



Dŵr Cymru
Welsh Water

June Return '07 **Overview**



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Summary

for the year

This report provides an overview of our performance in the year to 31 March 2007 and accompanies our annual June Return. It covers levels of service and outputs for our water and sewerage activities, environmental performance, financial performance and overall progress against targets established at the last price review in 2004.

Protecting public health

- Compliance with drinking water quality standards 'at the tap' as measured by the Operational Performance Index (OPI (TIM)) was 99.70% compared to 99.74% last year.
- 100% compliance with coliform standard at Water Treatment Works (WWTs), our best ever performance.
- Participation in the Public Health Partnership for Wales, a joint venture between ourselves and key stakeholders.
- Completion of an initial 22 drinking water plans for catchments and treatments.

Protecting the environment

- 99% of EEC designated beaches achieved the mandatory standards.
- 89% of EEC designated beaches achieved the higher guideline standards leading to 49 Blue Flag beaches/marina awards.
- Compliance with environmental quality standards (numeric consents) at Wastewater Treatment Works (WwTWs) was 97.60%, up from 96.49% last year
- The number of 'category 1 & 2' sewage related pollution incidents was 17, the same as last year.
- Leakage targets were achieved and reduced from 224MI/d last year to 209MI/d this year; we now abstract for public water supply some 25% less than 10 years ago.

Customer service delivery

- Properties at risk of low pressure (DG2) remained at 221 or 0.02% of connected properties.
- Unplanned interruptions to supply (DG3) was 0.03% down from 0.04% last year.
- Properties at risk of flooding (DG5) decreased from 514 last year to 484 this year.
- DG7 - A 39% reduction in stage 2 complaints.
- A good performance on telephone response times (DG9) and a score of 4.57 out of a maximum of 5 on the telephone handling satisfaction measure.

Overall performance assessment

- Our estimate for OPA this year is 393 points (2006: 406 points).
- The major loss of OPA points this year can be attributable to two main areas namely sewer flooding (other causes) 4.79 points down and category 1 & 2 pollution incidents with 6.44 points lost.

Customer benefits

- Customer dividend increased this year to £20, up from £19 in 2006.
- A significant improvement programme of IT Enabled Change (ITEC) has commenced, aimed at improving service to our customers.
- Creation of a dedicated centre for managing operational contact, known as the Operational Activity Centre (OAC).
- Preparation of our Strategic Direction Statement giving a long term view on what we are proposing to deliver for the benefit of customers and the environment.
- Development of Floodcare Packs which have improved the channels of communication with those customers who experience sewage flooding.
- The S19 programme has been reduced to reflect the amount of iron mains that require rehabilitation. We are in discussion with DWI to agree a revised undertaking.
- The cost of delivering the S19 programme is in excess of the FD mainly because of the increased proportion of large diameter mains and logistical difficulties, especially when working in urban areas.
- In the last year, the DG5 sewer flooding programme has been prioritised to ensure we get the best value of spend for our customers. Outputs and spend are below the FD. This will be redressed in years 3 and 4.
- There is concern going forward around recruiting and retaining staff as the construction industry 'hots up'. Indeed, some of our partners are experiencing staff turnover in excess of 20%.

Financial performance

- Glas Cymru's financial reserves (RCV less debt) of £876m is up from £683m in 2006.
- Glas Cymru's Financial Gearing reduced to 74%, down from 93% in May 2001.
- Profit before tax of £66m (2006: £63m) to be retained for the benefit of customers.
- Finance substantially in place to 2010 to fund the capital programme.
- Higher operating costs largely due to increased power costs (£34m in the report year against £17m 2 years ago).
- Increases in the cost of delivering the capital programme have been seen across all areas, and in particular the unit cost of delivering the WTW, Section 19 and DG5 investments are in excess of the FD.
- We are planning to invest some £600m over the next 2 years, challenging targets when compared to historical spend levels. This will bring expenditure broadly back in-line with the FD profile.
- Our goal is to achieve efficiency savings in the delivery of the programme by absorbing the difference between COPI and RPI inflation. However, we are facing significant upward cost pressures, particularly in the water programme, and it is likely that we will only partly achieve our efficiency savings goal.

AMP4 Investment Programme

- Our overall capital expenditure is behind the Final Determination (FD), but with the exception of the S19 mains rehabilitation and the DG5 sewer flooding programme, outputs are broadly in line with the determination when the change protocol with the Environment Agency (EA) and Drinking Water Inspectorate (DWI) undertakings are taken into account.

Performance

against the Monitoring Plan

In our Monitoring Plan, published in April 2005, we set out our commitments on the work to be done. This Overview provides a summary of our progress against this Plan

Water Service				
Performance Measure	Units	The Monitoring Plan Target	Previous Performance 2005-06	Actual Performance 2006-07
DG2 Properties below reference level for low pressure	No.	242	221	221
DG2 Properties at risk of receiving low pressure	%	0.02	0.02	0.02
DG3 Overall performance score (interruption to supply)	No.	0.08	0.04	0.03
DG4 Restrictions on water supply	No.	0	0	0
Burst mains per 1,000km of main	No.	194	171	167
Distribution input not covered by S19 undertakings	%	64.10	62.00	64.40
Water quality mean zonal compliance	%	-	99.95	99.95
Iron compliance 'at the tap'	%	98.90	99.16	99.10
Operational Performance Index (OPI)	%	-	99.82	99.77
Operational Performance Index (TIM)	%	-	99.74	99.70
Customer Service				
Performance Measure	Units	The Monitoring Plan Target	Previous Performance 2005-06	Actual Performance 2006-07
DG6 Billing contacts responded to within five days	%	100	99.97	100
DG7 Written complaints responded to within 10 days	%	99.90	99.40	99.70
DG8 Bills based on Company or customer meter readings	%	99.96	99.97	99.96
DG9 telephone handling satisfaction	%	-	4.59*	4.57

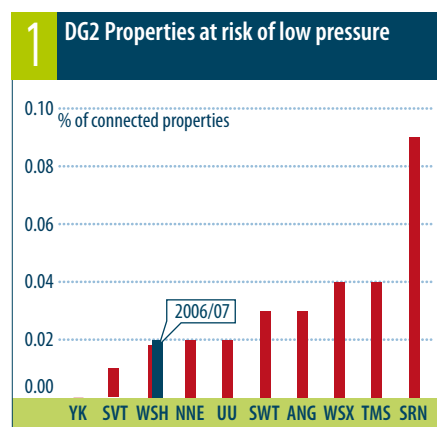
* Measure introduced in 2005-06 (score out of maximum 5)

Sewerage Service				
Performance Measure	Units	The Monitoring Plan Target	Previous Performance 2005-06	Actual Performance 2006-07
Properties flooded internally - Other causes (excluding extreme/severe weather)	No.	120	150	203
Properties flooded internally - Hydraulic overload (excluding extreme/severe weather)	No.	122	81	96
Total properties subject to internal flooding (excluding extreme/severe weather)	%	0.018	0.017	0.020
Properties at risk of flooding	No.	432	514	484
Sewer collapses per 1,000km of sewer	No.	27	28.90	35.80
Intermittent discharges satisfactory	%	90.80	88.23	91.20
Environmental Compliance				
Performance Measure	Units	The Monitoring Plan Target	Previous Performance 2005-06	Actual Performance 2006-07
Percentage population equivalent served by compliant works (LUT)	%	100	99.91	99.97
Sewage sludge disposed of satisfactorily	%	100	100	100
Wastewater Treatment Works complying with numeric consents	%	98.0	96.49	97.60
Bathing waters - compliance with mandatory standards	%	100	100	99
Bathing waters - compliance with guideline standards	%	Stable	91	89
Number of pollution incidents at CSOs and sewers (cat. 1 & 2)	No.	6-12	11	9

Key outputs

and service delivery

Over the last year we have generally maintained our levels of service to customers at acceptable levels, with some examples of very strong performance. We carry out regular research with customers to understand their satisfaction with the services we provide. Latest research shows that overall satisfaction with our levels of service remains high.



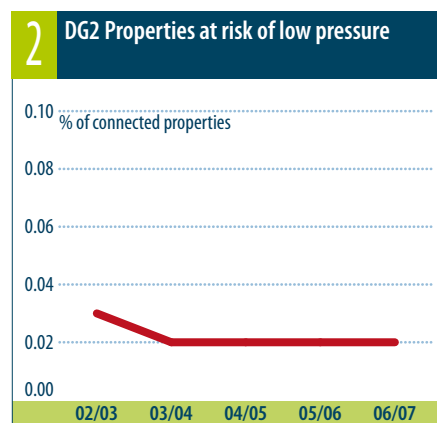
Water Service

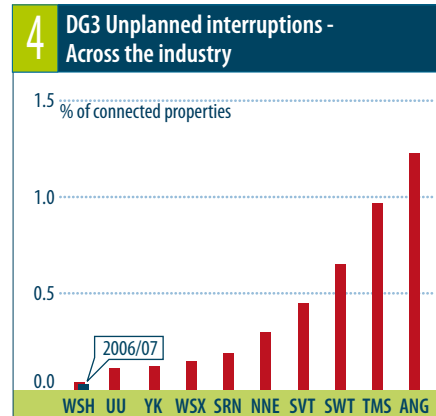
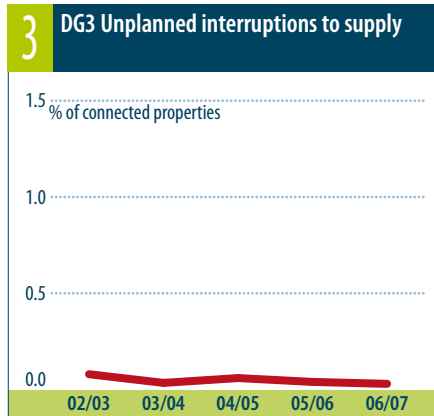
Low pressure DG2

A total of 221 properties remained on the low pressure register at the end of this report year, the same figure as in 2005-06. This is ahead of the AMP4 Monitoring Plan target of 242 properties. This represents 0.016% of our connected properties and we remain ahead of the sector average of 0.028%. **1 2**

We have continued with our pressure logging programme to identify properties experiencing low pressure during the year and especially during the summer months when demand is higher.

A total of 1,459 properties were added to the register during the year from this logging programme. However, as a result of company action, such as mains replacement, improved pressure control and operational changes or identification of pressure problems on the customers' supply pipes, the same number of properties (1,459) were removed from the register during the report year.





