

SEVERN TRENT PLC  
ANNUAL REVIEW 2004



THIS IS SEVERN TRENT

Severn Trent Plc is a leading environmental services group providing water, waste and utility services. We aim to increase shareholder value by providing integrated solutions to environmental problems; and by grasping the growth opportunities created by new legislation and new requirements in the private and public sectors.

Firmly embedded in our corporate strategy is a commitment to corporate responsibility and sound financial management.

You can find out more about Severn Trent Plc and the businesses within our group by visiting our website [www.severntrent.com](http://www.severntrent.com)

#### **Annual Report and Accounts 2004**

You can view and download a copy of the group's Annual Report and Accounts on our website at [www.severntrent.com/reports2004](http://www.severntrent.com/reports2004) or request a copy free of charge by contacting us using the details on the back cover of this report.

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## HIGHLIGHTS

## DIVIDEND

Final dividend of 29.27p bringing the total for the year to 47.04p

## GROUP TURNOVER

Up 8.8% to £2,015.1m (£1,852.0m)

## GROUP PROFIT BEFORE INTEREST, TAX, GOODWILL AMORTISATION AND EXCEPTIONAL ITEMS\*

Up 7.5% at £440.6m

\*Goodwill amortisation £29.8 million and exceptional items of £11.6 million.

## EARNINGS PER SHARE

53.5p (28.9p); before exceptional items and deferred tax 61.4p (58.1p)

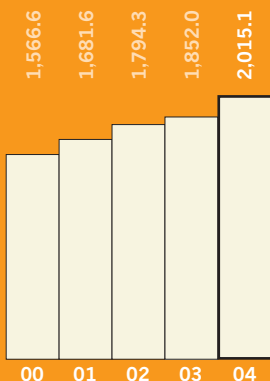
## CUSTOMER SERVICE AND QUALITY

UK's top performing water and sewerage company in Ofwat's 2002/2003 Overall Performance Assessment

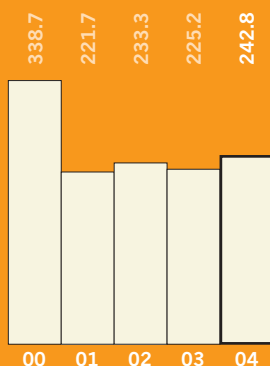
## LEADERSHIP

We hold market leadership positions in the UK waste market and in environmental testing in the US and the UK

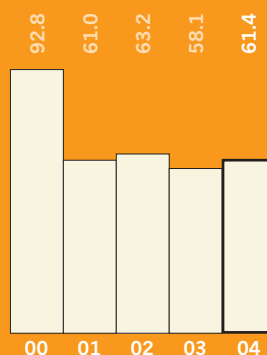
Group turnover  
£m



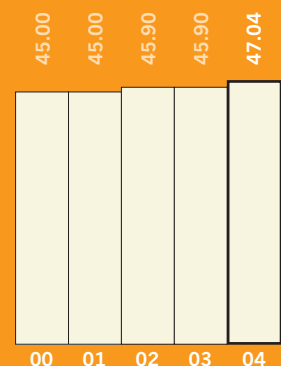
Group profit before tax  
before exceptional items  
£m



Earnings per share  
before exceptional items  
and deferred tax  
pence



Dividends per share  
pence



## CHAIRMAN'S STATEMENT

- Good full year results
- Increased overall profits from non-regulated businesses
- Severn Trent Water continues to outperform

Group profit before interest, tax, goodwill amortisation and exceptional items\* up 7.5% at

# £440.6 million

\*Goodwill amortisation £29.8 million and exceptional profits of £11.6 million.

We have enhanced our dividend policy such that, barring unforeseen circumstances, full-year dividends per share would be a minimum of 47.04p up to the end of the current review period in March 2005.

### Business performance

Severn Trent produced a good performance in 2003/2004. Excluding the impact of exchange rates, turnover rose in all the core businesses of water, waste and laboratories. We have worked hard to balance the expectations and needs of different parties – employees, customers, investors, regulators and communities. Sound day-to-day management is combined with a long-term commitment to sustainability.

Much of our management focus over the year has concerned the preparation of our draft and final AMP4 business plan for Ofwat, setting out our proposed investment plans for 2005-2010. We are confident in our ability to meet new targets for this period, just as we are confident that we will continue to outperform our AMP3 regulatory contract. In respect of 2002/2003 Severn Trent Water has the leading position in Ofwat's Overall Performance Assessment (OPA) of water and sewerage companies. Our charges are also among the lowest in the UK and, under current plans, will be the lowest by 2010.

Whilst developing the future strategy of our regulated business we have pressed ahead with developing Biffa as one of the leading waste management companies in the UK - the biggest event during the year being the acquisition of the former Hales business.

