense for the year		131 0	145 3	108 7	109 7

CASHFLOW STATEMENTS
For the year ended 31 March 2007

	Note	Group 2007 £m	Company 2007 £m	Group 2006 £m	Company 2006 £m
Operating activities					
Cash generated from operations	31	212 7	212 7	125 2	159 4
Interest paid		(43 6)	(43 6)	(50 0)	(50 0)
Interest received and similar income		11 8	11 8	2 8	2 8
Tax paid		(16 3)	(16 3)	(13 6)	(13 6)
Net cash generated from operating activities		164 6	164 6	64 4	98 6
Investing activities					
Disposal of subsidiaries	29	-	-	29 6	29 4
Purchase of investment property		(0 3)	(0 3)	-	-
Purchase of property, plant and equipment		(175 4)	(175 4)	(142 0)	(142 0)
Purchase of other intangible assets		(0 9)	(0 9)	(6 3)	(6 3)
Consumer contributions received		67 3	67 3	37 1	37 1
Proceeds from sale of investment property		6 0	6 0	5 8	5 8
Proceeds from sale of property, plant and equipment		1 3	1 3	3 3	3 3
Net cash used in investing activities		(102 0)	(102 0)	(72 5)	(72 7)
Financing activities					
Proceeds on issue of ordinary shares		-	-	160 0	160 0
Proceeds from borrowings		100 0	100 0	34 1	0 1
Repayment of borrowings		(4 4)	(4 4)	(4 4)	(4 4)
Dividends paid to equity shareholders of the Company		(36 0)	(36 0)	(50 8)	(50 8)
Net cash generated from financing activities		59 6	59 6	138 9	104 9
Net increase in cash and cash equivalents		122 2	122 2	130 8	130 8
Cash and cash equivalents at beginning of the year		128 9	128 9	(1 9)	(1 9)
Cash and cash equivalents at end of the year	16	251 1	251 1	128 9	128 9

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

1. ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these financial statements are set out below

a) Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards ('IFRS') as adopted for use in the European Union, including International Accounting Standards (IAS) and interpretations issued by the International Financial Reporting Interpretations Committee ('IFRIC')

The financial statements have been prepared on the historical cost basis, except for the revaluation of financial instruments, investment properties and certain property, plant and equipment

The preparation of financial statements, in conformity with generally accepted accounting principles ('GAAP') under IFRS, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from these estimates

b) Basis of consolidation

The Group financial statements consolidate the financial statements of the Company and entities controlled by the Company (its subsidiaries), made up to 31 March each year

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate

Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used under the relevant local GAAP into line with those used by the Group

Subsidiaries

Control is achieved where the Company has the power to govern the financial and operating policies, generally accompanied by a shareholding of more than one half of the voting rights, of an invested entity so as to obtain benefits from its activities On acquisition, the assets and liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill Any deficiency of the cost of acquisition below the fair values of the identifiable net assets acquired is credited to the income statement in the period of acquisition All intra-group transactions, balances, income and expenses are eliminated on consolidation

Associates

An associate is an entity over which the Group, either directly or indirectly, is in a position to exercise significant influence by participating in, but not controlling, the financial and operating policies of the entity Associates are accounted for using the equity method Losses of an associate in excess of the Group's interest in the associate are not recognised, except to the extent that the Group has incurred obligations in respect of the associate Unrealised profits and losses recognised by the Group on transactions with an associate are eliminated to the extent of the Group's interest in the associate concerned

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

1. ACCOUNTING POLICIES (continued)

c) Intangible assets

Intangible assets are measured initially at cost and are amortised on a straight-line basis over their estimated useful lives Carrying amount is reduced by any provision for impairment where necessary

Amortisation periods for categories of intangible assets are

Computer software 3-10 years

d) Property, plant and equipment

Property, plant and equipment comprises operational structures and other assets (including properties, overground plant and equipment and electricity operational assets)

Operational structures
Infrastructure assets are depreciated by writing off their deemed cost less the estimated residual value, evenly over their useful lives, which range from 5 to 80 years Employee costs incurred in implementing the capital schemes of the Group are capitalised within operational structure assets

Other assets
All other property, plant and equipment is stated at historical cost less accumulated depreciation

Historical cost includes expenditure that is directly attributable to the acquisition of the items Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred

Freehold land and assets in the course of construction are not depreciated Other assets are depreciated by writing off their cost evenly over their estimated useful lives, based on management's judgement and experience, which are principally as follows

Buildings 30-60 years
Operational assets 5-80 years
Fixtures, fittings, tools and equipment 3-40 years

Depreciation methods and useful lives are re-assessed annually and, if necessary, changes are accounted for prospectively

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in income

e) Impairment of tangible and intangible assets

Intangible assets with definite useful lives and property, plant and equipment are reviewed for impairment at each reporting date to determine whether there is any indication that those assets may have suffered an impairment loss If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any Where the asset does not generate cashflows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs

The recoverable amount is the higher of fair value less costs to sell, and value in use Value in use represents the net present value of expected future cashflows discounted on a pre-tax basis using a rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cashflows have not been adjusted

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

1. ACCOUNTING POLICIES (continued)

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount Impairment of non-current assets is recognised in the income statement within operating costs

Where an impairment loss subsequently reverses, the reversal is recognised in the income statement and the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but not so as to exceed the carrying amount that would have been determined had no impairment loss been recognised in prior years

f) Inventories

Inventories are stated at cost less any provision necessary to recognise damage or obsolescence

g) Financial instruments

Financial assets and financial liabilities are recognised on the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument

Cash and cash equivalents

In the consolidated cashflow statement and related notes, cash and cash equivalents includes cash at bank and in hand, deposits, other short-term highly liquid investments which are readily convertible on initial investment into known amounts of cash within three months and which are subject to an insignificant risk of change in value

Financial investments

Investments (other than interests in subsidiaries and fixed deposits) are recognised and derecognised on a trade date basis and are initially measured at fair value, including transaction costs Investments are classified as available-for-sale and are measured at subsequent reporting dates at fair value Gains and losses arising from changes in fair value are recognised directly in equity, until the security is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is included in the net profit or loss for the period

Trade receivables

Trade receivables are stated at nominal value less allowances for estimated irrecoverable amounts

Trade payables

Trade payables are stated at their nominal value

Financial liabilities and equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities

Equity instruments

Equity instruments issued by the Group are recorded at the proceeds received, net of direct issue costs

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

1. ACCOUNTING POLICIES (continued)

Bank borrowings

Interest-bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an amortised cost basis to the income statement using the effective interest method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise

Derivative financial instruments and hedge accounting

Interest rate swap agreements and financial futures are used to manage interest rate exposure The Group does not use derivative financial instruments for speculative purposes

All financial derivatives are recognised in the balance sheet at fair value Changes in the fair value of all derivative financial instruments are recognised in the income statement within finance expense as they arise, except for derivatives that are designated and effective in terms of cashflow hedging relationships, in which case the gains and losses are deferred in equity

Where hedge accounting has not been applied, the Group may elect to designate a financial liability at inception as fair value through the income statement provided the financial liability meets the conditions specified in IAS 39 'Financial Instruments Recognition and measurement' Where possible, hedge accounting is applied

Fair value hedges

For an effective hedge of an exposure to changes in the fair value, the hedged item is adjusted for changes in fair value attributable to the risk being hedged with the corresponding entry in the income statement Gains or losses from remeasuring the derivative are recognised in profit or loss

Where changes in the fair value of a derivative differ from changes in the fair value of the hedged item attributable to the risks being hedged, the hedge ineffectiveness is recorded in the income statement within finance costs Hedge accounting is discontinued prospectively when the hedging instrument is sold, terminated or exercised, where the hedge relationship no longer meets the criteria for hedge accounting in accordance with IFRS, or where the hedge designation is revoked Any adjustment that has been recognised to the hedged item, for which the effective interest rate is used, is amortised to the income statement and is based on the recalculated effective interest rate at the time at which amortisation commences

For those of the Group's derivative instruments stated at fair value, the fair value will be determined by the Group applying discounted cashflow analysis using quoted market rates as an input into the valuation model

Cashflow hedges

Changes in the fair value of derivative financial instruments that are designated and effective as hedges of future cashflows are recognised directly in equity and the ineffective portion is recognised immediately in the income statement For hedges that do not result in the recognition of a non-financial asset or liability, amounts deferred in equity are recognised in the income statement in the same period in which the hedged item affects net profit or loss Hedge ineffectiveness is recognised directly in the income statement within finance costs Hedge accounting is discontinued when the hedge designation is revoked, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting At that time, any cumulative gain or loss on the hedging instrument recognised in equity is retained in equity until the forecast transaction occurs If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to net profit or loss for the period