Interruptions to supply DG3

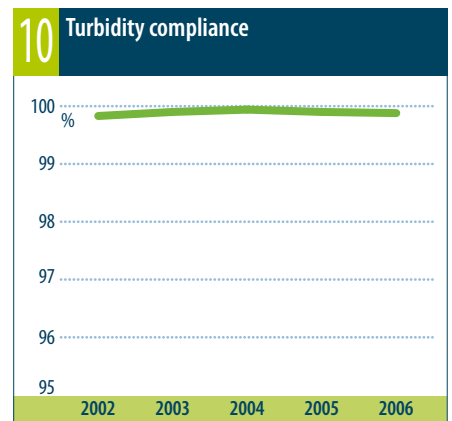
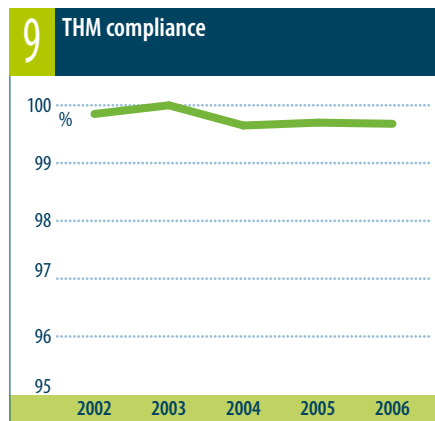
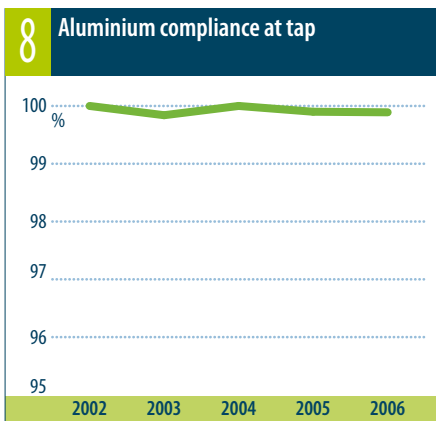
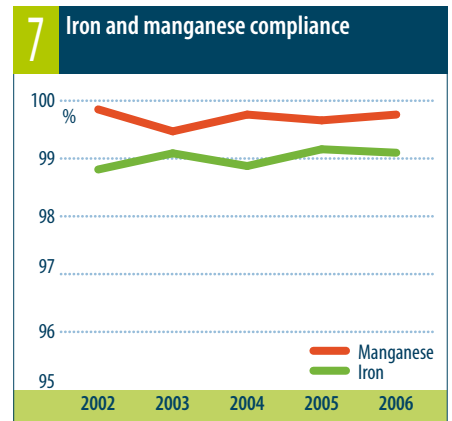
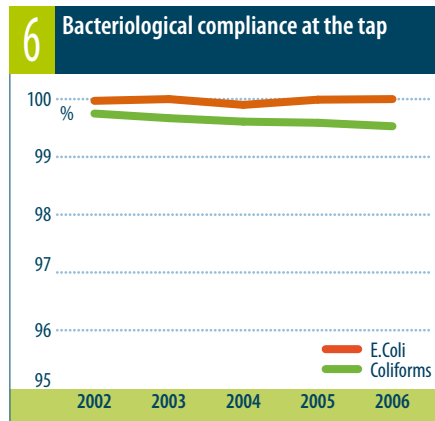
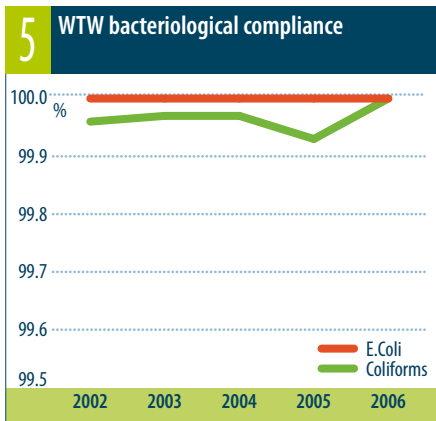
We have continued to sustain the low levels of unplanned supply interruptions lasting for more than 6 hours, with the number of properties affected falling from 454 in 2005-06 to 313 in the report year.

Our performance, as measured by Ofwat's overall performance score, was 0.028% compared to 0.04% last year. The number of properties affected by unplanned supply interruptions lasting more than 12 hours was 71 compared to last year's figure of 80. **3 4**

Notwithstanding our relatively high burst rate, this performance is currently amongst the best in the industry. We continue to look to improve our operational procedures throughout the supply chain and maintain the focus on responding quickly to supply interruptions so as to minimise interruption periods.

Amongst the measures introduced, are improving asset records, obtaining advance warning of asset failure through use of low flow alarms and extending the use of rapid response repair gangs and using better equipment.

We have continued to develop techniques designed to minimise the disruption of supply to customers during planned work. While the rate of asset renewals has remained relatively high, the number of advance warnings of interruptions lasting more than 12 hours, due to planned work, has fallen further, from 1,642 properties last year to 1,476 properties in the report year. Of these planned interruptions, there were no properties affected by overruns beyond the specified period of interruption.



Drinking water quality

During 2006, we have continued to sustain a high level of performance for drinking water compliance. In respect of both total coliforms and E.Coli recorded at WTWs, we achieved a 100% compliance, our best ever performance. This continuing improvement reflects the commitment of both ourselves and our operating partners to deliver drinking water that meets the required quality standards. **5**

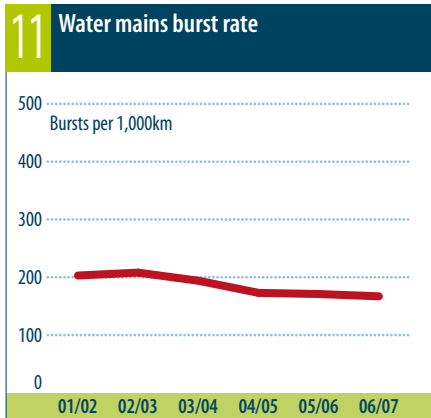
2006 also saw the development of the Public Health Partnership for Wales, a joint venture between ourselves, local authorities, health authorities, the Welsh Assembly Government, the Consumer Council for Wales and the DWI. This Forum meets regularly and aims to improve the way that the members work together to ensure an ongoing framework aimed at delivering a consistent understanding and management of water quality events, as well as protecting public health at all times.

The quality of water supplies is measured against a set of standards that are specified in the Water Supply (Water Quality) Regulations (Wales) 2001.

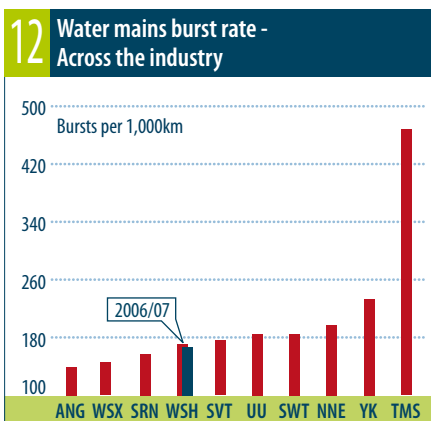
Following the introduction of these regulations, DWI has replaced overall compliance at the tap with two zonal measures, Operational Performance Index (OPI (TIM)), based on compliance for turbidity, iron and manganese, the principal parameters for discolouration problems, and mean zonal compliance. In 2006, the mean zonal compliance was 99.95 % and OPI (TIM) was 99.70% as compared to 99.95% and 99.74% respectively in 2005. These new measures for compliance set the base line for future improvement under these regulations, and highlight the areas where improvement strategies should be focused. Performance against a range of water quality parameters is shown in charts **6 7 8 9 10**.

After disinfection at WTWs, bacteriological quality may deteriorate slightly in service reservoirs, distribution mains and customer pipe work. Coliforms were absent from 99.93% of samples taken from service reservoirs and absent from 99.53% of samples taken from customers' taps. E.Coli was absent from 100% of samples from service reservoirs, WTWs and samples taken from customers' taps.

Bacteriological Compliance - 2006		
	Coliforms	E.Coli
WTW	100	100
Service Reservoirs	99.93	100
Zones	99.53	100

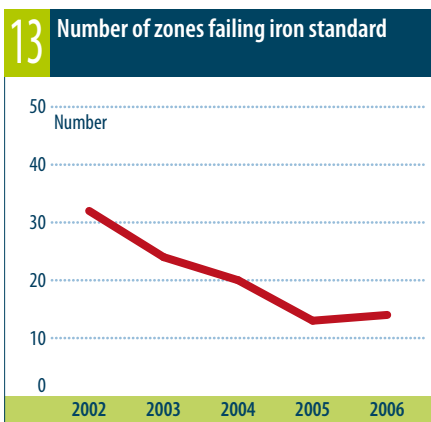


of high burst rates occur on older plastic and asbestos cement water mains in some areas. The overall burst rate during the year was 167 bursts per 1,000km, compared to an equivalent figure of 171 bursts in the previous year. This is well below our Monitoring Plan target of 194 per 1,000km, and this, together with our sustained levels of service performance, indicate marginally improving serviceability to customers. Our position relative to other companies has also improved. **11 12**



Delivering improved drinking water quality
The improving trend in iron compliance at customers' taps was tempered slightly this year by repeated iron failures in the Ledbury area. Apart from these localised problems, iron compliance elsewhere in the company was significantly better than in previous years. Substantial trunk and distribution mains renovation is now progressing under the Section 19 rehabilitation programme.

In 2006, 390km of unlined iron mains were refurbished in addition to the 407km in the previous year. The 797km of mains refurbished to date, is 169km behind the anticipated output in the FD. This is mainly due to the significant change in the nature of the programme with more work required on trunk mains and in more difficult urban areas than was originally planned. Also, despite the intensive water sampling programme on over 300km of unlined iron mains undertaken last year, far fewer schemes passed the justification criteria for inclusion in the Section 19 rehabilitation programme than expected. We propose to agree a revised undertaking with the DWI to deliver a lower length of output in AMP4, whilst still meeting our water quality targets.