Severn Trent Water and Biffa are sharing expertise and technology in wastewater disposal and energy generation; and Biffa is using Severn Trent facilities in its important integrated management contract for Leicester City Council. We expect such synergies to create further opportunities in the future.

Services delivered good profits in 2003/2004. Severn Trent Laboratories developed its capabilities in several new fields including mould; Severn Trent Services benefited from the management actions taken in 2002 in the Water Purification business.

Reflecting our commitment to environmental leadership, Severn Trent was named as the leading utility in the Dow Jones Sustainability Index for the third consecutive year. This is the first time that any utility has won this category three times in a row.

### Group results

Group turnover was £2,015 million, an increase of 8.8% over last year. The turnover of the non-regulated businesses increased by 12.7% to £1,161 million, representing 54.8% of the Group total. Turnover from water and sewerage increased by 4.2% to £957 million. Group profit before interest, tax, goodwill amortisation and exceptional items was up 7.5% to £441 million. The water and sewerage business was up by 3.8% to £338 million. The Group's non-regulated businesses in total were up 18.1% to £123 million, representing some 27% of the Group total.

Group profit before interest, tax and exceptional items was £411 million (£385 million). Group profit before interest and tax was £422 million (£344 million).

The Board is proposing a final dividend of 29.27 pence (28.56 pence) to be paid on 1 October 2004. This would give a total dividend for the year of 47.04 pence, an increase of 2.5%. It is the Board's intention that for the period up to 31 March 2005, barring unforeseen circumstances, full year dividends per share would be a minimum of 47.04 pence.

For the period of AMP4 (from 1 April 2005), the outcome of the AMP4 price review will be a critical input in the determination of the Group's dividend policy. Accordingly, the Board intends to consider its dividend policy for the period from 1 April 2005 to 31 March 2010 following the finalisation of the AMP4 price review.

Based on SSAP24, the Group expects a significant additional pension charge in 2004/2005 that is provisionally estimated to be of the order of around £30 million to £35 million (net of amounts allocated to own work capitalised), with broadly around two thirds to three quarters of this amount expected to be attributable to Severn Trent Water. However, given the preliminary nature of these estimates it is



quite possible that the actual additional pension charge, as a result of these valuations, could be materially different from these estimates. (See Financial Review – pensions.)

#### **Management and staff**

Robert Walker will reach retirement in February 2005, having completed nearly six years as Group Chief Executive. His contribution and legacy are considerable.

We are delighted that Robert's successor will be Colin Matthews who joined the Board as a non-executive director in October 2003. Colin has already had a distinguished career at Transco, British Airways and Hays where he has been Chief Executive for the last two years. We are very fortunate to have secured a man of his talents as our leader for the next few years.

Alan Perelman will be retiring as Group Finance Director as of 31 August 2004 and will be replaced by Mark Wilson currently Director of Finance and Regulation in Severn Trent Water. I would like to thank Alan for his dedicated service and wish him well in his retirement.

Brian Duckworth has decided to stand down as Managing Director of Severn Trent Water and from the Severn Trent Plc Board at the end of August but he will continue as an employee of the group until he leaves in March 2005 thus ensuring his expertise is available to help complete the regulatory process for the AMP4 review. Brian has served Severn Trent for 30 years with distinction and we thank him for his outstanding contributions to the group and the water industry, not just in the Midlands but nationally and internationally as well.

Three new non executive directors, Martin Houston, Colin Matthews and John Smith are already making a positive impact on the Board's work. We were sorry to lose Eric Anstee following his appointment as Chief Executive of the Institute of Chartered Accountants. We thank him for his contribution to the Board's work, not least as outgoing Chairman of the Audit Committee.

John Smith took over chairmanship of the Audit Committee from Eric Anstee; the Environment Committee has been renamed the Corporate Responsibility Committee to give a truer reflection of its work, and from now on it will always be chaired by the Group Chief Executive. The former chair, Derek Osborn, is still playing a leading role on that committee.

Marisa Cassoni stepped down as a pension trustee, and we are grateful for her valuable contribution during a time of change in the pensions arena. I would also like to thank Martin Flower for his continuing work as Chairman of the Remuneration Committee and as Senior Independent Director.

I am sad to say that I shall be standing down as Chairman as of 31 December 2004 after nearly nine years on the Board. I expect my successor to be appointed well before then.

Naturally, my thanks must also go to the staff of Severn Trent businesses all over the world. Our continuing ability to meet our objectives and serve our stakeholders is due to their hard work, commitment and levels of expertise.

#### **Outlook**

Although the Group expects significant additional pension charges in 2004/2005, we consider that, overall, our core businesses – Severn Trent Water, Biffa and Laboratories – in terms of experience, market position, financial strength and reputation provide a good platform for the future, with the Group well positioned to capitalise on opportunities. Clearly, the future will also bring challenges. Sound management and cost control will therefore remain a key element in our strategy for consolidating our position as the UK's leading integrated environmental services business and increasing shareholder value.