Financial assets and liabilities designated at fair value through profit or loss

The Group applies this designation where the complexity of the swaps means that they are disallowed from being allocated in a hedge relationship despite there being significant fair value offset between the hedged item and the derivative itself The otherwise inconsistent accounting treatment that would have resulted allows the Group to

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

1. ACCOUNTING POLICIES (continued)

satisfy the criteria for this designation The treatment of financial assets and liabilities designated at fair value through the income statement is consistent with the Group's documented risk management strategy

h) Borrowing costs and finance income

All borrowing costs and finance income are recognised in the income statement in the period in which they are accrued

i) Construction contracts

Where the outcome of a construction contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract activity at the balance sheet date, as measured by the proportion that contract costs incurred for work performed to date bear to the estimated total contract costs, except where this would not be representative of the stage of completion Variations in contract work, claims and incentive payments are included to the extent that they have been agreed with the customer

Where the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised to the extent of contract costs incurred that it is probable will be recovered Contract costs are recognised as expenses in the period in which they are incurred When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately

j) Operating profit

Operating profit is stated after charging operating expenses but before investment income and finance expense

k) Taxation

The tax expense represents the sum of the tax currently payable and deferred tax

Current taxation

Current tax, representing UK corporation tax, is based on the taxable profit for the period and is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantially enacted at the balance sheet date Taxable profit differs from the net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible

Deferred taxation

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit Deferred tax liabilities are provided, using the liability method, on all taxable temporary differences at the balance sheet date Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the temporary timing differences are expected to reverse based on tax rates and laws that have been enacted or substantially enacted at the balance sheet date

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer more likely than not that sufficient taxable profits will be available to allow all or part of the asset to be

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

1. ACCOUNTING POLICIES (continued)

recovered Deferred tax is charged or credited to the income statement, except when it relates to items charged or credited to equity, in which case the deferred tax is also dealt with in equity

l) Employee benefits

Retirement benefit obligations

The Group participates in two defined benefit pension schemes, operated by United Utilities PLC, which are independent of the Group's finances, for the substantial majority of its employees Actuarial valuations of the schemes for funding purposes are carried out using the projected unit credit method at intervals of not more than three years, the rates of contribution payable and the pension cost being determined on the advice of the actuaries, having regard to the results of these valuations In any intervening years, the actuaries review the continuing appropriateness of the contribution rates

Defined benefit assets are measured at fair value while liabilities are measured at present value The difference between the two amounts is recognised as a surplus or obligation in the balance sheet

The cost of providing pension benefits to employees relating to the current year's service and the difference between the expected return on scheme assets and interest on scheme liabilities are included within the income statement within employee costs The difference between the expected return on scheme assets and interest on scheme liabilities are included within the income statement within finance expense

All actuarial gains and losses are recognised outside the income statement in retained earnings and presented in the statement of recognised income and expense

In addition, the Group also operates defined contribution pension schemes Payments are charged as employee costs as they fall due The Group has no further payment obligations once the contributions have been paid

Share-based compensation arrangements

United Utilities PLC operates equity-settled, share-based compensation plans in the shares of United Utilities PLC In accordance with the transitional provisions, IFRS 2 'Share-based Payments' has been applied to all grants of equity instruments after 7 November 2002 that were unvested as of 1 April 2004

United Utilities PLC issues equity-settled share-based payments to certain employees Equity-settled share-based payments are measured at fair value at the date of grant The fair value determined at the grant date is expensed on a straight-line basis over the vesting period, based on estimates of the number of options that are expected to vest Fair value is based on both simulation and binomial models, according to the relevant measures of performance

At each balance sheet date, United Utilities PLC revises its estimate of the number of options that are expected to become exercisable with the impact of any revision being recognised in the income statement, and a corresponding adjustment to equity over the remaining vesting period The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised

United Utilities Electricity PLC is recharged the amount expensed under IFRS 2 that relates to United Utilities Electricity PLC employees

m) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated

Expenditure that relates to an existing condition caused by past operations that does not contribute to current or future earnings is expensed

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

1. ACCOUNTING POLICIES (continued)

n) Revenue recognition

Revenue represents the fair value of the income receivable in the ordinary course of business for the distribution of electricity during the year, exclusive of value-added tax

The Group recognises revenue generally at the time of delivery and when collection of the resulting receivable is reasonably assured Payments received in advance of revenue recognition are recorded as deferred revenue

o) Contributions

Contributions receivable in respect of property, plant and equipment are treated as deferred income, which is credited to the income statement over the estimated economic lives of the related assets

p) Leases

Operating lease rentals are charged to the income statement on a straight-line basis over the period of the lease

q) Critical accounting judgements and key sources of estimation uncertainty

In the process of applying the Group's accounting policies, the Group is required to make certain estimates, judgements and assumptions that it believes are reasonable based upon the information available These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the periods presented

On an ongoing basis, the Group evaluates its estimates using historical experience, consultation with experts and other methods considered reasonable in the particular circumstances Actual results may differ significantly from the estimates, the effect of which is recognised in the period in which the facts that give rise to the revision become known

The following paragraphs detail the policies the Group believes to have the most significant impact on the annual results under IFRS

Carrying value of property, plant and equipment

The carrying value of property, plant and equipment (PPE) as at 31 March 2007 was £1,831 6 million Additions to PPE totalled £176 7 million and the depreciation charge was £59 4 million in the year ended 31 March 2007 The estimated useful economic lives of PPE are based on management's judgement and experience When management identifies that actual useful lives differ materially from the estimates used to calculate depreciation, that charge is adjusted prospectively Due to the significance of PPE investment to the Group, variations between actual and estimated useful lives could impact operating results both positively and negatively, although historically, few changes to estimated useful lives have been required

The Group is required to evaluate the carrying values of PPE for impairment whenever circumstances indicate, in management's judgement, that the carrying value of such assets may not be recoverable An impairment review requires management to make subjective judgements concerning the cashflows, growth rates and discount rates of the cash-generating units under review

Revenue recognition

The Group recognises revenue generally at the time of delivery and when collection of the resulting receivable is reasonably assured Should management consider that the criteria for revenue recognition are not met for a transaction, revenue recognition would be delayed until such time as the transaction becomes fully earned Payments received in advance of revenue recognition are recorded as deferred revenue

The customers of the electricity distribution business are the electricity supply companies that utilise United Utilities Electricity PLC's distribution network to distribute electricity from generators to the end consumer

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

1. ACCOUNTING POLICIES (continued)

The receivable billed is dependent upon the volume of electricity distributed, including estimates of the units distributed to customers The estimated usage is based on historical data, judgement and assumptions Operating revenues are gradually adjusted to reflect actual usage in the period over which the meters are read

Provision for doubtful receivables

At each balance sheet date, the Company and each of its subsidiaries evaluate the collectability of trade receivables and record provisions for doubtful receivables based on experience These provisions are based on, amongst other things, comparisons of the relative age of accounts and consideration of actual write-off history The actual level of receivables collected may differ from the estimated levels of recovery, which could impact operating results positively or negatively As at 31 March 2007, the Group's gross trade receivables were £13 1 million and the provision for doubtful receivables was £0 8 million

Accounting for provisions and contingencies

The Group is subject to a number of claims incidental to the normal conduct of its business, relating to and including commercial, contractual and employment matters, which are handled and defended in the ordinary course of business The Group routinely assesses the likelihood of any adverse judgements or outcomes to these matters as well as ranges of probable and reasonably estimated losses Reasonable estimates involve judgements made by management after considering information including notifications, settlements, estimates performed by independent parties and legal counsel, available facts, identification of other potentially responsible parties and their ability to contribute, and prior experience A provision is recognised when it is probable that an obligation exists for which a reliable estimate can be made of the obligation after careful analysis of the individual matter. The required provision may change in the future due to new developments and as additional information becomes available Matters that either are possible obligations or do not meet the recognition criteria for a provision are disclosed, unless the possibility of transferring economic benefits is remote

Retirement benefits

The Group participates in two defined benefit schemes operated by United Utilities PLC, one of which has a defined contribution section, which are independent of the Group's finances Actuarial valuations of the schemes for funding purposes are carried out at intervals of not more than three years The pension cost under IAS 19 'Employee Benefits' is assessed in accordance with the advice of a firm of actuaries The assumptions are disclosed in note 20 Results are affected by the actuarial assumptions used These assumptions include those made for future investment returns on the schemes' assets, discount rates, pay growth and increases to pensions in payment and deferred pensions Actual experience may differ from the assumptions made for example due to changing market and economic conditions and longer or shorter lives of participants

Derivatives and borrowings

The Group's default treatment is for borrowings to be carried at amortised cost, whilst derivatives are recognised separately on the balance sheet at fair value with movements in those fair values reflected through the income statement This has the potential to introduce considerable volatility to both the income statement and balance sheet