Maintaining serviceability to customers

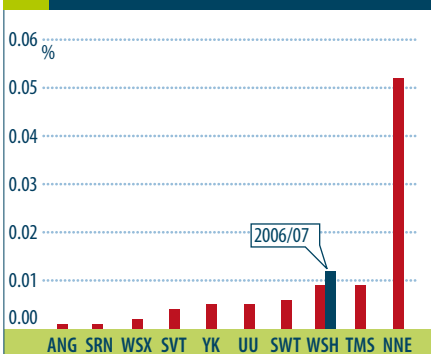
In addition to minimising the duration of supply interruptions, we have a programme of work aimed at reducing the frequency of supply interruptions to worst served customers. Our zonal approach to improving performance seeks to maximise the value from our water quality mains rehabilitation programme and prioritise the installation of pressure reducing valves and the replacement of those water mains that are in a poor condition. This has helped maintain the reducing trend of burst rates on our water mains, although local clusters

Fourteen out of 89 zones experienced sample failures against the water quality standard for iron, which is comparable to 2005, when 13 out of 91 zones experienced iron failures. Also, 99.10% of samples taken from customers' taps were compliant with the required water quality standard for iron, against 99.16% of samples being compliant in 2005. **13**

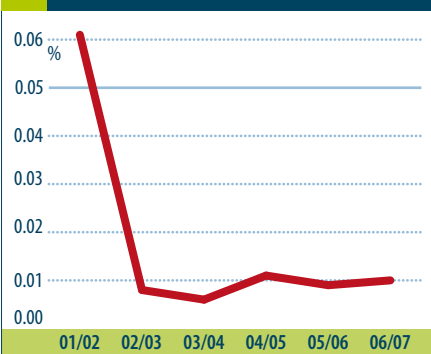
14 At risk register

	2 in 10	1 in 10	1 in 20
Start of report year	202	312	472
Removed (Company action)	24	20	41
Removed (better info)	2	2	0
Removed (lesser risk)	1	8	10
Added (better info)	6	12	77
Added (increased risk)	8	1	0
End of year report	189	295	498

15 % Properties flooded (hydraulic overload)



16 % Properties flooded (hydraulic overload)



Sewerage Service Sewer flooding DG5

The DG5 'at risk register' reached its lowest level ever at the end of AMP3. The register was rebased at the start of AMP4.

We continue to prioritise our work to address problems at properties where flooding has occurred most frequently.

Reducing the number of incidents and the risk of flooding remains a priority for us. In the AMP4 period, we will be investing to tackle current and new hydraulic overload problems and also contain the number of incidences of flooding from other causes (such as blockages, collapses and equipment failure). Our Monitoring Plan target is to tackle a total of 1165 flooding problems made up of 736 internal problems and 429 external problems. The outcome of this is expected to be a net reduction of 548 properties on the 'at risk register' (ARR) by 2010.

The primary aim of the AMP4 plan is to reduce the number of flooding incidents and therefore minimise customer suffering. In order to achieve these objectives, we have carried out a review of the programme which includes further analysis of the areas currently at risk and development of all projects to an outline solution stage with outline costs. Some projects with low benefits may not receive a full investment solution.

The initial results of the re-prioritisation exercise have been shared with Ofwat. The Reporter has subsequently carried out a review of the Company processes for allocating properties to the registers, the prioritisation criteria and the costing of projects.

We will continue to have dialogue with CCWater and Ofwat in the development of processes to identify the most beneficial programme of work for AMP4. We will be increasing the use of hydraulic analysis where appropriate to allocate affected properties to the relevant risk categories and also to develop the solutions for particular projects.

The 2006-07 report year began with a total of 514 properties on the ARR (2:10 and 1:10 risk categories).

During the report year, we carried out investment schemes to remove the risk of sewage flooding to 44 properties on the ARR. A further 4 properties were removed due to 'better information' becoming available. 41 properties were also removed from the '1 in 20 register'.

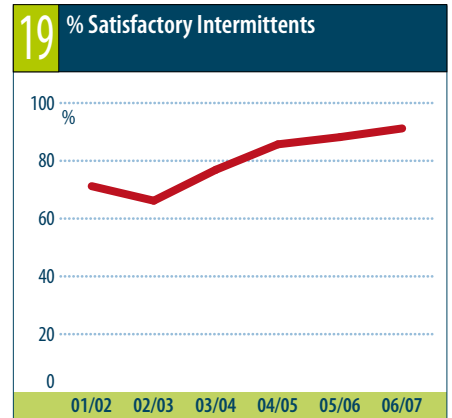
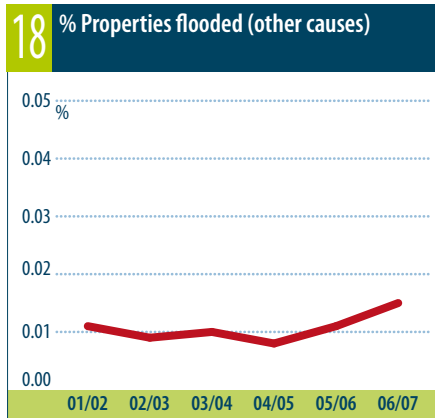
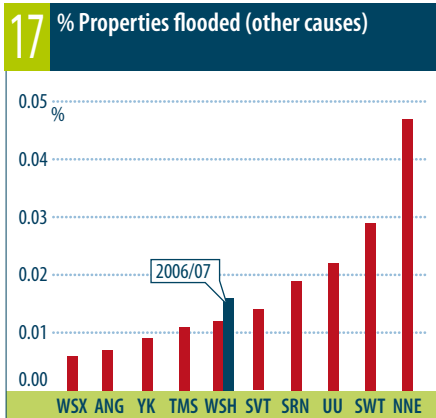
We have now reduced the ARR to 484 properties; this is 52 properties short of the Monitoring Plan target. We will accelerate the remaining programme to catch up to the Monitoring Plan target. ¹⁴

We removed a further 24 sites of 'area' flooding from the external flooding registers through capital schemes (one of these from the '1 in 20 +' register).

Although we are addressing the issues around properties that we know to be at risk, each year new incidents occur where flooding has not been experienced before. We continue to pursue initiatives to identify these vulnerable areas before problems occur, and are actively setting up more flooding forums in vulnerable areas in order to engage all parties including regulators and the other authorities that have responsibilities for flooding.

The percentage of properties that experienced internal flooding (all causes) was 0.022% in 2006-07, higher than the Monitoring Plan target of 0.018%.

A total number of 132 properties, (165 incidents), were affected by flooding due to hydraulic overload in the year. This is an increase of 14 properties compared to the previous year. This measure is very much affected by severe weather and there can be considerable changes year on year. Severe weather (storm return periods ranging from 10 year to 92 year) affected 36 properties in the months of August and October. Rainfall in the months of July, August, September and October accounted for 123 of the 165 incidents. The graph shows that the trend has been fairly stable over the past five years. ¹⁵ ¹⁶



We have seen an increase in the number of 'other cause' flooding in the year, from 150 properties to 203 properties. The number of incidents rose from 166 to 214.

The lowest ever level of 'other cause' incidents was achieved in 2005 and we have seen a gradual increase over the past two years. [17](#) [18](#)

Most of these incidents are caused by blockages in the sewer system. The main cause of blockages is fat, oil and grease deposited in sewers near food establishments, silt build up in flat sewers and ragging on open joints. We have made the reduction of sewer flooding and pollution our highest priority, and in 'other cause' flooding a number of initiatives are already in progress. These are described in the section of this overview headed 'Sewerage Network Performance Improvement Plan'.

We expect this strategy to deliver a substantial reduction in the incident numbers over the forthcoming year to meet the Monitoring Plan target of 120 incidents per year.

Delivering the quality enhancement programme

Our target during the AMP4 period is to tackle 446 intermittent discharges, achieve improvements at 135 WwTWs, carry out 77 environmental investigations and provide 'First Time Sewerage' services to 519 properties.

During the report year, we have dealt with 87 intermittent discharges against a Monitoring Plan target of 94. This includes the completion of improvements at one asset originally identified in AMP3.

A total of 91.2% of our intermittent discharges are now satisfactory against a Monitoring Plan target of 90.8% and a 2005 figure of 88.2%. [19](#)

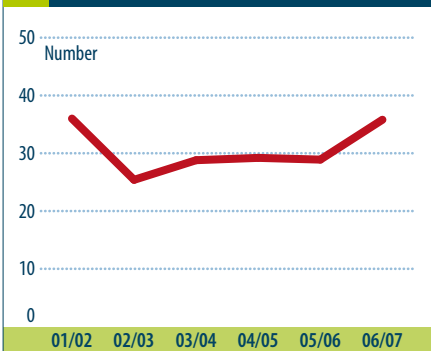
We have carried out improvements at nine WwTWs. Of the 13 outputs originally identified for year 2, seven have been completed, six have been delayed to allow completion of the EA review of consents under the Habitats Directive. A further two have been brought forward.

Improvements at seven sites to meet the Urban Wastewater Treatment Directive were delayed beyond the specified deadline due to land and planning issues. One of these has now been completed. Progress at the remaining sites is on schedule for completion within the time frame specified in enforcement notices issued by the EA.

We have carried out a cumulative total of 52 environmental investigations against a Monitoring Plan target of 66 investigations. A further 16 sites are complete and awaiting final confirmation from EA.

The 'First Time' sewerage programme has been reviewed to ascertain whether there is a benefit in carrying out some of the projects. Of the original 23 projects scheduled for completion during the AMP4 period, we have determined that only one project meets the cost and environmental benefit criteria. We are pursuing this project and six other projects where a duty already exists for us to provide public sewers to the customers affected. Two of these projects have been completed in the report year. For one of these schemes, not a single customer has yet connected to the new sewer (provided at a cost of £450k).

20 Number of sewer collapses per 1,000km



In the AMP4 period, we plan to renovate or replace 123km of sewers. In the report year, we have renovated or replaced 26km of sewer against a Monitoring Plan target of 29.6km. In the report year, we have also laid or adopted 35km of new sewers against a Monitoring Plan target of 41km. Our cumulative new sewers laid or adopted to the end of this year is 105km against a target of 82km. Our programme to target the most vulnerable assets remains a priority.

Our programme of desilting, cleaning and inspection continues. A total of 107km of sewers was inspected by CCTV in the report year, including 42km on the critical sewer network. This helped give us a better understanding of asset risk and the condition of the sewers and helped direct investment to the most appropriate cases.

We have reported a total of 17 category 1 & 2 pollution incidents of which nine were associated with CSOs and foul sewers. This compares with 17 last year of which 11 were at CSOs and foul sewers.

With the inclusion of 208 Category 3 incidents, the total number of sewage related incidents was 225 for the report year. Of this total, 166 were associated with CSOs and foul sewers, against a figure of 149 for 2005.

Pollution incident numbers used to calculate OPA exclude incidents at sites that are compliant with their discharge consent. In the report year, we have 15 incidents for Category 1 & 2 sewage for OPA purposes against a figure of 8 last year. The number of Category 3 incidents (water and sewerage) for OPA this year is 157 compared to 151 last year. [21](#) [22](#)

We have developed plans to address odour issues at the 33 sites identified in the Monitoring Plan. 11 of these sites have been completed in the report year and at the remaining sites, the work is either in progress or in the design and feasibility stages.