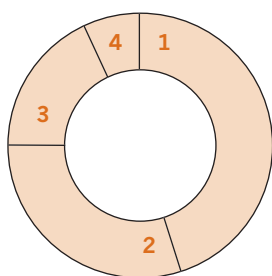
**David Arculus**  
Chairman

## GROUP CHIEF EXECUTIVE'S REVIEW

Group results are ahead of a year ago and our core businesses – water, waste and laboratories – are in good shape. These three businesses accounted for 83% of Group revenues and over 90% of Group Operating Profit.

### Turnover by business

% of group total in 2003/2004



1	Water	45%	£956.7m
2	Waste	30%	£633.1m
3	Services	18%	£381.2m
4	Others	7%	£147.1m

Our aim is to establish Severn Trent as the UK's leading supplier of environmental goods and services, and as a major provider of environmental solutions to the large and growing US market.

I am pleased to report a good all-round set of results for my last full year as Group Chief Executive. Our success has been achieved by concentrating on our five strategic fundamentals:

- Giving priority resources and management attention to the core businesses of water, waste and laboratories
- In terms of acquisitions, focusing significant attention on UK waste, with smaller or bolt on acquisitions in laboratories
- Improving or disposing of underperforming assets
- Driving for cost reduction and operating efficiencies in all businesses
- Exploiting Group synergies, in areas like business-wide cross selling initiatives, and better integrating the Group's purchasing, human resources and operating assets

### Water

Severn Trent has benefited from the price increase from December 2002's successful interim price determination (IDoK) and also from continuing efforts and initiatives to manage costs and control upward pressures in the business.

Water remains firmly on track to out-perform against its regulatory contract for the current five year period and meet its own stretching targets. On the operating expenditure front, we're confident of achieving £75 million of gross operating cost efficiencies by the final year, 2004/2005. Ofwat's target was £62 million.

The business continues to deliver efficiencies against its £2 billion investment programme and we're confident we will deliver average capital expenditure efficiencies of around 5% over the AMP3 period,

measured against the RPI Index. We are on track to deliver all our capital investment obligations.

Our final business plan as submitted to Ofwat for the next five year period aims to achieve the right balance between customer and investor expectations. Our ambition is to deliver noticeable service improvements to our customers whilst maintaining household bills that deliver value for money. At the same time we aim to achieve appropriate financial returns to our investors – all of this, of course, against a background of financial prudence and careful balance sheet management.

For the average bill our final business plan would mean an increase of £57 per household by 2009/2010 in real terms. On the basis of all the plans submitted to the Regulator, this would leave Severn Trent with the lowest average household bill for any water and sewerage company by 2009/2010.

### Waste

We are now starting to see legislative and regulatory change impacting on the way we handle and treat our waste.

In the industrial/commercial sector where the waste generated represents 79% of the UK's total waste tonnage, tighter packaging regulations are being implemented. To help customers, Biffa has a well established compliance scheme called Biffpack that has seen membership grow by 10% in the past year.

The Landfill Directive requires 65% of bio-degradable municipal waste to be diverted from landfill by 2020. Responsibility to ensure this happens has been assigned to each Waste Disposal Authority and 25 year PFI treatment and disposal contracts are now being let, with Biffa well placed to compete for them.

Biffa is well positioned to take advantage of these future opportunities, particularly now that the acquisition of Hales has firmly established Biffa as one of the largest integrated waste management companies in the UK.

Against this industry framework, Biffa has achieved a solid overall result, particularly in light of the uncertain economic background. This reflects the strength of Biffa's management and its integrated – Collection, Landfill and Special Waste – business model.



### Services

Excluding the impact of exchange rates, turnover and profit before interest, tax and goodwill amortisation improved. This satisfactory result principally reflects the P&K mould testing acquisition in April last year, which has enhanced our core laboratories business and also the significant management actions taken in 2002/2003 in our Water Purification Division to rationalise and improve the cost base and re-focus the business in growth segments.

Severn Trent Laboratories continued to drive forward with its core strategies of firstly, maximising the base business share in the traditional, routine environmental testing areas by low cost, high quality service turnround and secondly, expanding into higher growth, more attractive new areas of testing such as mould, and specialist microbiology.

Our remaining US businesses, Water Purification and Operating Services, made significant strides over the year, probably the most progress of any of our businesses.

Water Purification particularly has made significant improvements. This partly reflects the downsizing in 2002 and more effective IT systems and manufacturing processes, but most recently it reflects more aggressive and targeted sales efforts behind new and higher margin products and technologies.

The Operating Services business continues to strengthen. Contract Operations has delivered organic growth in revenue and we believe this is now the third largest business of its type in the US. The division is currently bidding on \$200 million of new business potential in the next six months in addition to the recently signed \$65 million Fresh Kills Landfill contract in New York.