Therefore, for fair value hedges, changes in the recognised value of hedged debt that are attributable to the hedged risk are adjusted through the income statement In the case of cashflow hedges, movements in the fair value of derivatives are deferred within reserves until they can be recycled through the income statement to offset the future income statement effect of changes in the hedged risk In order to apply this treatment, it must be demonstrated that the derivative has been, and will continue to be, an effective hedge of the hedged risk within the debt item Changes in the fair value of all derivatives are recognised in the income statement, except for derivatives that are designated and effective in terms of cashflow hedging relationships, in which case the gains and losses are deferred in equity The Group applies the fair value through profit or loss option where the complexity of the swaps means that they are disallowed from being allocated in a hedge relationship despite there being significant fair value offset between the hedged item and the derivative itself This area is considered to be of significance due to the magnitude of the Group's level of borrowings

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

1. ACCOUNTING POLICIES (continued)

Recently issued accounting pronouncements - International Financial Reporting Standards

At the date of authorisation of these financial statements, the following relevant standards and interpretations were in issue but not yet effective The directors anticipate that the adoption of these standards and interpretations will have no material impact on the Group's financial statements The directors anticipate that the Group will adopt these standards and interpretations on their effective dates

IAS 1 'Amendment – Capital Disclosures', is effective for periods commencing on or after 1 January 2007
IAS 23 'Amendment – Borrowing Costs' On 29 March 2007, the International Accounting Standards Board (IASB) issued a revised IAS 23 'Borrowing costs' The main change from the previous version is the removal of the option of immediately recognising as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for sale The revised standard is effective for periods commencing on or after 1 January 2009 The Group is, therefore, required to capitalise borrowing costs as part of the qualifying assets from 1 April 2009
IFRS 7 'Financial Instruments Disclosures' On 18 August 2005, the IASB issued IFRS 7 'Financial Instruments Disclosures' This standard is effective for periods commencing after 1 January 2007 As a result of the adoption of this standard, the Group's disclosures regarding financial instruments will change from those currently disclosed in the financial statements
IFRS 8 'Operating Segments', issued in November 2006, is effective for periods commencing on or after 1 January 2009
IFRIC 8 'Scope of IFRS 2', issued in January 2006, is effective for periods commencing on or after 1 May 2006
IFRIC 9 'Reassessment of Embedded Derivatives', issued in March 2006, is effective for periods commencing on or after 1 June 2006
IFRIC 10 'Interim Financial Reporting and Impairment', issued in July 2006, is effective for periods commencing on or after 1 November 2006
IFRIC 11 'Group and Treasury Share Transactions', issued in November 2006, is effective for periods commencing on or after 1 March 2007
IFRIC 12 'Service Concession Arrangements', issued in November 2006, is effective for periods commencing on or after 1 January 2008

Interpretations in issue but not considered relevant to the activities of the group are as follows

IFRIC 1 'Changes in Existing Decommissioning, Restoration and Similar Liabilities'
IFRIC 2 'Members' Shares in Cooperative Entities and Similar Instruments'
IFRIC 5 'Rights to Interests Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds'
IFRIC 6 'Liabilities Arising from Participating in a Specific Market–Waste Electrical and Electronic Equipment'
IFRIC 7 'Applying the Re-statement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies'

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

2. REVENUE

	2007 £m	2006 £m
Revenue	315 6	282 4

All revenue predominantly arises from the principal activity of electricity distribution and associated activities

The geographical origin and destination of revenue is all within the United Kingdom.

3. OPERATING PROFIT

The following items have been included in arriving at the Group's operating profit

	2007 £m	2006 £m
Employee benefits expense		
Employee costs (see note 4)	18 3	21 2
Depreciation and amortisation expense		
Depreciation of property, plant and equipment		
Owned assets (see note 11)	59 4	52 5
Investment property (see note 12)	0 8	0 3
Amortisation of intangible assets and contributions		
Software (see note 10)	3 5	2 7
Consumer contributions (see note 23)	(8 2)	(6 6)
Other income		
Profit on disposal of property, plant and equipment	1 3	1 5
Profit on disposal of investment property	1 1	0 5
Other operating costs include:		
Research and development	1 3	0 7
Operating leases		
- land and buildings	0 6	0 4
- hire of plant and machinery	1 8	2 2
Restructuring credit	(0 6)	(0 6)

During the year, the Group obtained the following services from the Group's auditors, at costs detailed below

	2007 £m	2006 £m
Audit services		
Statutory audit	0 2	0 1
Audit related regulatory reporting	0 1	-

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

4. DIRECTORS AND EMPLOYEES

Directors' remuneration

	2007 £m	2006 £m
Salaries	0 3	0 3
Benefits	-	0 1
Bonus	0 1	0 1
Share-based payments	0 1	0 1
	0 5	0 6

Employee costs

	2007 £m	2006 £m
Wages and salaries	48 2	46 8
Social security costs	4 2	4 1
Pension costs (see note 20)	5 5	7 8
	57 9	58 7
Capital schemes and charges against provisions	(39 6)	(37 5)
Charged to the income statement	18 3	21 2

Average number of employees during the year (full-time equivalent)

	2007 Number	2006 Number
Electricity distribution	1,306	1,305

The total expense included within operating profit in respect of share-based payments was £0 4 million (2006 £0 1million)

5. INVESTMENT INCOME

	2007 £m	2007 £m	2006 £m	2006 £m
Interest receivable		12 8		3 6
Profit on disposal of subsidiary (see note 29)		-		0 3
Expected return on pension scheme assets	42 5		36 2	
Interest cost on pension scheme obligations	(35 6)		(31 3)	
Net pension interest credit		6 9		4 9
		19 7		8 8

The Group has changed its presentation of interest income and expenditure associated with its defined benefit pension schemes (see note 20) The amounts were previously disclosed within operating profit, but have been reclassified to investment income in the income statement as the directors believe this provides a fairer presentation of the nature of the income and costs Corresponding amounts for 2006 have been re-presented accordingly

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

6. FINANCE EXPENSE

	2007 £m	2006 £m
Fair value loss on debt and derivative instruments	23 2	25 5
Interest payable on bank borrowings	27 1	26 7
Interest payable to Group undertakings	0 6	1 8
	50 9	54 0

The Group has changed its presentation of interest on swaps and interest on debt under the fair value option The amounts were previously disclosed within interest payable on bank borrowings but have been reclassified to the fair value movement on debt and derivative instruments line as the directors believe this provides a fairer presentation of the nature of the interest Corresponding amounts for 2006 have been re-presented accordingly The reclassification for 2006 has reduced interest payable on bank borrowings by £22 0 million and increased the fair value loss on debt and derivative instruments by the same amount

7. TAXATION

	2007 £m	2006 £m
Current tax:		
UK corporation tax	38 0	23 8
Prior year	(16 8)	0 4
Deferred tax (note 21):		
Current year	8 9	6 0
Prior year	2 5	(4 5)
	32 6	25 7

Corporation tax is calculated at 30 per cent (2006 30 per cent) of the estimated assessable profit for the year

The table below reconciles the notional tax charge at the UK corporation tax rate to the effective tax rate for the year

	2007 £m	2007 %	2006 £m	2006 %
Profit before tax	144 9		103 0	
Tax at the UK corporation tax rate of 30%	43 5	30 0	30 9	30 0
Prior years' tax adjustments	(14 3)	(9 9)	(4 1)	(4 0)
Non-taxable (income)/expense	3 4	2 4	(1 1)	(1 1)
	32 6	22 5	25 7	24 9

In addition to the amount charged to the income statement, deferred tax relating to actuarial gains on defined benefits schemes of £7 6 million charge (2006 £10 7 million) and adjustments under IAS 32 and 39 of £0 6 million (2006 £3 0 million) was also charged to the statement of recognised income and expense

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

8. DIVIDENDS

Amounts recognised as distributions to equity holders in the year comprise

	2007 £m	2006 £m
Final dividend for the year ended 31 March 2006 (31 March 2005)	24 0	39 1
Interim dividend for the year ended 31 March 2007 (31 March 2006)	12 0	11 7
	36 0	50 8

The proposed final dividends for the year ended 31 March 2007 (£100 0 million) and 31 March 2006 are subject to approval by equity holders of the Company and, hence, have not been included as a liability in the financial statements at 31 March 2007 and 31 March 2006 respectively

The directors have recommended a final ordinary dividend for 2006/07 of £100 0 million which is not recognised as a liability at the balance sheet date

9. DIRECTORS AND THEIR INTERESTS

The aggregate emoluments of the directors in 2007 amounted to £534,401 (2006 £525,290) Emoluments comprise salaries, fees, taxable benefits and the value of short-term incentive awards The emoluments of T Weller and S G Batey are not included in the aggregate emoluments figures The emoluments of these two directors are disclosed in the accounts of United Utilities PLC The emoluments of the highest paid director (E Cooke) in 2007 in respect of services to the Company amounted to £171,561 (2006 E Cooke £188,899)