Sewerage Network Performance Improvement Plan

Having seen the performance of the sewerage network deteriorate in the report year, we have reviewed our strategic and tactical improvement plans in this key area. During the report year we developed our improvement plans to include:

- An Asset Performance Analysis - This is being undertaken by our Tactical Sewerage Management team,

which has helped determine a clear understanding of the performance of our sewerage network. This has identified approximately 300 locations where a higher risk of pollution exists. This thorough examination of our assets and historical incident analysis, has allowed us to build improvement plans to address this issue.

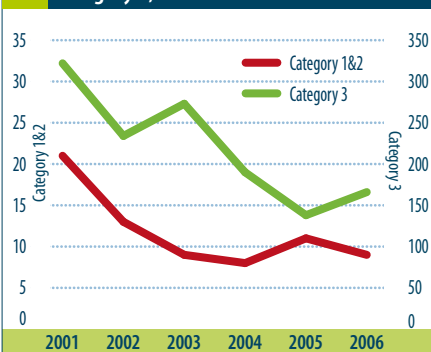
- Increased use of telemetry – We undertook a pilot study at Afan Baglan catchment, one of our worst performing areas. This involved the installation of telemetry alarm devices on key points on the network. The positive results of the trial has resulted in a plan to install over 500 devices on a prioritised basis across the region in 2007-08.
- Targeted sewer de-silting - This was initially piloted as part of the Afan Baglan trial. We have developed a plan for deployment across the region which will be rolled out in 2007-08.
- Operational Maintenance Frequency – We have reviewed operational maintenance frequency and have increased the frequency of visits where we have known 'hot spots', particularly at combined sewer overflows and on sewers which are susceptible to hydraulic overload.

We anticipate that these initiatives will deliver increased on going benefit and improve the performance of the sewerage network in 2007-08.

Asset Management and Planning

Over the last year, we have continued the development of our asset management systems to deliver asset management principles in line with those of the common framework. We have delivered improvements in maintenance prioritisation systems, and embedded maintenance optimisation within SAP. Following a review by Tynemarch, we evaluated our asset investment planning tools and began a project, that will lead to decisions being based on forward looking risk-based analysis of our assets. This system, which will be introduced in 2007-08, will be built on the foundation of the improvements in asset data and systems achieved in the report year.

21 Number of pollution incidents at CSOs Category 1, 2 and 3



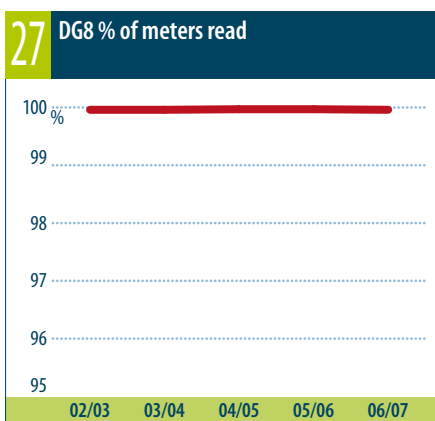
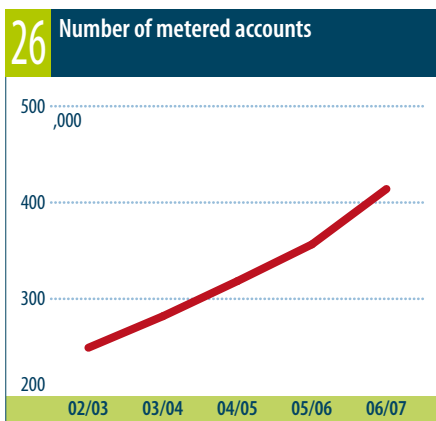
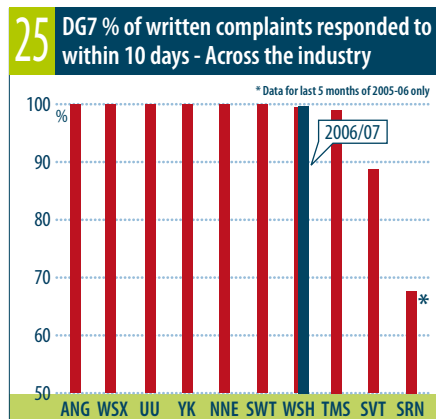
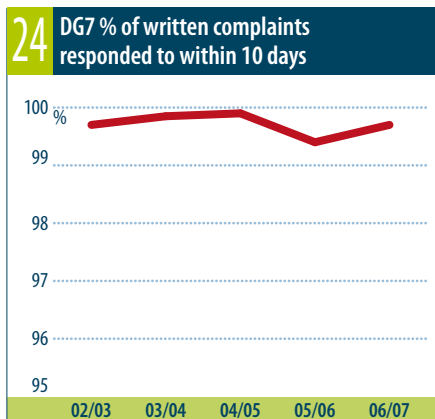
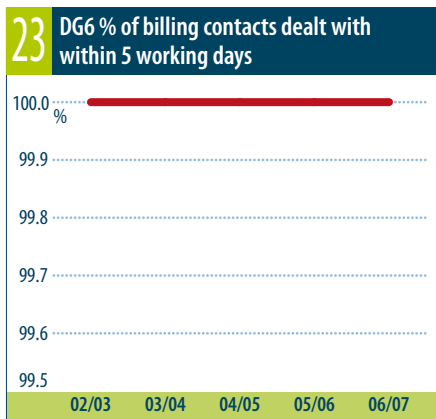
22 Number of pollution incidents associated with CSOs and foul sewers during 2006

Incident Category	No. of incidents associated with CSOs	No. of incidents associated with foul sewers
1	1	0
2	1	7
3	71	86
Total	73	93

Maintaining serviceability to customers

In the AMP4 period, our target is to maintain stable serviceability to customers.

The main Ofwat measures of serviceability are the number of collapses and blockages on the sewer network. In AMP3 we targeted a reduction of 25% in the sewer collapse rate. In AMP4 we are targeting an average sewer collapse rate of 27 per 1,000km. The collapse rate remains significantly higher than the sector average (approximately 13 per 1,000km). In the report year the number of collapses have risen from 28.9 per 1,000km to 35.8 per 1,000km. Although the trend has improved since 1999, the rate has been rising in the last two years. We are analysing the data to understand this deteriorating trend and we have detected an increase in the number of failures on particularly sensitive rising mains. [20](#)



Customer Contact

Billing contacts DG6

During the report year, we handled a total of 1,017,704 billing contacts, a decrease of 1.77% on last's figure of 1,035,447. The total billing contacts consists of 132,664 written contacts and 884,873 telephone contacts. The remaining 167 contacts were visits to our offices.

The company sustained performance on the DG6 measure, with almost 100% receiving a response within 5 working days. [23](#)

Written complaints DG7

In the report year, we responded to 10,348 written complaints compared with 9,691 in the previous year.

Of the 10,348 responses to written complaints during the report year, 79% related to our charges, 8% to sewerage services and the remainder were in respect of water distribution, water quality, leakage and environmental issues. The increase in the number of complaints was mainly attributable to increase in queries relating to metered supplies.

There has been a 39% reduction in stage 2 complaints. This has been attributed to staff providing fuller and more substantive responses to customers and ensuring that promises made in correspondence are kept. [24](#) [25](#)

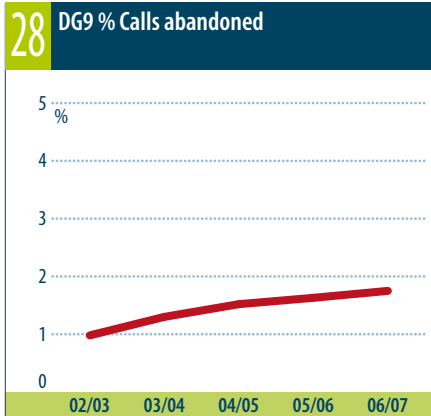
Meter reading DG8

During the report year, we have continued with the programme of improvement, achieving a DG8 position of 99.96%. Only 0.04% (146 meters) remain unread by either the company or the customer at year end.

The total number of metered accounts rose by 29,145 during the year to 414,061. The increase is primarily due to 'free' meter options, but is partly attributable to an increase in new connections.

Internal meters continue to pose a challenge. This year we adopted a structured mail shot and outbound dialling approach to unread internal meters in order to prompt customer contact. This, along with the meter readers adopting flexible work patterns to capture difficult domestic meters in early evenings and weekends, has also helped drive the performance forward.

[26](#) [27](#)



Telephone contact DG9

During the report year, the Call Centre experienced a busy year with our call agents handling a total of 1,220,893 calls. This represents an increase of 9.4% on the previous year.

From the 1st of October 2006, water operational calls were handled at our new OAC. This increased all lines available from the 140 in the original combined call handling facility to 260, with 120 lines being added for operational call handling. The transfer of calls occurred successfully, without any impact on the service offered to our customers.

On the 26 February 2007, sewerage operational calls were moved from our call handling facility at Longcross Court to the new OAC in St Mellons, Cardiff. Prior to the outsourcing of the Sewerage Operating Contracts in 2002, the sewerage calls were handled by the Local Councils.

Performance against the DG9 measure was again good with only 1.76% of calls being abandoned. 30% of these were abandoned in the first 10 seconds of the call. 0.4% of callers received an engaged tone, the main component of all lines busy occurring in August 2006, when a partial failure of the ACD (automatic call distributor) led to a complete loss of telephony service to the call centre. This resulted in 3,842 customers receiving an engaged tone. [28](#)

GSS payments

All payments were made against the enhanced category of Guaranteed Standards of Service payments. The total number of payments made was 1,076. Of the payments made, 531 related to appointment failures and 472 to sewer flooding. Efforts have been made to reduce the number of penalty payments through automation of the link between two main

computer systems and running frequent reconciliations between the two systems to prevent any missed payments.

Customer Experience

Our aim is to deliver the highest standards of service to our customers. Consequently, we are putting in considerable effort to develop and improve the 'customer experience' when people have reason to contact us.

In the report year we have made a number of improvements to our service delivery, all of which were designed to achieve higher standards of service.

The starting point for our improvements is our Customer Service Strategy. This was incorporated into our Business Plan for the year and the initiatives it contains are highlighted below:

Customer Research – This involved undertaking extensive research (via Beaufort Research Ltd) to understand what customers think of the key water and waste water services we provide. This includes a 'Mystery shopping' initiative to randomly test the service provided at our call centres. We also participate in the National Complaints Culture Survey where we partake in a survey measuring how we compare with other service sector industries.