### Core Businesses

We are confident that our core businesses of water, waste and laboratories are in fine shape to take the group forward. They each share common characteristics of leadership, scale and low cost advantage; among the best management teams in each sector; consistent strong past performance and long-term opportunities for profitable growth.

### Outlook

The past year's results have clearly benefited from a focused strategy, disciplined management and tight cost controls throughout the business and we are confident that we have the right platform for the future.

As this is my last report as Group Chief Executive I must stress that everything Severn Trent has achieved has been made possible by the enthusiasm and skill of all my colleagues. I shall miss them greatly but I know they will give my successor the same excellence and dedication which will serve the Group well in the future.

**Robert Walker**  
Group Chief Executive

## CORE BUSINESSES AT A GLANCE

Severn Trent generates revenues of £2.0 billion and employs over 15,000 people across the UK, US and Europe. We are increasingly focused on the industrial and commercial sectors to help business customers meet environmental objectives.

## Business

## Key strengths

## WATER



**Severn Trent Water** provides essential water and sewerage services to around 3 million households in England and Wales. It also provides products and services to business customers in its region. It has a good track record on service levels, gross operating cost efficiencies and quality, and environmental compliance.

For further information please visit [www.stwater.co.uk](http://www.stwater.co.uk)

- Track record of outperforming regulatory contract
- Strong management structures and cost controls
- Good account management for business customers
- Excellent customer service, quality and biodiversity record

## WASTE



**Biffa** is one of the UK's largest integrated waste management businesses, providing collection, landfill and special waste services to local authorities and industrial/commercial clients. It has around 90,000 customers, and an infrastructure that includes 34 operational landfill sites and 13 special waste treatment facilities. It also has 11 operational facilities in Belgium.

For further information please visit [www.biffa.co.uk](http://www.biffa.co.uk)

- Specialist fleet achieving high levels of fuel and operational efficiency
- Over 30 landfill sites with good geographic coverage and high environmental standards
- Special waste solutions based on innovation and new technologies
- Strong IT infrastructure delivering synergies and efficiencies
- Good strategic partnerships in recycling

## LABORATORIES



**Severn Trent Laboratories (STL)** is the largest environmental testing company in the world, providing environmental analysis services in the US and the UK. It has 31 laboratories and 21 service centres in the US, and 4 laboratories and 1 service centre in the UK.

For further information please visit [www.stl-inc.com](http://www.stl-inc.com) [www.stl-analytical.co.uk](http://www.stl-analytical.co.uk)

- Record of innovation and being at the forefront of new markets
- History of successful acquisitions and organic growth
- Reputation for good customer service
- Client list of leading US and UK companies

**Performance highlights**

- Turnover up 4.2% at £956.7 million
- Top-performing water and sewerage company in Ofwat's latest Overall Performance Assessment
- Total AMP3 gross operating efficiencies of some £69 million, £17 million more than Ofwat targets
- Started £16 million programme to generate 13% of annual energy needs from renewable resources

**Outlook**

In December 2004, Ofwat will announce the final determination of its AMP4 price review for the years 2005-2010. Until this is finalised, there is some uncertainty about the outlook for all water companies. However, Severn Trent Water is well on track to outperform Ofwat's AMP3 targets for the five year period to 2004/2005. It is also well positioned to benefit from the new competition framework for large customers, which comes into operation for 2005.

- Turnover up 23.9% at £633.1 million
- Acquisition of Hales strengthens position as one of the UK's largest waste management companies
- Extended contracts with local authorities, working towards achieving new recycling targets
- Boosted capacity to generate power from landfill gas to around 90MW in the UK

Legislation and taxation will drive demand in the UK for alternative methods of waste disposal in the UK. Aided by its experience in Belgium, Biffa is in a strong position to capitalise on this. Its expertise in special waste will also help it use the openings created by the Landfill Directive in the UK.

- In local currency, turnover in the US up some 8%, and in the UK up 2%
- Acquisition of P&K, a microbiology business with a high profile in the growing market for indoor air quality testing in the US
- Acquisition of Aerotech strengthens presence in south-western US, and puts STL at forefront of markets for indoor air quality, food microbiology, and industrial hygiene
- Opening of new service centres in US extends geographical strength

The STL strategy to be a leader in high-end markets continues to present new opportunities in emerging markets such as indoor air quality and mould, food microbiology, endocrine disrupters, and perchlorate testing. In the US, legislation concerning harbour infrastructure and dredging cleanup also positions STL favourably for the high growth market of sediments analysis. In the UK, EU legislation like the Water Framework Directive, the Groundwater Directive, and the Landfill Directive will create new openings for growth.