Seven long-term incentive awards vested in the year ended 31 March 2007 (2006 four) Information relating to long-term incentive awards is contained in the accounts of United Utilities PLC

With the exception of M J Boxall and G Dixon, all directors are members of, and contribute to, the United Utilities Pension Scheme, which is an exempt approved pension scheme with defined benefit and defined contribution sections of membership Only the defined contribution section is open to eligible employees The defined benefit section provides an entitlement on normal retirement of age 60 (or age 65 for some people) equal to between $1/30^{th}$ and $1/60^{th}$ of pensionable earnings for each completed year of service Early retirement is possible from the age of 50 if the Company agrees

M J Boxall and G Dixon are members of, and contribute to, the Electricity Supply Pension Scheme, a defined benefit scheme which provides on normal retirement at the age of 60 a pension equal to $1/80^{th}$ of pensionable earnings for each completed year of service (plus $3/80^{th}$ cash) Early retirement is possible from the age of 50 if the Company agrees

The earnings cap previously applying to directors under the Finance Act 1989 was removed as part of the "A-day" changes introduced by the Company as at 6 April 2006

The pension contributions for the highest paid director for 31 March 2007 (E Cooke) were £3,938 (2006 E Cooke £15,502) The accrued pension at 31 March 2007 for the highest paid director (E Cooke) was £33,065 (2006 E Cooke £25,474)

At 31 March 2007 and 2006, or date of appointment, the directors and their families had the following interests, all of which were beneficial interests, in the ordinary shares and options to subscribe for ordinary shares in United Utilities PLC The interests of S G Batey, C Cornish and T Weller in United Utilities PLC are disclosed in that company's accounts

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

9. DIRECTORS AND THEIR INTERESTS (continued)

	At 31 March 2007			At 31 March 2006		
	Ordinary shares	Executive option scheme options	Employee sharesave options	Ordinary shares	Executive option scheme options	Employee sharesave options
S Beaumont	-	-	-	10,758	27,258	2,909
M Beesley	7,534	578	-	6,769	578	465
M J Boxall	4,293	-	-	3,006	-	950
K M Budinger	-	-	-	1,213	-	-
E Cooke	4,553	3,758	-	2,465	3,758	1,751
A Cowan	2,963	13,906	-	-	-	-
G Dixon	-	-	-	8,637	5,585	2,609

During the year three directors exercised share options (2006 four)

Details of the employee sharesave scheme and the executive share option scheme operated by United Utilities PLC are given in that company's accounts

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

10. INTANGIBLE ASSETS

Group and Company	Software £m	Assets in course of construction £m	Total £m
Cost at 1 April 2005	14 6	15 9	30 5
Additions	6 3	-	6 3
Transfer	15 9	(15 9)	-
Disposals	(2 0)	-	(2 0)
At 31 March 2006	34 8	-	34 8
Amortisation at 1 April 2005	6 0	-	6 0
Charge for the year	2 7	-	2 7
Disposals	(2 0)	-	(2 0)
At 31 March 2006	6 7	-	6 7
Cost at 1 April 2006	34 8	-	34 8
Additions	(1 3)	0 9	(0 4)
Transfers	-	-	-
At 31 March 2007	33 5	0 9	34 4
Amortisation at 1 April 2006	6 7	-	6 7
Charge for the year	3 5	-	3 5
At 31 March 2007	10 2	-	10 2
Net book value at 31 March 2007	23 3	0 9	24 2
Net book value at 31 March 2006	28 1	-	28 1

At 31 March 2007, the Group had entered into contractual commitments for the acquisition of intangible assets amounting to £0 4 million (2006 £2 9 million)

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

11. PROPERTY, PLANT AND EQUIPMENT

Group and Company	Operational structures £m	Non operational land and buildings £m	Fixtures and equipment, vehicles and other £m	Assets in course of construction £m	Total £m
Cost or valuation at 1 April 2005	2,129 6	21 2	70 6	143 1	2,364 5
IFRS opening restatement	0 7	-	-	-	0 7
Additions	75 5	3 9	1 2	60 6	141 2
Transfers	57 0	-	4 1	(61 1)	-
Disposals	(4 3)	(2 0)	(20 2)	-	(26 5)
At 31 March 2006	2,258 5	23 1	55 7	142 6	2,479 9
Depreciation at 1 April 2005	680 3	4 1	53 4	-	737 8
Charge for the year	45 3	0 7	6 5	-	52 5
Disposals	(4 4)	(0 5)	(19 8)	-	(24 7)
At 31 March 2006	721 2	4 3	40 1	-	765 6
Cost or valuation at 1 April 2006	2,258 5	23 1	55 7	142 6	2,479 9
Additions	97 5	0 4	1 5	77 3	176 7
Transfers	79 5	-	-	(79 5)	-
Disposals	(3 2)	(0 1)	(3 9)	-	(7 2)
At 31 March 2007	2,432 3	23 4	53 3	140 4	2,649 4
Depreciation at 1 April 2006	721 2	4 3	40 1	-	765 6
Charge for the year	54 5	(0 2)	5 1	-	59 4
Disposals	(3 2)	(0 1)	(3 9)	-	(7 2)
At 31 March 2007	772 5	4 0	41 3	-	817 8
Net book value at 31 March 2007	1,659 8	19 4	12 0	140 4	1,831 6
Net book value at 31 March 2006	1,537 3	18 8	15 6	142 6	1,714 3

At 31 March 2007, had the property, plant and equipment other than investment property of the Group been carried at historical cost less accumulated depreciation and accumulated impairment losses, the carrying amount would have been approximately £1,657 8 million (2006 £1,533 9 million)

The revaluation surplus is disclosed in note 26 The revaluation surplus arose following a directors' revaluation of operational assets and non operational land and buildings in 1997

At 31 March 2007, the Group had entered into contractual commitments for the acquisition of property, plant and equipment amounting to £96 9 million (2006 £29 1 million)

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

12. INVESTMENT PROPERTY

Group and Company	Fair Value	Depreciation	Net Book Value
	£m	£m	£m
At 1 April 2005	11 0	-	11 0
Disposal	(5 3)	-	(5 3)
Depreciation	-	(0 3)	(0 3)
At 31 March 2006	5 7	(0 3)	5 4
Additions	0 3	-	0 3
Depreciation	-	(0 8)	(0 8)
Disposal	(6 0)	1 1	(4 9)
At 31 March 2007	-	-	-

The fair value of the Group's investment property at 1 April 2004 was arrived at following a valuation performed by property advisers Matthew and Goodman following International Valuation Standards

The property rental income earned by the Group from its investment property, all of which is leased out under operating leases, amounted to £0 2 million (2006 £0 9 million) Direct operating expenses arising on the investment property in the period amounted to nil (2006 nil)

13. OTHER INVESTMENTS

	Group £m	Company £m
Cost		
At 1 April 2005	2 0	65 0
Disposals	(1 0)	(29 3)
At 31 March 2006	1 0	35 7
Disposals (note 29)	(1 0)	(35 7)
At 31 March 2007	-	-

The Group disposal is shown in note 29

Details of the other investments at 31 March 2007 are as follows

<u>Company</u>

Subsidiary undertaking	Description of holding	Proportion held	Nature of business
NB Property and Estate Services No 1 Limited (formerly NB Property and Estate Services Limited)	Ordinary shares of £1 each	100%	Non-trading
NB Leasing Limited	Ordinary shares of £1 each	100%	Non-trading
NB (Miles Platting Community Project) Limited (formerly NB Miles Platting Limited)	Ordinary shares of £1 each	100%	Dormant

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

13. OTHER INVESTMENTS (continued)

<u>Group and Company</u>

Other investments	Description of holding	Proportion held	Nature of business
ESN Holdings Limited	Ordinary shares of £1 each	6 20%	Investment company
National Grid plc	Ordinary shares of 11 76p each	Negligible	Energy distribution

<u>Group and Company</u>

Associated undertaking	Description of holding	Proportion held	Nature of business
Nor Web Limited	Ordinary shares of £1 each	50%	Dormant

14. INVENTORIES

Group and Company	2007 £m	2006 £m
Raw materials and consumables	3 3	3 4

15. TRADE AND OTHER RECEIVABLES

	Group 2007 £m	Company 2007 £m	Group 2006 £m	Company 2006 £m
Trade receivables	12 3	12 0	14 5	14 5
Amounts owed by group undertakings	61 7	61 7	12 5	9 1
Prepayments and accrued income	32 8	32 8	27 4	27 2
	106 8	106 5	54 4	50 8