Operations Activity Centre (OAC) – As stated above, in the Autumn of 2006 we implemented the first stage of our OAC, where we established a separate call centre to handle operational calls. Prior to this, water operational and billing calls, were handled in a single call centre with the same staff handling a mixture of customer contacts. In October 2006, we transferred our potable water calls and on the 26 February 2007 we moved our sewerage calls into the OAC. Our plan is to offer the very best service to customers when they have a problem with their water or sewerage service. One of the key benefits we have seen is an improvement in dealing with customer problems on the first call. This means that less calls are 'passed on' and instead they are dealt with at the point of contact. To date, 95% of all calls have been answered within 30 seconds and we are achieving a 58% resolution of calls relating to potable water activities on first contact, compared to an approximate figure of 40% for the same period last year.

Floodcare Packs – There can be no worse service failure than sewage flooding. In the report year, we have introduced Floodcare packs, which have substantively improved communication those customers who experienced an internal or external sewage flooding incident. The process ensures customers are fully informed of the measures being put in place to avoid reoccurrence of a serious incident.

Staff Training – During the year, we have communicated our ‘Customer Handbook’ to all staff who have a direct interface with customers. This provides our staff with valuable information on who is responsible for specific service delivery, policies, procedures and the standards we expect of our staff who deal with customers. It involves face to face training sessions led by our central customer service team and helps reinforce our commitment to providing a high quality customer service.

During the report year, telephone call recording was introduced into the billing contacts centre, this is being used to help train staff and improve the service offered to customers.

Looking Forward – We have established a Customer Service Leadership team consisting of directors from our operational and billing & income partners. This team, led by our Head of Customer Service, is focused on developing specific improvement plans to further reduce complaints, improve ‘first time’ resolution of customer concerns and to improve the customer service skills of our staff. In addition, the team will also support the development of our service improvement plans as part of the PR09/AMP5 planning process.

Special Services

This year has seen a further rise in the number of successful applicants on the Vulnerable Group Tariff (VGT) aimed at helping those on low income, large families or with illnesses which would necessitate the use of higher than average volumes of water.

The number of customers on our Special Assistance Register has risen slightly by 3% in the report year. We continue to promote our services through care organisations, company leaflets, the bill and through contact with staff. We have continued our work to prevent Bogus Callers with information sharing links established with all the regional Police Forces.

Sustainability

Our aim is to meet our customers’ expectation that our provision of water and wastewater services to them will not have an unduly adverse impact on the environment within which they live. As well as working to ensure that our bills are affordable to our customers, we aim to operate a sustainable business.

An important aspect of this is how we respond to the challenge of potential climate change. We believe it prudent to make plans to mitigate our contribution to climate change as well as adapting to the challenges we may have to face. Over the last twelve months we have worked with the Carbon Trust and have undertaken a study to evaluate how we may be contributing to climate change.

This study has provided us with information to enable better decision making regarding those parts of our business with the largest potential to contribute to climate change. In terms of carbon equivalents we have also worked to cost the investments that could be required to enable compliance with the Water Framework and Habitats Directives. As a result of this work, where appropriate, more sustainable treatment technologies such as reed beds are now considered where there is a clear environmental benefit in terms of carbon emissions.

During the last year, we have also invested in plant utilising biogas generated from our sludge digestion facilities and undertaken work to optimise treatment processes to minimise carbon emissions.

Health & Safety

performance in 2006-07

Our health and safety management system applies to all contract partners who work with us to deliver services to water and sewerage customers and is described more fully in our annual health and safety report. The 2007 Health and Safety Report will be published on our website on or shortly after 9th July 2007.

We assess the health and safety competence of all contractors before appointment. We set proactive performance targets and monitor against them on a monthly basis to promote continuous improvement and establish robust health and safety practices. Furthermore, we operate an innovative process of internal cross auditing to supplement the external and independent auditing of health and safety performance.

Our management system ensures that all incidents and 'near hits' are reported and investigated, and this helps set targets to drive continuous improvement in health and safety performance.

This is the third year in which we have captured performance data not only from contract partners, but also for their lead subcontractors.

Performance in 2006-07

In the report year, we set 172 individual health and safety targets of which 96% were fully met during the year. The remaining 4% will be completed within the first quarter of 2007-08.

On a like for like basis, and including lead subcontractors, reportable incidents fell by 12% and days lost due to illness reduced by 4%. However, non-reportable incidents increased by 6%. Overall, this continues a steady improvement year on year and encourages us to focus on this very important area of our business.

Regrettably, against this overall backdrop of continuous improvement, we experienced our first fatal accident when a colleague employed by one of our contractors was killed at Prioress Mill

	2003-04	2004-05	2005-06	2006-07
Reportable incidents				
Exc. subcontractors	32	28	-	-
Inc. subcontractors	N/A	40	46	42
Non-reportable incidents				
Exc. subcontractors	345	263	-	-
Inc. subcontractors	N/A	343	284	301
Dangerous occurrences				
Exc. subcontractors	4	3	-	-
Inc. subcontractors	N/A	6	0	1

Pumping Station near Usk in May 2006. This incident is still being investigated by the Police and the Health and Safety Executive.

During the report year, we also undertook a number of other health and safety initiatives and, in particular, we:

- Embarked upon a review of our health, safety and procurement procedures with a view to securing certification to OHSAS18001 by April 2008.
- Commenced the development of an IT system database to provide us with on-line reporting of health and safety performance and document management.
- Extended further our training initiatives to increase the competency of staff in investigating health and safety incidents and auditing.
- We have added robustness to the process by formalising completion of actions to address non-conformances.
- Introduction of the first annual Health and Safety Conference incorporating Contractor of the Year awards.

Monitoring of days lost related to accidents and staff ill health (including non-work related absence) shows that in the report year around 2.31% of available working days was lost. This compares well with industry benchmarks.

In 2007-08, our general focus will be to drive further improvement in health and safety performance, with a particular focus on the behavioural aspects of health and safety management.

Financial

overview

Financial results

Our appointed business turnover in the year to 31 March 2007 was £569 million (2006: £545m) – an increase of 4%. The increase primarily reflects the price increase of 6.4% in the year offset by a loss of revenue due to customers switching to metered charging and a reduction in consumption from metered and trade effluent customers. The effect of ‘customer dividends’ in the year was that turnover was some £25m (2006: £23m) below the level that would have resulted from the full price control allowed by Ofwat. The rate of voluntary customer switching to metered charging in the year slowed somewhat to nearly 22,000 customers (2006: 27,000 customers), whilst some 9,000 new customers (2006: 10,000 customers) were added during the year, all of whom are metered.

The current cost depreciation charge was £134m (2006: £122m). The increase is due to additional charges arising on the £128m of above ground capital expenditure during the year and a revision to the expected useful lives of certain assets.

The infrastructure renewals charge was £52m (2006: £50m). The charge reflects the medium to long-term maintenance needs of the infrastructure network and is based on expected maintenance expenditure over the period 2001 to 2015.

Net interest charges for the year were £153m (2006: £151m). Despite interest rate increases, the average cost of net debt during the period was 6.2% (2006: 6.4%), reflecting the benefit of refinancing undertaken during the year.

Current cost profit before tax was £84m (2006: £63m). This profit was made after funding the ‘customer dividend’ of £19 for customers receiving both water and wastewater services. The Board of Glas Cymru (the Board) has decided to increase the ‘customer dividend’ for 2007-08 to £20.

The tax credit for the period was £13m (2006: £nil), comprising of £12m deferred tax credit and a £1m current tax credit.

Continued focus on cost control

Our appointed business operating costs (excluding depreciation and infrastructure renewals charge) were £220m (2006: £205m), which represents an increase in real terms of some £8m. This increase largely reflects substantial increases in energy costs, which were some £8m (or 29%) higher than in the previous year, which in turn were some £9m higher than the year before.

Around 70% of operating costs were incurred under outsourced service contracts, including the contract with United Utilities Operating Services (UUOS) for the operation of the water network and the wastewater network in North Wales and with Kelda Water Services, for the operation of the wastewater network in South Wales and Herefordshire. These contracts operate on a target cost basis which are designed to incentivise further improvements in operating efficiency in the period up to March 2010.

Customer debt recovery remains subject to very close attention by both ourselves and by Thames Water, the billing and income services contract partner. Despite a difficult environment with water companies not being allowed to disconnect supplies to domestic customers for non-payment, cash collection performance was on target. The bad debt charge for the year of £11m (2006: £8m) represents around 2% of annual turnover.

Our capital expenditure during the year (before capital grants and developer contributions and including infrastructure renewals expenditure) was £269m (2006: £238m), bringing the total expenditure over the first two years of the five-year AMP4 period to £507m or some two fifths of the total programme.

We work with an alliance of capital investment partners (Laing Utilities, Morrison, AMEC, Costain, Imtech Process, MEICA, and Black and Veatch) with the aim of delivering the AMP4 investment programme at the best value for money

for customers. A priority during the first two years of the programme has been to reappraise rigorously the design of certain key schemes with a view to achieving the reductions in unit costs assumed by Ofwat in the 2004 Price Review. We are planning to invest some £600m over the next two years, challenging targets when compared to historical spend levels. At this stage, it is expected that investment expenditure over the AMP4 period as a whole of some £1.3 billion will be broadly in line with the allowance made by Ofwat in the FD.

Financing strategy

The Board considers that it is in the best long-term interests of our customers to continue to reduce the level of gearing, with a view to achieving further reductions in its cost of finance.

Credit ratings are unchanged during the year. However on 14 June 2007 Moody's assigned an A3 corporate rating to Welsh Water, reflecting the improved credit quality of the Company. To protect the Group's high credit quality, the Board has implemented prudent financial policies, covering the fixing of interest rates and the investment of cash balances. The Board considers that liabilities index linked to UK RPI inflation are particularly appropriate for the business, as its revenues and RCV are also linked to RPI through the regulatory system operated by Ofwat. As at 31 March 2007, approximately 57% of the group's gross debt was index linked via bonds and derivatives.

Future prospects

The objective of the Board will be to continue to improve the financial performance of the company during the period to 31 March 2010. The Board believes that its financial strategy will put the company in a strong position to raise the funding for the following five-year investment programme in the period

to 2010 on efficient terms, which is an important part of the company's strategy to keep down customers' bills in the long-term.

The main risks to the achievement of this financial objective involve upward cost pressures. The unit costs of investment schemes are under upward pressure due to increasing materials costs and emerging resource shortages in the construction industry. We continue to seek to mitigate these input cost increases by securing the resources for a long-term programme of work with its partners and by revisiting designs and working methods to secure offsetting efficiency improvements.