For information on our other businesses visit the following websites:

Severn Trent Services [www.severntrentservices.com](http://www.severntrentservices.com)  
 Severn Trent Water International [www.stwaterinternational.com](http://www.stwaterinternational.com)  
 Severn Trent Systems [www.aseriti.com](http://www.aseriti.com) / [www.worksuite.com](http://www.worksuite.com)

Severn Trent Retail Services [www.stretailservices.co.uk](http://www.stretailservices.co.uk)  
 Severn Trent Utility Services [www.stutilityservices.co.uk](http://www.stutilityservices.co.uk)  
 Severn Trent Property [www.severntrentproperty.com](http://www.severntrentproperty.com)  
 Charles Haswell and Partners [www.haswell.co.uk](http://www.haswell.co.uk)

## SUMMARY REVIEW OF OPERATIONS

### WATER

Severn Trent Water achieved another good performance in 2003/2004 building on the strong foundations we have put down in previous years. We remain well positioned to outperform our Ofwat targets for the period 2000 to 2005.

Turnover up 4.2% at  
**£956.7m**

Profit before interest, tax, goodwill amortisation and exceptional items\* up 3.8% at  
**£337.9m**

\*Goodwill amortisation £1.3 million and exceptional profits of £19.8 million.

### Performance

In 2003/2004 turnover from water and sewerage services increased by 4.2% to £956.7 million. Contributing to this rise in turnover were the price increases resulting from the IDoK of December 2002, in which Ofwat allowed our request to raise prices by 2.1% above inflation from April 2003. The IDoK increase benefited turnover by some £19 million. In addition increased consumption by metered customers during the dry hot Summer is estimated to have added some £2.5 million to turnover in the year.

Profit before interest, tax, goodwill amortisation and exceptional items was up 3.8% to £337.9 million. Goodwill amortisation was £1.3 million (£0.1 million), and profit before interest, tax and exceptional items, was £336.6 million (£325.4 million). Including an exceptional profit of £19.8 million from the sales of land and property, profit before tax and interest was £356.4 million (£325.4 million). Given its magnitude, the profit from the sale of fixed assets of £6.7 million was not treated as exceptional in 2002/2003. There was an additional pension charge (net of amounts allocated to own work capitalised) of £1.8 million for water and sewerage to reflect the valuation of pension schemes (see Financial Review – pensions).

### Outperforming the regulatory contract

Our programme for delivering gross operating cost efficiencies, in line with Ofwat's AMP3 targets for 2000-2005, continued to make good progress. At 31 March 2004, total AMP3 gross operating cost efficiencies amounted to approximately £69 million, some £17 million more than our Ofwat target.

In 2003/2004 we invested approximately £442 million in programmes to improve drinking water quality, the effluent from our sewage treatment works and a range of customer service improvements. We continued to deliver efficiencies against our investment programme of approximately £2 billion for the 5 year period.

### The 2005-2010 price review

A critical activity in 2003/2004 was the preparation of our strategic business plan for AMP4, Ofwat's fourth asset management plan since privatisation, which covers investment and prices for the period 2005-2010. In drawing up our business plan, we have had



**Levels of service**

Severn Trent Water is the UK's top performing water and sewerage company in Ofwat's Overall Performance Assessment



to balance often conflicting pressures and expectations on price levels and investor returns; environmental and customer service improvements; efficiency and operational risk. Ofwat will make an interim determination on AMP4 in August 2004, and a final determination in December.

**Water supply**

Low Autumn rainfall in 2003 meant that the year was one of the driest on record. As a result some of our reservoirs were less than 60% full at the start of winter. However, we maintained water supply to all our customers.

In July 2003, we changed the way we collected data on water consumption by our customers; based on this and other new information we recalibrated our total leakage on the company's and customers' pipes. We worked with Ofwat to establish new leakage targets for March 2005, and we have started to put in place improved monitoring systems to measure losses.

**Competition and commercial customers**

The Water Act 2003, which came into force in November, set a framework for introducing competition in the water industry for business customers using more than 50 mega litres of water a year. We look forward to the arrival of competition in 2005, and we are confident that we can offer an excellent product range and account management to business customers inside or outside our region.

**Environment and community**

Corporate responsibility is firmly embedded in Severn Trent's business, and we recognise that our work has a significant

impact on the environment and communities of the Midlands. We support hundreds of projects across the region, all with a sustainability agenda.

Energy management is an important aspect of our commitment to environmental leadership. In 2003/2004 we embarked on a £16 million programme that will enable us to generate 27 megawatts of power, more than 13% of our energy needs, through new CHP units.

**Outlook**

The AMP4 pricing review is enormously important to the outlook for Severn Trent Water. We are confident that the regulators understand that Severn Trent has achieved significant efficiencies in its work but that further investment is still needed. It is widely understood that prices for customers will have to rise, but the average household water bill in the Midlands will still be among the best value in the country.