Trade receivables do not carry interest and are stated net of allowances for doubtful receivables of £0 8 million (2006 £0 6 million) estimated by management based on known specific circumstances, past default experience and their assessment of the current economic environment

The Group has no significant concentration of credit risk with exposure spread over a large number of customers The average credit period taken on sales is 13 8 days (2006 18 7 days)

The directors consider that the carrying amount of trade and other receivables approximates to their fair value

16. CASH AND CASH EQUIVALENTS

Group and company	2007 £m	2006 £m
Short-term bank deposits	258 4	137 0
Bank overdrafts (note 17)	(7 3)	(8 1)
	251 1	128 9

Cash and cash equivalents comprise cash at bank and other short-term highly liquid investments with a maturity of three months or less, net of bank overdrafts which are payable on demand

The effective interest rate on short term deposits was 4 89 per cent (2006 4 50 per cent) and these deposits had an average maturity of 42 days (2006 22 days)

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

17. BORROWINGS

This note provides information about the contractual terms of the Group's loans and borrowings For more information about the Group's exposure to interest rate risk see note 18

	2007	2006
Group and company	**£m**	£m
Non-current liabilities		
Bank and other term borrowings	**90.0**	90 1
Bonds	**642.6**	553 8
	732.6	643 9
Current liabilities		
Bank overdrafts	**7 3**	8 1
Amounts owed to parent undertaking	**0.4**	6 6
	7.7	14 7
	740.3	658 6

Borrowings for 2006 have been re-presented to include 'Amounts owed to parent undertakings' of £6 6 million which was previously included within the 'Trade and Other Payables' category on the balance sheet

Terms and debt repayment schedule

The principal economic terms and conditions of outstanding loans and borrowings were as follows

			2007	2006
Group and company	Currency	Year of maturity	**Carrying value**	Carrying value
			£m	£m
Borrowings designated at fair value through profit and loss				
8 875% 250m bond	GBP[2]	2026	**344.7**	358 9
Borrowings in cash flow hedge relationship				
EIB 90m (floating) loan – 5 6%	GBP[2]	2013	**90.0**	90 1
Borrowings measured at amortised cost				
8 875% 200m bond	GBP[2]	2026	**194.9**	194 9
1 4746%+RPI[1] 100m index-linked bond	GBP[2]	2046	**103.0**	-
Bank overdrafts	GBP[2]	2007	**7.3**	8 1
Amounts owed to parent undertaking	GBP[2]	2007	**0.4**	6 6
			740.3	658 6

[1] RPI - Retail Price Index – the UK general index of retail prices (for all items) as published by the Office of National Statistics (Jan 1987 = 0) as published by HM Government

[2] GBP - Pound Sterling

All loans and borrowings are unsecured Bank overdrafts are repayable on demand

The fair values of the Group's financial instruments are shown in note 18

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

17. BORROWINGS (continued)

Borrowing facilities

The Group and Company had available unutilised committed bank facilities of £50 0 million at 31 March 2007 (2006 £75 0 million) Of the amounts unutilised, £20 0 million expires within one year (2006 £30 0 million), £nil expires after one year but in less than two years (2006 £20 0 million), and £30 0 million expires in more than two years (2006 £25 0 million)

18. FINANCIAL INSTRUMENTS

Exposure to credit and interest rate risks arise in the normal course of the Group's business Derivatives are used to hedge exposure to fluctuations in interest rates

Risk management

The primary financial risk faced by the Group is interest rate risk The board has reviewed and agreed policies for managing this risk, as summarised below The board has also approved all of the classes of financial instruments used by the group The United Utilities PLC's treasury function, which is authorised to conduct the day-to-day treasury activities of the Group, reports at least annually to the board The use of financial derivatives is governed by the Group's policies approved by the board, which provide written principles on the use of financial derivatives

All of the Group's activities involve analysis, acceptance and management of some degree of risk or combination of risks The most important types of financial risk are credit risk, liquidity risk and market risk Market risk includes foreign exchange, interest rate and equity price risks

The Group's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls and to monitor the risks and limits continually by means of reliable and up to date systems The Group modifies and enhances its risk management policies and systems to reflect changes in markets and products The United Utilities PLC Audit Committee, under authority delegated by the board, formulates high level Group risk management policy, monitors risk and receives reports that allow it to review the effectiveness of the Group's risk management policies

Credit risk

Credit risk is the risk that financial loss arises from the failure of a customer or counterparty to meet its obligations under a contract It arises principally from lending, trade finance, treasury and leasing activities The Group has dedicated standards, policies and procedures to control and monitor all such risks.

The counterparties under these activities consist of financial institutions and other bodies with good credit ratings Although the Group is potentially exposed to credit loss in the event of non-performance by counterparties, such credit risk is controlled through credit rating reviews of the counterparties and by limiting the total amount of exposure to any one party Management does not anticipate any counterparty will fail to meet is obligations

The directors do not believe that the Group is exposed to any material concentrations of credit risk The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivatives, in the balance sheet

Liquidity risk

Liquidity risk is the risk that the Group will not have sufficient funds to meet the obligations or commitments associated with its financial instruments The Group maintains a strong liquidity position and manages the liquidity profile of its assets, liabilities and commitments so that cashflows are appropriately balanced and all funding obligations are met when due

The cashflow hedge relates to the management of cashflow on a particular floating rate loan over the regulatory period to 2010 The group largely manages all of its financing cashflows over the observed five-year regulatory period, however, the majority of these economic hedges do not qualify for hedge accounting as they would be overlaid onto transactions which are already within fair value hedge relationships

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

18. FINANCIAL INSTRUMENTS (continued)

Market rısk
Market rısk ıs the rısk that movements ın market rates, ıncludıng foreıgn exchange rates, ınterest rates, equıty and commodıty prıces wıll reduce the Group's ıncome on the value of ıts portfolıos The management of market rısk ıs undertaken usıng rısk lımıts approved by the finance dırector under delegated authorıty

The Group borrows ın the major global debt markets at both fixed and floatıng rates of ınterest, usıng derıvatıves, where approprıate, to generate the desıred effectıve ınterest basıs

The Group uses a varıety of financıal ınstruments, ıncludıng derıvatıves, when raısıng finance for ıts operatıons ın order to manage any exposure arısıng from fundıng actıvıty

Interest rate rısk

The Group's fixed rate borrowıngs are exposed to a rısk of change ın theır faır value due to changes ın ınterest rates The Group's floatıng rate borrowıngs are exposed to a rısk of change ın cashflows due to changes ın ınterest rates Investments ın equıty securıtıes and short-term receıvables and payables are not exposed to ınterest rate rısk

The Group uses ınterest rate swap contracts and financıal futures to hedge these exposures

Under an ınterest rate swap, the Group agrees wıth another party to exchange at specıfic ıntervals the dıfference between fixed rate and floatıng rate ınterest amounts calculated by reference to an agreed notıonal prıncıpal amount The notıonal prıncıpal of these ınstruments reflects the extent of the Group's ınvolvement ın the ınstruments, but does not represent ıts exposure to credıt rısk, whıch ıs assessed by reference to the faır value

Non-current asset ınvestments, trade and other receıvables, and trade and other payables are not dırectly exposed to ınterest rate rısk

Currency rısk

The Group makes no sıgnıficant sales or purchases ın currencıes other than ıts functıonal currency Accordıngly, the Group has no materıal unhedged foreıgn currency exposures

Hedging
The Group does not use derıvatıve financıal ınstruments for speculatıve purposes, and has not pledged collateral ın relatıon to any of ıts derıvatıve ınstruments The derıvatıve financıal ınstruments do not contaın any early settlement or termınatıon optıons

Those derıvatıve ınstruments that are not part of a desıgnated and effectıve hedgıng relatıonshıp are classıfied as held for tradıng and are therefore measured at faır value through profit and loss Where faır value hedges occur these hedges are managıng ınterest rate rısk ın relatıon to financıng

The derıvatıve financıal ınstruments utılısed by the Group to achıeve the hedgıng of these exposures can be summarısed as follows

Interest rate swaps

Interest rate swaps are used to manage floatıng rate borrowıngs ın order to reduce the financıal rısk to the Group from potentıal future changes ın medıum-term ınterest rates

Interest rate swaps mature between 2010 and 2026 Swaps are executed ın conjunctıon wıth bond ıssues to ensure that the combıned cashflows approxımate to floatıng sterlıng In these cases, ınterest on the swap ıs receıved to coıncıde wıth bond ınterest payments whıch are generally annual on fixed rate bonds Interest receıved on these swaps wıll match the nomınal ınterest paıd on the bonds, these rates are detaıled ın the borrowıngs note 17 'Terms and debt repayment schedule' The floatıng sterlıng sıde payable on these swaps wıll generally occur semı-annually Takıng ınto account the latest fixıngs prıor to year end, rates range from 5 73 to 7 30 per cent on these floatıng legs Addıtıonally, swaps are executed to fix floatıng rate cashflows over the regulatory perıod Cashflows on these regulatory swaps wıll coıncıde wıth the floatıng cashflow they