In addition, power costs have increased dramatically over the last two years and we, like all water and sewerage companies, have a large energy requirement, notably for pumping and treatment processes. The increase in power prices can be only partially offset by improved working practices and investment in energy efficiency schemes. More recently, power prices have fallen back, which has enabled us to purchase a large proportion of our power needs for the year to 31 March 2008 at a reduced cost. However, the risk of future volatility in power prices remains. Under the target cost arrangements, these upward cost pressures are shared only to an extent between ourselves and our relevant partners.

We and our partner, Thames Water, also maintain a tight focus on customer cash collection in recognition of the continuing risk to cash collection posed by increasing water bills and the absence of a disconnection sanction.

We do not expect to pay tax on our trading profits during the year to 31 March 2008, due to the availability of tax allowances on our investment programme. Future tax liabilities beyond that date will also be primarily influenced by this factor.

Key supporting

information

Water Service

Water capital outputs

During the report year, we delivered the following major outputs from our water service investment programme:

Water Treatment Works (WTWs):

- Two schemes completed at Felindre and Bolton Hill WTWs in line with the agreed undertaking with DWI.
- Construction commenced at Bretton WTW and scheme design commenced at a further 4 WTWs.

Water mains programme:

- 390km of unlined iron water mains refurbished to improve water quality and iron compliance at customers' taps.
- 82km of water mains causing frequent supply interruptions to customer supplies replaced.
- 20km of water mains relined under maintenance programmes.
- 301km of mains cleaned for water quality improvements and ongoing maintenance of the distribution system.

Water supply asset maintenance

We are required to identify any WTWs where maintenance investment in the year has exceeded £5m or is over £100k and is 10% or more of the Gross Modern Equivalent Asset (GMEA) value of the works. This threshold of investment is high and does not reflect the amount of capital maintenance we actually carried out.

During the report year, we have carried out planned capital maintenance work at 55 WTWs with 22 WTWs having more than £100k invested in the report year. However, expenditure did not exceed the £5m or the 10% GMEA value for any single WTW.

Planned maintenance work has been undertaken during the year at 52 service reservoirs and 28 water pumping stations with 11 single sites incurring investment of over £100k and 10% of GMEA.

During the report year, we renewed a total of 269km of water mains which included 174km of water mains renewed to meet the DWI S19 undertaking. A total of 82km of water mains were renewed under

prime purpose maintenance, and 10km were replaced as a result of diversions.

Renewal of asbestos cement and older plastic mains remains at a low rate and is confined to short lengths of mains prone to high incidence of bursts. This is unsustainable over the longer term, as it will take approximately 200 years to replace all asbestos cement and old plastic mains at the current renewal rate.

Capital expenditure water

Actual expenditure during the report year was £132m, £3m higher than the £129m allowed in the FD (inflated by RPI).

The cumulative position for the first 2 years of the AMP4 period shows an overall underspend of £14m. The main variances are explained as follows:

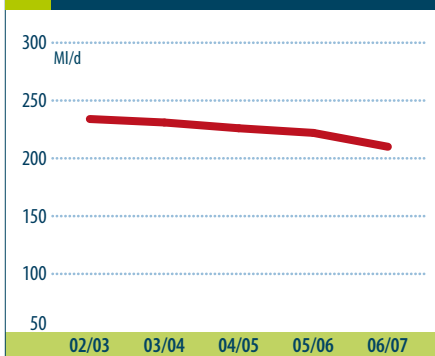
- The Section 19 programme is some £3m less than the FD allowance, primarily due to a reduction in the outputs. The current estimate for the total AMP4 programme is 1,900km against the FD target of 2,557km. We are in dialogue with the DWI with a view to agreeing a new Undertaking. Additionally, we are £1m below allowance on S19 mains cleansing (34km against 902 km in FD). The shortfall arises as a consequence of cleansing being suspended during the dry summer months.
- The WTW quality programme is £3m less than the FD allowance, reflecting delays primarily at Court Farm WTW. Such delays have been agreed with the DWI.
- Total maintenance expenditure is £2m below the FD having caught up significantly during year 2.
- Expenditure on security measures at key sites is £2m behind the allowance as we continue to re-evaluate schemes.
- Expenditure on supply/demand schemes was £5m behind the allowance due to a lower spend on servicing new developments and a lower take up of option meters by customers.
- We have also incurred £2m of late expenditure on AMP3 schemes not included in the FD

29 Capital expenditure by purpose water service

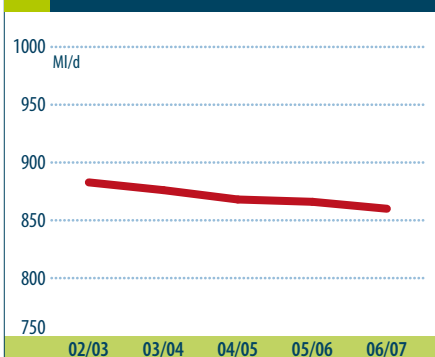
£m	Previous year Capex 2005-06 (Outturn)	Actual Year Capex 2006-07 (Outturn)
Base - Infrastructure	31.1	37.4
Base - Non infrastructure	27.4	42.3
Enhanced service	0.0	0.0
Supply & demand and IDOK	8.8	7.0
Quality and IDOK	36.8	45.2
*Total water service (£m)	104.1	131.9

*Total capex for water and sewerage (2006-07) was £269 million gross of infrastructure contributions and third party costs.

30 Total leakage MI/d



31 Distribution Input MI/d



New assets for development and growth:

- 55km of new water mains were laid during the report year, the vast majority being mains extensions or branch mains to serve new developments. [29](#)

Environmental Performance

- The quality of rivers in Wales continues to be amongst the best in the UK. The last survey of river quality published by the EA confirmed that over 98% of rivers in Wales were good or fair on the assessment of chemical quality and over 99% were good to fair on the assessment for biological quality.

- 99% of EEC designated beaches achieved the mandatory standards.
- 89% of EEC designated beaches achieved the higher guideline standards leading to 49 Blue Flag beaches/marina awards
- Proposals to reduce carbon footprint and expand capacity to generate renewable energy.
- During the report year, there were almost a million visitors to our recreation facilities and 12,500 children visited our education centres.

Leakage

Leakage reduction

- Continuation of leakage identification, repairs and prevention work resulting in a significant reduction in leakage from 224 MI/day to 209 MI/day.
- The rate of leakage was 7.7m³/km/day, down from 8.2m³/km/day in the previous year. This rate of improvement in reducing leakage is ahead of the rest of the sector and on target to achieve our ELL target by 2009-10. [30](#)

Distribution input and water delivered

The amount of water supplied from our WTWs (Distribution Input) has reduced again over the report year as a result of a reduction in the average daily demand for water, which includes lower leakage.

The average distribution input for the report year was 860MI/d. Significant increases in peak demand were observed during the summer of 2006 (up to 40% higher in some zones). We are embarking on a comprehensive programme to promote water efficiency to customers over the coming year, and our efforts to reduce leakage are continuing. [31](#)

Water Efficiency

In February 2007, we launched our 'Be Waterwise' campaign which is designed to inform customers that whilst they can use all the drinking water they need, water is a finite resource and wasting it is bad for the environment. The campaign comprises a number of activities scheduled to take place over the year. In addition, we are working with our main stakeholders to develop a joint water resource communication plan. We are also fully committed to reducing leakage and, having met our targets, encourage customers to report any leaks they see.

Metering

During the report year, nearly 20,800 household customers opted to switch to a measured based charge. A total of 18,753 meters were fitted. Where option meters could not practically be fitted (2040 cases), customers were allowed an Assessed Measured Charge (AMC).

We now have nearly 27% of total billed households on metered charges (of which 1.6% are AMC's).

In addition, in the report year, 7,439 household and approx 7,700 non-household meters were replaced.

Sewerage Service

Wastewater Treatment Works (WwTW)

- 9 identified AMP4 outputs serving a population of 4,824 have been delivered in the report year (6 projects originally identified for year 2, two projects brought forward from later years and one project delayed from year1).
- 13 outputs were identified in the Monitoring Plan, seven have been completed, two brought forward and six have been delayed pending the EA's Review of Consents around the Habitats Directive.
- A total of 92 outputs were delivered in the first two years of the AMP4 period of which 83 are AMP4 schemes against a Monitoring Plan target of 93.

Sludge/Biosolids

- Continuing work at our 36 sludge centres to maintain compliant sludge for agricultural disposal.
- Developing a feasibility project to identify sites for advanced digestion to reduce carbon emissions and mitigate the impacts of fluctuating energy costs.
- All sludge was disposed of satisfactorily. Treated sludge was largely disposed to agricultural land to meet either the conventional or enhanced treated standard and in compliance with the Safe Sludge Matrix. The total figure for sludge, grit and screenings was 85.4 ttds.

Section 101A Schemes

- We have reviewed the benefits of the 23 schemes in our Monitoring Plan.
- The assessment concluded that we would be progressing with only six of the 23 schemes, one of which demonstrates positive cost benefit.

The other five are schemes, where we have a commitment to provide a public sewer.

- Two of the schemes have been completed.

Intermittent Discharges

- 87 schemes have been completed in the report year against our Monitoring Plan target of 94 schemes.
- One AMP3 identified scheme was also completed.
- Cumulative progress to the end of the report year is 155 schemes against a target of 149 schemes.

Environmental Investigations

- 30 investigations for Groundwater and Habitats directives were completed against a Monitoring Plan target of 57 investigations.
- Cumulatively we have now delivered 52 investigations against a target of 66.
- A further 16 investigations are complete, but we are awaiting final confirmation from EA. This will take our cumulative total to 68 against a target of 66.

Sewer Flooding

- 48 properties were removed from the 'at risk register', a further 41 from the '1 in 20 register'.
- Four properties were removed due to better information being available.
- We also tackled 24 external flooding problems.

New sewers and other sewer refurbishment

- 35km of new sewers were laid and 26km of sewers were refurbished in the report year.
- A programme of CCTV surveys continues with 107km of sewers inspected in the report year of which 42km were on the critical sewers.

Sewerage Asset Maintenance

- Work was carried out at a substantial number of sites to improve or maintain asset serviceability and ensure compliance with consents.
- We are required to identify where maintenance investment in the report year has exceeded £5m or is over £100k and 10% or more of the GMEA of the asset.