Our record against all the current AMP3 regulatory contract and on Ofwat's Overall Performance Assessment, combined with the opportunities that competition will create, gives us a good platform for the future.

**CASE STUDY****OUTPERFORMING OUR SECTOR ON SERVICE AND QUALITY**

Ofwat's most recent Overall Performance Assessment for 2002/2003 showed Severn Trent Water was the UK's top-performing water and sewerage company. In 2003/2004 we have maintained, and improved, the quality of our service to customers.

**New technology**

Improving customer service and efficiency by delivering information direct to employees wherever they are working

Each year Ofwat publishes a report on the levels of service provided by water companies to their customers. The report includes an Overall Performance Assessment (OPA) which compares companies' performance on measures like water supply, sewerage services, customer service and environmental impact. It is thus an extremely important gauge of the quality of service that companies are delivering.

The most recent OPA was published in March 2004, and evaluated companies' performance in 2002/2003. We were delighted that the assessment showed Severn Trent Water to be the UK's top-performing water and sewerage company, once our revised leakage targets had been taken into account.

Although the assessment covers the previous year, we are confident that we maintained the quality and efficiency of the service we deliver.

Indeed we improved on it in 2003/2004.

Two IT projects implemented in 2003/2004 contributed to improved efficiency and customer service. The first uses mobile technology to improve the efficiency of Severn Trent's mobile workforce, by delivering information such as job details, location maps, biodiversity plans, and health and safety information direct to their laptop computer.

The second – Integrated Customer Experience or ICE – improves customers' experience when they phone our operations call centre. Information from different systems is presented to customer service agents in a single, intuitive format, enabling them to complete customer requests more quickly and efficiently.

## SUMMARY REVIEW OF OPERATIONS

### WASTE

The two main stories in our Waste business in 2003/2004 were the acquisition of Hales and the way that legislation has continued to create new opportunities in all areas of the business – collection, landfill and special waste. The Hales' acquisition means that Biffa is now even better placed than previously to capitalise on these new opportunities.

Turnover up 23.9% at  
**£633.1m**

Profit before interest, tax, goodwill amortisation and exceptional items\* up 16.6% at  
**£79.2m**

\*Goodwill amortisation £21.3 million and exceptional costs of £10.9 million.

### Performance

Waste management's turnover increased by 23.9% to £633.1 million, benefiting from the contribution of Hales' turnover. Turnover in the UK rose to £573.9 million, an increase of 25.5%; Belgian turnover rose by 10.4% to £59.2 million. Biffa's profit before interest, tax, goodwill amortisation and exceptional items was £79.2 million, up 16.6% on the previous year. Goodwill amortisation was £21.3 million. There was an exceptional charge for Hales integration costs of £10.9 million. There was also an additional pension charge of £1.8 million for waste management to reflect the valuation of pension schemes (see Financial Review – pensions). Profit before interest and tax was £47.0 million.

On 19 June 2003 Biffa acquired Hales from RMC (UK) Limited for approximately £126 million and paid approximately £15 million (exclusive of VAT) to ING to purchase vehicles and equipment used in the Hales' business, being a total consideration of approximately £141 million (excluding transaction costs). Biffa targeted synergies of around £7.5 million per annum (in terms of run rate) from the integration of Hales. The integration process has gone well and is now close to completion. In 2003/2004, Hales contributed (including synergies) an estimated £10.4 million to waste management's profit before interest, tax, goodwill amortisation and exceptional items. Excluding the impact of acquisitions (Hales £10.4 million, other acquisitions £0.2 million) and of increased pension charges, waste management's profit before interest, tax, goodwill amortisation and exceptional items was up by 3.7% compared to last year. The results for the year include the cost of settling legal disputes and insurance credits (of a broadly similar scale). These items have been allocated to UK central costs so as to provide more comparable figures, year-on-year, for the three UK business units of Collection, Landfill and Special Waste.

### Collection

Biffa's Collection division works with around 90,000 industrial/commercial customers across the UK, and operates almost 50 local authority contracts. Despite softness in the industrial/commercial market, Collection turnover in the UK increased to £360.6 million (£270.7 million) in 2003/2004.

Including the contribution of Hales, profit before interest, tax, goodwill amortisation and exceptional items was £51.6 million, up 18.3%. Excluding the estimated contribution from Hales, Collection's profit before interest, tax and goodwill amortisation was down by around





2%. In 2003/2004, with local authorities striving to meet statutory recycling targets, Biffa was able to extend several contracts with additional services. Success in gaining important new contracts on the industrial/commercial side continued, capitalising on Biffa's national coverage of depots and supporting IT infrastructure.

#### Landfill

Although legislation and increases in landfill tax are likely to drive demand for alternative methods of disposal in the future, landfill remains the primary waste disposal route in the UK. Biffa currently operates 34 landfill sites, and it has been recommended for the ISO14001 environmental management accreditation for its landfill division.