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

18. FINANCIAL INSTRUMENTS (continued)

are intended to fix Interest received on these regulatory swaps is floating sterling and the fixed payable side ranges from 4 81 to 5 37 per cent

Financial futures

Financial futures are used to manage the Group's exposure to possible future changes in short-term interest rates The financial future contracts are traded on the London International Financial Futures and Options Exchange

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

18. FINANCIAL INSTRUMENTS (continued)

Effective interest rates and repricing analysis

In respect of interest bearing financial liabilities, the following tables indicate their average effective interest rates at the reporting date and the periods in which they mature or, if earlier, reprice

Group and Company – 31 March 2007	**Average effective interest rate**	**Total**	**1 year or less**	**1-2 years**	**2-3 years**	**3-4 years**	**4-5 years**	**More than 5 years**
	%	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Borrowings designated at fair value through profit and loss								
Fixed rate instruments:								
8 875% GBP 250m bond due 2026	5 87	344 7	-	-	-	-	-	344 7
Effect of swaps	0 79	-	344 7	-	-	-	-	(344 7)
Total after effect of swaps[1]	6 66	344 7	344 7	-	-	-	-	-
Borrowings in cashflow hedge relationship								
Floating rate instruments:								
EIB GBP 90m loan due 2013	5 60	90 0	90 0	-	-	-	-	-
Effect of swaps	(0 78)	-	(90 0)	-	90 0	-	-	-
Total after effect of swaps[1]	4 82	90 0	-	-	90 0	-	-	-
Borrowings measured at amortised cost								
Fixed rate instruments:								
8 875% GBP 200m bond due 2026	9 16	194 9	-	-	-	-	-	194 9
Floating rate instruments								
Bank overdraft[2]	Various	7 3	7 3	-	-	-	-	-
Amounts owed to parent undertaking	LIBOR[3] +0 5%	0 4	0 4	-	-	-	-	-
		7 7	7 7	-	-	-	-	-
Index-linked instruments								
1 4746% GBP 100m index-linked bond due 2046	1 4746% +RPI	103 0	103 0	-	-	-	-	-
Effect of fixed hedge for the term of the regulatory business plan[1]	4 98	-	(340 0)	-	265 0	75 0	-	-
		740 3	115 4	-	355 0	75 0	-	194 9

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

18. FINANCIAL INSTRUMENTS (continued)

Effective interest rates and repricing analysis

The debt balance on the 1 4746% GBP 100m index-linked bond, and thus the balance upon which interest is paid at the quoted coupon, is adjusted for movements in the Retail Price Index established at the trade date The corresponding annualised inflation rate for the year to 31 March 2007 was 4 8 per cent (31 March 2006 2 4 per cent)

Group and Company - 31 March 2006	Average effective interest rate	Total	1 year or less	1-2 years	2-3 years	3-4 years	4-5 years	More than 5 years
	%	£m	£m	£m	£m	£m	£m	£m
Borrowings designated at fair value through profit and loss								
Fixed rate instruments								
8 875% GBP 250m bond due 2026	5 87	358 9	-	-	-	-	-	358 9
Effect of swaps	(0 17)	-	358 9	-	-	-	-	(358 9)
Total after effect of swaps[1]	5 70	358 9	358 9	-	-	-	-	-
Borrowings in cashflow hedge relationship								
Floating rate instruments								
EIB GBP 90m loan due 2013	4 65	90 1	90 1	-	-	-	-	-
Effect of swaps	0 17	-	(90 1)	-	-	90 1	-	-
Total after effect of swaps[1]	4 82	90 1	-	-	-	90 1	-	-
Borrowings measured at amortised cost								
Fixed rate instruments								
8 875% GBP 200m bond due 2026	9 16	194 9	-	-	-	-	-	194 9
Floating rate instruments								
Bank overdraft[2]	Various	8 1	8 1	-	-	-	-	-
Amounts owed to parent undertaking	LIBOR[3] + 0 5%	6 6	6 6	-	-	-	-	-
		14 7	14 7	-	-	-	-	-
Effect of fixed hedge for the term of the regulatory business plan[1]	4 98	-	(340 0)	-	-	265 0	75 0	-
		658 6	33 6	-	-	355 1	75 0	194 9

[1] The rate quoted is the last GBP LIBOR fixing plus any margin which is payable under the relevant swap The interest receivable on these swaps will be on the coupon due on the corresponding debt item

[2] This represents a number of bank balances with various floating rates

[3] LIBOR – London Inter-Bank Offered Rate

Where a floating rate is quoted, the latest fixing is quoted including any appropriate margins

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

18. FINANCIAL INSTRUMENTS (continued)

Sensitivity analysis

In managing interest rate risk the Group aims to reduce the impact of short-term fluctuations on its earnings Over the longer term, permanent changes in interest rates will have an impact on profit

The analysis in the table below illustrates the sensitivity of the market value (fair value) of the Group's financial instruments to changes in interest rates The analysis assumes a general increase or decrease of one percentage point in interest rates for all maturities and currencies from their levels at 31 March with all other variances held constant

	Fair value 31 March 2007	+1% movement in interest rate	-1% movement in interest rate
Group and Company			
Interest rate movement	**£m**	**£m**	**£m**
Non-current borrowings	(801 0)	83 5	(102 4)
Derivatives	(0 2)	(25 9)	31 3
Cash and cash equivalents	259 5	(0 3)	0 3

	Fair value 31 March 2006	+1% movement in interest rate	-1% movement in interest rate
Interest rate movement	**£m**	**£m**	**£m**
Non-current borrowings	(760 0)	78 0	(91 4)
Derivatives	11 1	(27 9)	34 6
Cash and cash equivalents	137 0	-	-

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

18. FINANCIAL INSTRUMENTS (continued)

Fair values

The fair values of financial assets and liabilities, together with the carrying amounts shown in the balance sheet, are as follows

Group and company	2007 Carrying value	2007 Fair value	2006 Carrying value	2006 Fair value
	£m	£m	£m	£m
Financial assets:				
Non-current assets:				
Derivative financial instruments - cashflow hedge swaps[1]	2 1	2 1	-	-
Current assets:				
Cash and cash equivalents[2]	258 4	259 5	137 0	137 0
Derivative financial instruments - held for trading swaps	4 4	4 4	13 0	13 0

[1] During the year a gain on the fair value movement of the cashflow hedge derivative of £2 1 million (2006 loss £0 7 million) was recognised and taken to reserves, gross of tax

[2] The fair value of cash and cash equivalents includes £1 1 million of interest receivable The interest receivable is included within trade and other receivables

The carrying value of trade and other receivables approximates to their fair value for both the Group and Company

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

18. FINANCIAL INSTRUMENTS (contınued)

Fair values (continued)

Group and Company	2007 Carryıng value	2007 Fair value	2006 Carryıng value	2006 Faır value
	£m	£m	£m	£m
Financial liabılitıes:				
Non-current liabılities				
Borrowıngs desıgnated at faır value through profit and loss [1]	(344 7)	(344 7)	(358 9)	(358 9)
Borrowıngs ın cash flow hedge relatıonshıp [1]	(90 0)	(90 4)	(90 1)	(90 0)
Borrowıngs measured at amortısed cost [1]	(297 9)	(365 9)	(194 9)	(311 1)
	(732 6)	(801 0)	(643 9)	(760 0)
Current liabilities:				
Borrowıngs - bank overdrafts	(7 3)	(7 3)	(8 1)	(8 1)
Borrowıngs - amounts owed to parent undertakıng	(0 4)	(0 4)	(6 6)	(6 6)
	(7 7)	(7 7)	(14 7)	(14 7)
Derıvatıve financıal ınstruments - held for tradıng swaps	(6 7)	(6 7)	(1 9)	(1 9)

[1] The total faır value of non-current borrowıngs ıncludes £1 3 mıllıon of ınterest payable The ınterest payable ıs ıncluded wıthın trade and other payables

Of the £14 2 mıllıon gaın (2006 £17 8 mıllıon loss) ın faır value of financıal lıabılıtıes desıgnated at faır value through profit and loss, a loss of £8 4 mıllıon (2006 £4 3 mıllıon gaın) ıs attrıbutable to changes ın credıt rısk

The carryıng value of trade and other payables approxımates to theır faır value for both the Group and Company