- There were 10 WwTW sites where these parameters were exceeded. In addition capital maintenance in excess of £100k has been carried out at 42 WwTWs, five sludge centres and six pumping stations during the report year.
- There was one sludge treatment centre site and three pumping station sites where these parameters were exceeded.
- An increase of bursts on strategic mains has led to further investment. For example, Northumberland Road glass reinforced plastic main (GRP) had 4km of 900 diameter of rising main replaced, at a cost of £4.8m.
- The intermittent discharge scheme at Cardiff Western District Pumping Station, valued at £11m, has been deferred until 2008, in agreement with the EA, to allow the necessary environmental impact assessments to be finalised.
- A number of 'misidentified' intermittent discharge schemes have been reprofiled to year 5 in agreement with the EA - valued at £10m. These will be subject to the Change Protocol process.
- Delays in the intermittent discharge programme have been mitigated via the Change Protocol process resulting in the overall achievement of 155 outputs against a Monitoring Plan target of 145 for the 2 years. Clearly, the schemes brought forward have been less complex requiring lower cost solutions.

Capital Expenditure

Actual expenditure in the report year was £130m, some £37m lower than the £167m allowed in the FD (inflated at RPI). The cumulative position for the first 2 years of the AMP4 period shows an overall underspend of £80m. The main variances are explained as follows:-

- Maintenance expenditure on the sewerage infrastructure network is some £7m below the FD. A significant element of this represents analysed maintenance as a result of delays to the quality programme.
- Whilst significantly increasing our year 2 expenditure on above ground maintenance, we remain £16m below the allowance primarily due to delays on odour and sludge schemes, which were re-profiled pending DEFRA guidance and a strategic review aimed at mitigating increased power and energy costs. Delays to the quality programme have also contributed to the analysed maintenance element falling behind.
- Expenditure on the continuous discharge programme is £6m less than the allowance due to five UWWTD schemes being re-phased to later years in agreement with the EA.
- Intermittent outputs within the Llanelli and Cog Moors catchments (valued at £20m) have been delayed in agreement with the EA.

- A total of six Section 101a schemes with a total value of £6m were included in the Monitoring Plan for year 2 completion. Two schemes have been completed at a value of £1m, the remainder being deferred/delayed pending cost benefit analysis.
- Reprioritisation of the DG5 sewer flooding programme has resulted in a delay against FD of £2m.

31 Capital expenditure by purpose sewerage service		
£m	Previous year Capex 2005-06 (Outturn)	Actual Year Capex 2006-07 (Outturn)
Base - Infrastructure	17.0	19.8
Base - Non infrastructure	29.4	47.0
Enhanced service	3.6	6.0
Supply & demand and IDOK	5.5	12.5
Quality and IDOK	72.4	44.4
*Total sewerage service (£m)	127.9	129.7

*Total capex for water and sewerage (2006-07) was £269 million gross of infrastructure contributions and third party costs.

Sustainable procurement

The period April 2006 to March 2007 has seen a consolidation of our supply chain procurement activities. We have continued to develop the contractual relationships with our operations and investment service providers UUOS, Kelda Water Services Wales, Laing O'Rourke, Costain, AMEC, Morrison, Black and Veatch and Imtech. Through the Asset Management Alliance (AMA) established with our operations, investment and billing and income partners, we continue to develop a programme of relationship management aimed at supporting integrated working and the efficient and effective delivery of service to our customers.

In August 2006, we awarded contracts for an initial 5 year period, for information technology supply and Services to Capgemini UK Plc, Logica CMG UK Ltd, and TATA Services Ltd. An Information Technology Centre of Excellence has been formed to successfully deliver and maintain the upgrading and transformation of our IT infrastructure and that of our partners, enabling the business to operate at maximum efficiency.

Following a rigorous competitive procurement exercise, in December 2006, the sampling and analytical services contract was awarded to Severn Trent Laboratories Ltd (Severn Trent) for an initial period of 5 years. Severn Trent will provide services across the whole of our operating area and has joined the AMA supporting the delivery of our business plan.

These appointments were made following competitive tendering processes undertaken in line with European procurement directives and the principles embodied in the British Water 'Sustainable Procurement in the Water Industry' guidelines.

The Supply Chain Business Support Team (SCBST), which operates under the auspices of the AMA and comprises members of both operational and investment partners, has had a successful year awarding framework agreements to tier 1 suppliers in a number of areas including: electrical panels and installation work, pumps, ready mixed concrete, aggregates, coated stone and building merchant supplies.

Although there are individual contracts in place between the AMA partners and the suppliers, the aim is to ensure that a consistent approach to the supply chain in terms of specifications, terms and conditions and associated documentation is taken across the AMA. With the on going development of an AMA web site and portal, all partners will have the facility to access documents associated with the contracts. This will facilitate a consistent, consolidated approach to the supply chain and help alleviate wasted effort and duplication.

Our operations and investment partners have confirmed that their company's procurement procedures encompass the key principles outlined in the guide to 'Sustainable Procurement in the Water Industry' published by British Water. Additionally, all tenderers whether successful or not, are offered feedback on their proposals, providing an insight into the positive and negatives aspects of their submissions.

A number of agreements have been procured in the report year including:

- Pension and Actuarial Services;
- External Audit Services;
- Office Space Planning and Supply of Furniture;
- CMSPS Scope Study;
- Customer Research Services;
- Water Resource Planning Consultants;
- Health and Safety Auditors;
- Legal advice around Pension Services;
- IT Induction Training;
- Study for the Reduction of Flows in Combined and Foul Sewers;
- Strategic Environmental Assessment; and
- Payroll and Accounts payable.

We will continue to follow best practice in our procurement activities. A number of significant procurement exercises will be undertaken over the next year and we are committed to ensuring that we and our AMA partners adopt and assess the key criteria established in the British Water guide to ensure effective utilisation and engagement within the supply chain.

Efficiencies

Cost Comparison 2006-07		£m (2006-07 prices)			
£m (2005-06 prices)	JR 2006.	JR 2005	Change	FD	Variance
Water	115.4	112.8	2.6	122.0	(6.6)
Sewerage	104.5	100.1	4.4	108.2	(3.7)
Total	219.9	212.9	7	230.2	(10.3)

Operating Expenditure

This is the second June Return since the new outsourced contracts with operating partners were awarded. Our primary objectives have remained;

- To promote economy and efficiency in our water and sewerage services.
- To provide strong incentives for continuing improvements in efficiency throughout the business.

Our commitment to working with best in class, blue chip outsourced service providers has supported the delivery of efficiencies in recent years, principally through improved clarity and focus. The table above compares 2006-07's costs to the figure reported at JR06 and also to Ofwat's FD. Our operating expenditure forecast for 2006-07 was around £220m, so our actual performance has been consistent with this, and is also broadly in line with the Final Business Plan.

The increase in costs has principally resulted from ongoing increases in energy costs, which were some £8m (27%) higher than at JR06. The increases in power costs can only be partially mitigated by our efforts to improve working practices and investment in energy efficiency schemes. In addition we have experienced above inflation increases in Governmental charges and ongoing costs due to the Albion Water Competition Appeals Tribunal case.

Efficiencies

By continuing to encourage and support our partners to work collaboratively together, we have sought to consolidate the benefits from the retendering process and new operating agreements implemented during 2004-05. Through this, we benefit from the expertise and experience of highly competent organisations who through a commitment to continuous improvement will share best practice ultimately for the benefit of our customers. We remain committed to progressing over 75 bid initiatives with our operating partners, UUOS, Kelda and Thames Water, ranging from restructuring and integration, through chemical optimisation to site specific projects.

The operating partners remain focused on the delivery of performance improvements over and above the FD targets and systems and processes are in place to monitor their performance. Their contracts operate on a target cost basis which are designed to incentivise ongoing improvements in operating efficiency throughout AMP4.

Despite the increase in operating costs during the report year, our operating partners have undertaken a range of projects that have, had a beneficial impact on operating costs in the report year. A proportion of these savings came from the part-year effect of those projects delivered during the first year of the new contracts.

Voluntary severance programmes have reduced manpower numbers by around 100 in the period. Within the billing and income contract, Thames Water has continued to maintain a highly interactive approach to customer cash collection and its work to mitigate the continuing risk to cash collection posed by increasing bills.

We have sought to obtain additional operating efficiencies through reviewing our use of materials. For example, several small site specific schemes were undertaken with the intention of optimising chemical dosing to better match operational conditions.

Fundamentally, power costs remain the greatest risk to further upward pressure on operating costs. However, together with our partners we have sought to undertake measures to mitigate the impact of this exposure. A variety of projects were commenced during 2006/07 including tariff and triad management, sludge thickening to reduce gas consumption during sludge drying and aeration optimisation. We also undertook a scheme to heat offices on a WwTW from the residual heat in the final effluent with the intention of saving over 75% of the office heating bills. Work on more significant energy schemes also commenced in the report year, including those related to energy generation from bio-gas which we expect to come on-line in 2007-08.

In addition, a competitive retendering exercise for both Information and Communications Technology (ICT) services and labs and sampling were also completed during the year. It is expected that improved operating costs will result. The ICT contract will enable the business to take advantage of technology advances which are fundamental to continuous service improvement and the success of the organisation's ITEC programme. The labs and sampling contract with Severn Trent labs will deliver improved value for money.

Processes and Systems

A significant improvement programme of IT Enabled Change (ITEC) has commenced, led by ourselves. The outputs from ITEC will be new processes supported by the upgrade and replacement of legacy IT systems. This change programme will enhance many of the activities we undertake with our partners. It will deliver improvements throughout the business that will allow us to work in a more efficient manner, providing better service to our customers, whilst collecting relevant data and information to inform our decision making processes. This programme will be integral to the initiatives designed to achieve ongoing efficiency savings for the remainder of AMP4 and beyond. During the report year, this has involved;

- Adding operational assets into SAP to allow operational routines and work activity to be recorded in a single database alongside the mechanical and electrical assets already recorded on SAP.
- Introducing mobile working technology to elements of the work force enabling the field force to receive work directly on their device, avoiding unnecessary trips to depots. In addition, asset data is being improved with collection via the hand held device recorded against a consistent asset hierarchy set up in SAP.
- Creating a dedicated centre for managing operational contact, known as the OAC at our St Mellons site in South Wales. We are now able to monitor customer calls and work progress alongside asset alarms and work dispatch. This process improvement will put a greater focus on complaint management and avoidable repeat calls.

In the coming twelve months, we intend to commence the upgrade of customer reactive work management system in order that customer generated work and customer history is also managed through SAP. This will be integrated with a new geographical mapping system. The integration of these systems will provide easy access to customer, work and asset information to those carrying out excavations and repairs in the field and teams in the centre managing customer contact and work scheduling.