Landfill turnover in the UK was up 15.2% to £163.1 million in 2003/2004. Landfill volumes, excluding the estimated impact of Hales, were up by around 3%, and unit revenues were up 1%. Landfill's profit before interest, tax and goodwill amortisation was up 17.6% to £34.0 million, including the Hales' contribution; and up by around 7% if that contribution is excluded.

#### Special Waste

The Special Waste division's turnover increased by 11.6% to £50.2 million in 2003/2004. Profit before interest, tax and goodwill amortisation for the division was £7.0 million; excluding the contribution from Hales, this figure was up by around 7% on the previous year. With its range of products and technologies for handling special waste, the division is well placed to exploit the opportunities offered by the Landfill Directive and hazardous waste regulations. Biffa's power generation activity is a key component of the Special Waste division. In 2003/2004 we boosted our capacity to generate power from landfill gas to around 90 MW in the UK.

#### Unique market position

Biffa is well placed to capitalise on opportunities created by legislation driving the need for alternative methods of waste disposal

#### Integrated municipal contracts

In the previous financial year, Biffa won a £300 million integrated waste contract with Leicester City Council, to manage all its waste collection and disposal facilities. Development and implementation of the contract progressed well in 2003/2004.

#### Community and environment

Biffa donates its landfill tax credits to community and environment projects through the Biffaward fund. Changes to the Landfill Tax Credit Scheme by the government in 2003 have reduced the scope of Biffaward's contributions to projects and the type of projects it can fund; however, almost £7.5 million was given to community and environment projects in 2003/2004.

#### Belgium

Biffa's turnover in Belgium was up 10.4% to £59.2 million. A change in Belgian legislation means that turnover there is now reported gross of the recovery for environmental taxes (making it consistent with the UK), so this has boosted turnover figures for the year. Without the effect of that change, turnover would have been up by about 6%. Profit before interest, tax and goodwill amortisation in Belgium was £3.2 million.

#### Outlook

Biffa's market position comprising strengths in collection, landfill and special waste continues to provide a positive outlook for Biffa's future development and performance. Legislation and increases in landfill tax will continue to drive demand for alternative methods of waste disposal in the UK. Biffa's experience in Belgium means we are well placed to capitalise on these opportunities, as do our recognised high standards in pretreatment and recycling.

#### CASE STUDY

### HALES ACQUISITION STRENGTHENS BIFFA'S MARKET LEADERSHIP

In buying Hales in June 2003, Biffa has strengthened its geographical coverage, its product range and its customer base.

#### Successful integration

The Hales acquisition is already delivering cost efficiencies by improving vehicle utilisation throughout the enlarged collection infrastructure

June 2003 saw Biffa acquire Hales Waste Control and RMC Environmental Services, in a £141 million deal that established Biffa as one of the largest integrated waste management companies in the UK.

Hales was one of the top 10 waste companies in the UK, with some 27,000 industrial/commercial customers, 38 operating depots, 8 operational landfill sites, and 5 transfer stations. Its Waste-Safe service for small amounts of special waste is well known in the marketplace, and complements Biffa's existing services for bulk liquid waste.

With around 1,000 employees and 450 industrial/commercial collection vehicles, the Hales' integration was a substantial project. Employee and Union consultations had to be undertaken, collection depots and landfill sites had to be integrated into the Biffa system; sales forces had

to be integrated, and, crucially, a common IT system had to be set up.

The acquisition of Hales gives Biffa greatly increased coverage in London and East Anglia, enabling it to offer better geographical coverage to customers with multiple sites. It also greatly increases Biffa's operational landfill void in the south of England. In addition, the acquisition is delivering important cost efficiencies through improved fleet utilisation. It also enhances the combined company's ability to capitalise on new market opportunities.

## SUMMARY REVIEW OF OPERATIONS THE SERVICES GROUP

Our US and other international businesses delivered good results in 2003/2004, often in difficult market conditions. Strong management had a positive impact on margins and profits, and the high levels of innovation and service achieved in different parts of this group were recognised through prestigious industry awards and accolades.

Turnover down 1.1% at  
**£381.2m**

Profit before interest, tax and goodwill amortisation\* up 13.2% at  
**£38.7m**

\*Goodwill amortisation of £7.2 million.

### Performance

Severn Trent Services' turnover decreased by 1.1% to £381.2 million in 2003/2004, with a little under 80% of turnover arising in the US. Excluding the impact of the exchange rates, turnover increased by around 6%.

Profits before the impact of exchange rates were also affected by the weak dollar. Profit before interest, tax, goodwill amortisation and exceptional items was £38.7 million, up 13.2%; excluding the effect of exchange rates, this figure increased by around 16% on the previous year.