19. TRADE AND OTHER PAYABLES

	Group 2007 £m	Company 2007 £m	Group 2006 £m	Company 2006 £m
Trade credıtors	8 0	8 0	8 0	7 9
Amounts owed to group undertakıngs	57 6	56 7	24 2	24 3
Amounts owed to subsıdıary undertakıngs	-	-	-	47 7
Other taxatıon and socıal securıty	5 5	5 5	4 4	4 4
Other credıtors	-	-	6 4	6 4
Consumers' contrıbutıons	14 2	14 2	6 8	6 8
Refundable customer deposıts	8 7	8 7	19 1	19 1
Accruals and deferred ıncome	58 3	58 3	43 8	43 9
	152 3	151 4	112 7	160 5

Trade credıtors prıncıpally comprıse amounts outstandıng for trade purchases and ongoıng costs The average credıt perıod taken for trade purchases ıs 41 days (2006 43 days) The prıor year amounts owed to group undertakıngs has been restated by £6 6m to reflect the treatment of ıntercompany debt Thıs has been reflected ın note 18

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

19. TRADE AND OTHER PAYABLES (continued)

Trade and Other Payables for 2006 have been re-presented to exclude 'Amounts owed to parent undertakings' of £6 6 million which is now included within the Borrowings category on the balance sheet

20. RETIREMENT BENEFIT SCHEMES

Group and Company

The Group participates in a number of pension schemes principally in the UK The major schemes are funded defined benefit schemes – the United Utilities Pension Scheme (UUPS) and the United Utilities Group of Electricity Supply Pension Scheme (ESPS) (the 'Schemes') Both defined benefit Schemes are closed to new employees UUPS also includes a defined contribution section which constitutes less than 0 5 per cent of the total asset value The assets of these Schemes are held in trust funds independent of Group finances

The last actuarial valuations of the Schemes were carried out as at 31 March 2006 These valuations have been updated to take account of the requirements of IAS 19 'Employee Benefits' in order to assess the position at 31 March 2007 by projecting forward from 31 March 2006, and have been performed by an independent actuary, Mercer Human Resource Consulting

On 31 March 2005, the Group made lump sum payments of £8 6 million and £71 0 million to UUPS and ESPS respectively The payments were in lieu of the estimated Company contributions that would have been payable for defined benefit members over the five years from 1 April 2005 Subject to the results of the actuarial valuations at 31 March 2007, Company contributions are expected to resume from 1 April 2010 In the meantime, the Group will continue to pay contributions in respect of the defined contribution members and insurance premiums Other payments will be made by the Group in accordance with the funding agreement between the Trustee and the Group

The total defined benefit pension income for the year was £1 4 million (2006 pension cost £2 9 million) A pension surplus of £24 5 million is included in the balance sheet at 31 March 2007 (2006 obligation of £1 8 million) Information about the pension arrangements for executive directors is contained in note 9

The main financial assumptions used by the actuary were as follows

	At 31 March 2007	**At 31 March 2006**
Discount rate – UUPS	5 20%	4 90%
Discount rate - ESPS	5 30%	4 90%
Expected return on assets –UUPS	6 50%	6 20%
Expected return on assets – ESPS	6 30%	5 90%
Pensionable salary growth - UUPS	3 95%	3 75%
Pensionable salary growth - ESPS	4 00%	3 80%
Pension increases	3 00%	2 80%
Price inflation	3 00%	2 80%

The current life expectancies (in years) underlying the value of the accrued liabilities for the Schemes are

	At 31 March 2007	**At 31 March 2006**
Male life expectancy at age 60		
Retired member	23 8	22 5
Non-retired member	25 9	24 8

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

20. RETIREMENT BENEFIT SCHEMES (continued)

Recent studies have shown faster rates of life expectancy improvement than had previously been expected An allowance has been made for these faster rates of improvements Studies have also illustrated that mortality rates vary significantly with the location of employees and the nature of their work These factors have been taken into account in the calculation of the defined benefit obligations of the company

As at 31 March 2007, the Group's share of the fair value of Schemes assets, together with the liabilities in the Schemes recognised in the balance sheet were as follows

	Scheme assets at 31 March 2007 %	Value at 31 March 2007 £m	Scheme assets at 31 March 2006 %	Value at 31 March 2006 £m
Equities	58 4	496 6	66 6	493 9
Gilts	26 1	222 4	22 3	165 2
Bonds	14 5	123 1	11 0	81 5
Property	-	-	0 1	0 7
Cash	1 0	8 5	-	-
Total fair value of assets	100 0	850 6	100 0	741 3
Present value of liabilities		(826 1)		(743 1)
Net retirement benefit surplus / (obligations)		24 5		(1 8)

To develop the expected long-term rate of return on assets assumption, the Group considered the level of expected returns on risk-free investments, the historical level of the risk premium associated with the other asset class in which the portfolio is invested and the expectations for future returns of each asset class The expected return for each asset class was then weighted based on the actual asset allocation to develop the expected long-term return on assets assumption for the portfolio The actual return on Scheme assets for the Schemes was £17 4 million (2006 £147 8 million)

Movements in the present value of the defined benefit obligations are as follows

	2007 £m	2006 £m
At 1 April	(743 1)	(666 3)
Current service cost	(7 6)	(7 5)
Interest cost on scheme obligations	(35 6)	(31 3)
Member contributions	(1 9)	(2 0)
Past service credit/(cost)	2 1	(0 3)
Actuarial losses	(86 1)	(76 0)
Benefits paid	46 1	40 3
At 31 March	(826 1)	(743 1)

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

20. RETIREMENT BENEFIT SCHEMES (continued)

Movements in the fair value of the Scheme assets were as follows

	2007 £m	2006 £m
At 1 April	741 3	631 3
Expected return on scheme assets	42 5	36 2
Actuarial gains	110 9	111 6
Company contributions	0 1	0 5
Member contributions	1 9	2 0
Benefits paid	(46 1)	(40 3)
At 31 March	850 6	741 3

The net pension income/(expense) before taxation recognised in the income statement in respect of the defined benefit Schemes is summarised as follows

	2007 £m	2006 £m
Current service cost	(7 6)	(7 5)
Past service credit/(cost)	2 1	(0 3)
Expected return on scheme assets	42 5	36 2
Interest on scheme obligations	(35 6)	(31 3)
Net pension income/(expense) before taxation	1 4	(2 9)

The above amounts are recognised in arriving at operating profit except for expected return on scheme assets and interest on scheme obligations which have been recognised within investment income

The reconciliation of the opening and closing balance sheet position is as follows

	2007 £m	2006 £m
At 1 April	(1 8)	(35 0)
Income/(expenses) recognised in the income statement	1 4	(2 9)
Contributions paid	0 1	0 5
Net actuarial gains gross of taxation	24 8	35 6
	24 5	(1 8)

Actuarial gains and losses are recognised directly in the statement of recognised income and expense At 31 March 2007, a cumulative gain of £54 7 million (2006 £29 9 million) had been recorded directly in the statement of recognised income and expense

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

20. RETIREMENT BENEFIT SCHEMES (continued)

The history of the Schemes for the current and prior years is as follows

	2007 £m	2006 £m	2005 £m
Present value of defined benefit obligation	(826 1)	(743 1)	(666 3)
Fair value of scheme assets	850 6	741 3	631 3
Net retirement benefit surplus/(obligation)	24 5	(1 8)	(35 0)
Experience adjustments on scheme liabilities	38 6	-	(8 1)
Experience adjustments on scheme assets	(25 1)	111 6	25 6

21. DEFERRED TAX

The following are the major deferred tax liabilities and assets recognised by the Group and Company, and the movements thereon, during the current and prior reporting periods

Group and Company	Accelerated tax depreciation £m	Retirement benefit obligations £m	Other £m	Total £m
At 1 April 2005	341 4	(10 5)	(40 7)	290 2
Charged to the income statement	(6 9)	(0 9)	9 3	1 5
Charged to equity for the year	-	10 7	3 0	13 7
At 31 March 2006	334 5	(0 7)	(28 4)	305 4
Charged to the income statement	(2 6)	0 3	13 7	11 4
Charged to equity for the year	-	7 6	0 6	8 2
At 31 March 2007	331 9	7 2	(14 1)	325 0

The 2007 Chancellor's Budget proposed various changes to the rules for claiming tax allowances on capital expenditure together with a reduction in the main corporate tax rate The impact of these changes on the Group and Company's future deferred tax position is currently under review

22. PROVISIONS

Group and Company	Restructuring Provision £m	Other £m	Total £m
At 1 April 2006	0 8	0 5	1 3
Released to the income statement	(0 6)	(0 3)	(0 9)
Utilisation of provision	(0 2)	(0 2)	(0 4)
At 31 March 2007	-	-	-

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

23. CONSUMER CONTRIBUTIONS

Consumer contributions are amounts received from a customer in respect of the provision of a new connection to the network

Consumer contributions are amortised through the income statement over the lifetime of the relevant asset