Making use of the improved asset data will come over time through better management information provided via SAP Business Information systems and the implementation of the Strategic Investment Planning System (SIPS), where asset management decisions will be made based on historical and forecast information for cost, risk and performance.

Capital Expenditure

The water and sewerage capital programme for AMP4, allowed in the FD, is approximately £1.3 billion (inflated at RPI). Our total capital expenditure during the first two years of the five-year AMP4 period is £507m which equates to some 38% of the total programme. We continue to progress delivery of the investment programme at a cost broadly in-line with the FD allowance. However, as we have noted, a number of challenges remain.

The construction costs of investment schemes remain under upward cost pressure and efforts are being directed at mitigating the impact of such factors through rigorous review. Increasing materials costs and emerging resource constraints will also provide challenges moving through the AMP period. For example in recent months, we have experienced the loss of some 40 skilled mains laying personnel from the Section 19 programme due largely to the LNG pipeline project in south Wales.

The programme is also now addressing some more complex schemes in more urban locations than previously, requiring a the reappraisal of the design and planning of schemes and programmes to achieve reductions in unit costs which were assumed by Ofwat in the 2004 Price Review. However, having secured the services of the partners for a long-term programme and constantly reviewing working methods, designs and costs, we consider there will be the opportunity to benefit from further efficiency improvements. For example, we continue to assess working practices to identify and eliminate any instances of low productivity, duplication, high error rates, wastage and bureaucracy.

We also extended the AMP4 owner controlled Construction Insurance programme to all relevant partners and this helped deliver efficiencies and establish streamlined procedures.

Last year we stated that it was our ambition to achieve efficiency savings in the delivery of the programme by absorbing the difference between COPI and RPI inflation. This remains our goal. However, our experience during the first two years of the programme shows that the cost of investment schemes are facing significant upward pressures, particularly in the water programme. As a result, it is increasingly likely that we will only partly achieve our original efficiency savings goals.

Competition

Water Act 2003

Our Access Code was revised and published in October 2006. A further version is due to be published shortly. We will also be reviewing our Indicative Access Prices. We have been negotiating a wholesale master agreement with a licensed water supplier. Agreement has been reached on the majority of the terms. However, progress has been affected by difficulties in agreeing some of the clauses, which have been recognised in the general Ofwat competition review as 'contentious clauses.' Further guidance covering these points is due from Ofwat and we have contributed to the consultation on this revised guidance.

Albion Water

In 2000, Albion Water Limited (Albion) made a complaint under the Competition Act 1998 (the CA 98) to Ofwat regarding the terms we had offered to Albion for access to our distribution and treatment infrastructure to supply water to Albion's customer, the Shotton Paper Mill. In 2004 Ofwat concluded that Welsh Water had not breached the CA 98.

Albion commenced proceedings against Ofwat in the Competition Appeal Tribunal (the CAT) for allegedly failing to enforce and observe the requirements of the CA 98. We intervened in the case in support of Ofwat.

The CAT has now given two substantive judgments in the case. These have found us guilty of abusing a dominant position in contravention of Chapter II of the CA 98 and of having engaged in margin squeeze.

However, to finalise the case the CAT considered it necessary to refer back to Ofwat for further investigation the matter of the costs reasonably attributable to the service of the transportation and partial treatment of water by us, generally and through the Ashgrove system in particular. They also referred back the associated question of whether, in the light of those costs, the access price offered by us was an unfair price within the meaning of the CA 98. Ofwat is currently undertaking this investigation and is due to report back to the CAT by 18th June 2007.

We have sought permission to appeal the CAT judgments. This was refused by the CAT and our written appreciation for leave was subsequently rejected by the Court of Appeal. However, we will now be seeking permission to appeal at an oral hearing before the Court of Appeal.

Inset Appointments

There have been no new inset appointments during the report year.

Board

endorsement

The Company has established processes and systems of internal control for ensuring the reliability, accuracy and completeness of the information provided in the June Return, which are summarised below.

Policies and procedures

- Subsequent to the June Return 2006 submission, Grant Thornton was asked to undertake an audit evaluating the systems utilised within the business for the completion of that Return. This involved documenting key processes and internal controls and Grant Thornton assessing the quality of systems and processes used for generating regulatory information. The conclusion of this study found that the systems of control were largely satisfactory.
- A process mapping exercise was undertaken by Grant Thornton, which expanded on initial work undertaken following receipt of MD220. Internal reviews of key subject areas helped prioritise this exercise. The outputs of this were detailed process templates documenting internal methodologies and controls. During the report year, a number of written methodologies and process documentation for selected June Return tables were produced. This was supplemented by procedure notes, produced by individual table owners (where necessary), ahead of the full suite of methodologies and process documentation being completed by Grant Thornton. These have proved to be valuable points of reference for this June Return when compiling data, reviewing outputs and undertaking due diligence.
- Publication of our policy document for the June Return (the 'Process for the Welsh Water June Return'). This outlined the formal process to be undertaken and, inter alia, the roles and responsibilities of key people including line owners, table owners, the Regulation Department, Welsh Water Executive (collectively and individually), the Audit Committee and the Board. This document was circulated internally and sent to everyone directly involved in the June Return process. This ensured that all parties involved in the process were aware of their specific requirements prior to commencement of the process;
- Where new table owners have assumed responsibility for analysis and compilation of data for the June Return, transition arrangements were put in place ensuring continuity and that the transfer of responsibility was robustly managed. In addition, training and familiarisation of staff involved in the process (particularly those involved in the June Return for the first time) was undertaken to ensure that they were reminded of the Company's obligations under MD209 and the importance of submitting reliable, accurate and complete regulatory data.
- The Company's 'Whistle-Blowing Policy' was reissued as part of the Welsh Water Compliance for Staff booklet with its importance re emphasised, both to Welsh Water staff and those of service providers.
- Maintenance of a culture of openness within Welsh Water and right across the AMA, where issues can be discussed and any concerns raised without fear of criticism or recrimination.
- The establishment of a clearly defined organisational structure for completion of the June Return with appropriate delegated authorities and clearly defined allocation of responsibilities, all co-ordinated and managed by the Regulation Department.
- Clearly delegated ownership and responsibility for each line of each regulatory table. These individuals were responsible for adhering to all appropriate guidance in the compilation of the data and associated

commentary. This also involved formal 'sign off' by the individual, verifying that the figures in each line had been obtained from a recognised and verifiable data source and had been accurately compiled. In addition, confirmation was required that any material judgements or assumptions had been stated, ensuring where appropriate an accurate audit trail and a review of confidence grades where applicable;

- Clearly delegated ownership and responsibility for each regulatory table. These individuals were responsible for adhering to all appropriate guidance in the compilation of the table and associated table commentary. This also involved formal 'sign off' by the individual, verifying that the figures in each table had been obtained from a recognised and verifiable data source and had been accurately compiled. In addition, confirmation was required that any material judgements or assumptions had been stated, ensuring where appropriate an accurate audit trail and a review of confidence grades where applicable.
- Allocation of overall responsibility for particular tables and associated commentaries was assigned to the appropriate Welsh Water Executive member. They were responsible for review and 'sign off' of the table(s) and commentary.

Implementation and Internal Review

- Production of 'June Return Table Packs' by the Regulation Department ensured that all table owners had a single point of reference for all information necessary to undertake their specific responsibilities. This information was also maintained on the Welsh Water Regulation Department intranet site for reference. These 'Packs' included the Reporting Requirements for each table, any subsequent points of clarification

issued by Ofwat, queries received on the previous June Return with the Company response, any Company specific guidance to Reporters and information on confidence grades. They also indicated the assurance ('sign-off') processes applicable to the line owner, table owner and the responsible member of the Welsh Water Executive Team.

- Regular communication between the Regulation Department and all line and table owners was undertaken prior to and during the preparation of the June Return. This included scheduled meetings which reviewed Reporting Requirements, discussed the audit plan, individual progress towards completion, and considered due diligence matters.
- During the report year, a programme of mid-term audits and ongoing dialogue with the Reporter was undertaken to ensure that issues were identified and highlighted at an early stage. We can report that no significant issues were raised via these audits during the report year.
- Regular reporting of key performance indicators throughout the report year to the Board, the Quality and Environment Committee (QEC) and Senior Management Team.
- A rigorous process of internal due diligence meetings was undertaken by the Regulation Department between the 15th May and 8th June, to challenge information, judgments, assumptions made and ensure compliance with all necessary regulatory guidance. Particular scrutiny was undertaken of those subject areas which Ofwat had highlighted as requiring improvement at the previous June Return.
- A review was undertaken by the Regulation Department to ensure consistency between the Overview and the individual tables and commentaries.

- The internal letters of compliance were endorsed by each line owner, table owner and responsible member of the Welsh Water Executive before the June Return was submitted to Ofwat. All completed process maps were also signed off before the submission of the June Return.
- Process review meetings, involving Welsh Water Executive, took place on 30th May, 5th June and the 12th June 2007 (the latter meeting also attended by the Reporter and the Auditor). They scrutinised each table together with progress reports on the internal challenge and 'sign off' processes, highlighting and discussing any relevant issues.

External Review and Board Engagement

- Grant Thornton's involvement in the review of processes meant that there was a rigorous independent evaluation of the procedures in place.
- Formal review and certification of the June Return by the external Reporter and Auditor. The Reporter and Auditor also attended the June Board Meeting and provided a briefing on the results at that stage of their oversight process;
- Formal Audit Committee and Board review of the June Return process and progress in the implementation of these processes. The processes were reviewed and approved at the Board meetings held on 2nd February and 8th March 2007 and at the Audit Committee meetings on the 1st February and the 26th May 2007.
- At its June meeting, the Board received reports from management, Grant Thornton, the Reporter and the Auditor on the implementation and review of the June Return process which it had approved at its earlier meetings. The Board also reviewed and endorsed the Board Overview document.

As part of the June Return process, each Director has confirmed, as at the date of the Board Overview, that as far as the director is aware, there is no relevant audit information of which the Company's Auditor or Reporter are unaware. The Directors have also taken the steps to make themselves aware of any relevant audit information and to establish that the Company's Auditor and Reporter are aware of that information.

The Board met on 8th June 2007 to review the overall June Return process and the operation of the process and systems of internal control as highlighted above. On this basis, the Board were satisfied that these processes provide the necessary degree of assurance that the information reported in the June Return was of the standard that can reasonably be expected of a water and sewerage company complying with its regulatory obligations.



Terry Burns
Chairman



Nigel Annett
Managing Director



15 June 2007