Group and Company

	£m
At 1 April 2005	228 0
Additions during the year	31 3
Amortisation	(6 6)
At 31 March 2006	252 7
Additions during the year	70 2
Amortisation	(8 2)
At 31 March 2007	314 7
Amounts due in less than one year (see note 19)	14 2
Amounts due after more than one year	300 5
	314 7

24. REFUNDABLE CUSTOMER DEPOSITS

Refundable customer deposits are those consumer contributions which may be in part refundable, dependent on contracted targets

Group and Company	2007 £m	2006 £m
Amounts due in less than one year (see note 19)	8 7	19 1
Amounts due after more than one year	10 6	6 1

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

25. SHARE CAPITAL

	2007 £	2006 £
Authorised:		
569,999,996 (2006 569,999,996) ordinary shares of 50 pence each	284,999,998	284,999,998
4 'A' ordinary shares of 50 pence each	2	2
Special rights redeemable preference share of £1	1	1
	285,000,001	285,000,001

	2007 £	2006 £
Allotted, called up and fully paid:		
476,821,341 (2006 476,821,341) ordinary shares of 50 pence each	238,410,671	238,410,671
4 'A' ordinary shares of 50 pence each	2	2
	238,410,673	238,410,673

The 'A' ordinary shares and the ordinary shares rank pari passu in all respects, save that dividends may be declared on one class of shares without being declared on the other

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

26. SHAREHOLDERS' EQUITY

Group

	Called up share capital £m	Share premium account £m	Revaluation reserve £m	Capital redemption reserve £m	Retained earnings £m	Total £m
At 1 April 2005	78 4	4 4	129 0	8 6	155 4	375 8
Profit for the year	-	-	-	-	77 3	77 3
Dividends	-	-	-	-	(50 8)	(50 8)
Fair value loss on cashflow hedges	-	-	-	-	(0 7)	(0 7)
Transfer from revaluation reserve	-	-	(2 0)	-	2 0	-
Post employment benefits actuarial gains on defined benefit schemes	-	-	-	-	25 0	25 0
New share capital issued	160 0	-	-	-	-	160 0
At 31 March 2006	238 4	4 4	127 0	8 6	208 2	586 6
Profit for the year	-	-	-	-	112 3	112 3
Dividends	-	-	-	-	(36 0)	(36 0)
Post tax fair value gain on cashflow hedges	-	-	-	-	1 5	1 5
Transfer from revaluation Reserve	-	-	(4 6)	-	4 6	-
Post employment benefits Post tax actuarial gains on defined benefit schemes	-	-	-	-	17 3	17 3
At 31 March 2007	238 4	4 4	122 4	8 6	307 9	681 7

As allowed by section 230(4) of the Companies Act 1985, the Company has not presented its own income statement The amount of Group profit after tax for the financial year dealt with in the Company's income statement is £126 6 million (2006 £78 3 million)

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

26. SHAREHOLDERS' EQUITY (continued)

Company

	Called up share capital £m	Share premium account £m	Revaluation reserve £m	Capital redemption reserve £m	Retained earnings £m	Total £m
At 1 April 2005	78 4	4 4	129 0	8 6	140 7	361 1
Profit for the year	-	-	-	-	78 3	78 3
Dividends	-	-	-	-	(50 8)	(50 8)
Fair value loss on cashflow hedges	-	-	-	-	(0 7)	(0 7)
Transfer from revaluation reserve	-	-	(2 0)	-	2 0	-
Post employment benefits actuarial gains on defined benefit schemes	-	-	-	-	25 0	25 0
New share capital issued	160 0	-	-	-	-	160 0
At 31 March 2006	238 4	4 4	127 0	8 6	194 5	572 9
Profit for the year	-	-			126 6	126 6
Dividends	-	-	-	-	(36 0)	(36 0)
Post tax fair value gain on cashflow hedges	-	-	-	-	1 5	1 5
Transfer from revaluation Reserve	-	-	(4 6)	-	4 6	-
Post employment benefits post tax actuarial gains on defined benefit schemes	-	-	-	-	17 3	17 3
At 31 March 2007	238 4	4 4	122 4	8 6	308 5	682 3

27. OPERATING LEASES

The Group and Company are committed to making the following payments over the lifetime of the lease in respect of non-cancellable operating leases which expire in

	Land and buildings 2007 £m	Plant and machinery 2007 £m	Land and buildings 2006 £m	Plant and machinery 2006 £m
Within one year	1 1	0 2	0 6	0 5
In the second to fifth years inclusive	4 2	0 6	2 1	0 6
After five years	6 3	2 3	3 1	0 1
	11 6	3 1	5 8	1 2

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

28. RELATED PARTY TRANSACTIONS

Group and Company

The Group receives and pays interest and recharges to other businesses in United Utilities PLC, which are related parties, in the normal course of business Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note Transactions between the United Utilities Electricity PLC Group and other parts of United Utilities PLC were as follows

	2007 £m	2006 £m
Interest paid	0 6	1 5
Recharges to group companies	13 3	13 9
Recharges from group companies	59 3	91 6

Amounts outstanding at 31 March 2007 and 2006 between the United Utilities Electricity PLC Group and other companies within United Utilities PLC are provided in notes 15 and 19

The following transactions were carried out with other related parties

	Sale of goods £m	Purchase of goods £m	Amounts owed by related parties £m	Amounts owed to related parties £m
Associates of parent company	1 2	1 2	0 8	-

Sale of goods to related parties were on the Group's normal trading terms

29. DISPOSAL OF SUBSIDIARY

As referred to in note 13, on 30 March 2007 the Group disposed of its interest in NB Generation Limited

The unaudited net assets of NB Generation Limited at the date of disposal and Group gain on disposal were as follows

	2007 £m
Investments	1 0
Trade receivables	4 4
Current tax liability	(3 0)
Amounts owed from parent	47 6
	50 0
Gain on disposal	-
Total consideration	50 0
Satisfied by	
Increase in amount owed by group undertakings	(50 0)
	(50 0)

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

29. DISPOSAL OF SUBSIDIARY (continued)

On 13 September 2005 the Group disposed of its interest in UU Investments (No 2) Limited

The unaudited net assets of UU Investments (No 2) Limited at the date of disposal and Group gain on disposal were as follows

	2006 £m
Investments	1 0
Trade receivables	49 2
Current tax liability	(11 8)
Amounts owed to parent	(9 1)
	29 3
Gain on disposal	0 3
Total consideration	29 6
Satisfied by	
Cash	29 6
	29 6
Net cash inflow arising on disposal	
Cash consideration	29 6
	29 6

30. ULTIMATE PARENT UNDERTAKING AND CONTROLLING PARTY

The accounts of the Company and the Group are consolidated in the group accounts of the ultimate parent undertaking and ultimate controlling entity United Utilities PLC, a company registered in England and Wales Copies of the accounts of United Utilities PLC may be obtained from the Company Secretary, United Utilities PLC, Haweswater House, Lingley Mere Business Park, Lingley Green Avenue, Great Sankey, Warrington, WA5 3LP The immediate parent of the Company is United Utilities North West PLC

NOTES TO THE ACCOUNTS
For the year ended 31 March 2007

31. CASH GENERATED FROM OPERATIONS

Cash generated from operations	Group 2007 £m	Company 2007 £m	Group 2006 £m	Company 2006 £m
Profit before taxation	144 9	159 2	103 0	104 0
Adjustment for investment income and finance expense	31 2	16 9	45 2	44 2
Operating profit	176 1	176 1	148 2	148 2
Adjustments for				
Depreciation of property, plant and equipment	59 4	59 4	52 5	52 5
Depreciation of investment properties	0 8	0 8	0 3	0 3
Amortisation of intangible assets	3 5	3 5	2 7	2 7
Amortisation of customer contributions	(8 2)	(8 2)	(6 6)	(6 6)
Profit on disposal of subsidiary	-	-	(0 3)	(0 1)
Profit on disposal of investment property	(1 1)	(1 1)	(0 5)	(0 5)
Profit on disposal of property, plant and equipment	(1 3)	(1 3)	(1 5)	(1 5)
Restructuring credit	(0 6)	(0 6)	(0 6)	(0 6)
Changes in working capital				
Decrease in inventories	0 1	0 1	0 2	0 2
Increase in trade and other receivables	(4 5)	(4 5)	(13 8)	(14 9)
Decrease in provisions and payables	(11 5)	(11 5)	(55 4)	(20 3)
Cash generated from continuing operations	212 7	212 7	125 2	159 4

32. EVENTS AFTER THE BALANCE SHEET DATE

On 4 June 2007, the United Utilities PLC board took the decision to initiate a sale process for United Utilities Electricity PLC's distribution assets United Utilities PLC intends to retain a contract for the operation of those electricity distribution assets