Goodwill amortisation for the Services Group was £7.2 million (£8.5 million). Profit before interest and tax was £31.5 million (loss of £21.1 million).

### SEVERN TRENT LABORATORIES

Turnover in Laboratories, the largest business within Services, was down 1.0% to £170.1 million, but excluding the impact of exchange rates turnover increased by around 7%. Turnover in the US (in US\$) was up by around 8% and turnover in the UK (£) was up by around 2%. A little over 80% of Laboratories' turnover arose in the US.

The US performance took place against a background of difficult markets – for example, federal budget deficits have led to cutbacks in the United States Environmental Protection Agency funding. Nevertheless, excluding the impact of exchange rates, the Laboratories business has continued to grow turnover.

### Leading the market

Severn Trent Laboratories expanded its geographical reach in 2003/2004, opening new service centres in five US states. Its operations now comprise 31 laboratories and 21 service centres in the US, 4 laboratories and 1 service centre in the UK, and a large fleet of mobile laboratories.

STL's market leadership is not just size-related; it also takes the form of being at the forefront of emerging areas in contaminant testing.



### Acquisitions

In April 2003 STL acquired P&K Microbiology Services, a microbiology and mycology testing business recognised as a pioneer in mould testing. In March 2004, STL acquired Aerotech Laboratories Inc (Aerotech), another leader in this field. Targeted acquisitions have been a key part of STL's strategy for growing its business, and will continue to be so.

### Outlook

Whilst economic conditions in the US are likely to remain difficult, there are a number of positive market opportunities. Emerging market areas such as indoor air quality and mould, food hygiene, and testing for perchlorate all provide good opportunities for profitable growth. On the UK side of the business, EU legislation is also creating opportunities.

### SEVERN TRENT SERVICES

Severn Trent Services improved its performance, before the impact of exchange rates. The restructuring programme initiated in 2002/2003 has led to a more focused management approach, and tighter controls on costs. This in turn has helped to increase margins.

### Water Purification

The Water Purification division was one of the main objects of last year's restructuring programme, and the benefits are visible. Cost reductions have brought a substantial improvement in margins. Turnover decreased by 5.3% to £82.9 million, but excluding the impact of exchange rates turnover was up by around 2%.



### Operating Services

The Operating Services division handles operating and maintenance contracts for customers in the US. Contract Operations saw positive effects from the weak US economy, since state and local municipalities faced with budget deficits are increasingly looking to public-private partnerships to improve the operating efficiency of water and waste treatment sites.

Turnover in 2003/2004 grew 1.7%, but excluding the impact of exchange rates turnover was up by around 7%.

In contrast, budget deficits are a negative backdrop for the Pipeline Services business, providing minimal support for infrastructure projects. However, last year's restructuring programme and a strategy of cutting costs and focusing on the core business of repair, rehabilitation and flow metering work has borne fruit.

Our Metering Services business achieved good growth in 2003/2004.

Severn Trent Water International (STWI) provides a range of management and consultancy services in Europe and the developing world. Contracts include a public-private partnership to operate water and wastewater services in Umbria (begun in 2002/2003); and longstanding public-private partnerships with the Flemish government in Belgium (Aquafin), and in Portugal with the joint venture company Indaqua.

### Improved performance

The Services Group has made significant progress

### CASE STUDY

## NEW MARKETS IN THE US

Targeted acquisitions have extended STL's capabilities in key emerging markets.

### Scale and breadth

Severn Trent Laboratories leadership position and wide spectrum of services remains key to its success

Indoor Air Quality ("IAQ") is a major market opportunity in the US and elsewhere. There is widespread concern that mould and toxic mould could be linked to 'sick building syndrome', and this is creating major legal and financial problems for property owners and insurers.

In April 2003, Severn Trent Laboratories put itself at the vanguard of this market when it acquired P&K Microbiology Services, a microbiology business whose staff have worked on many high-profile mould-testing cases in the US.

Eleven months later, Severn Trent also acquired Aerotech Laboratories in Arizona, the US's largest commercial Indoor Air Quality laboratory. Aerotech's analytical services include mould testing, food microbiology, industrial hygiene and bioterrorism response analysis. As well as giving STL a huge presence in the valuable and growing IAQ market,

the acquisition also accomplishes other important goals.

First, food microbiology is another emerging market, and represents an area of synergy to STL's existing testing range. Second, it closes a gap in STL's western US coverage. Phoenix, Arizona is one of the fastest-growing cities in the US, and this growth is promoting environmental work relating to infrastructure development. The opportunities for STL thus go far beyond the market potential of IAQ.

## SUMMARY REVIEW OF OPERATIONS OTHER BUSINESSES

Sales in the UK, North America and Australia led to an improved performance from Severn Trent's Systems group. In Property, there was good progress on current projects.

Turnover up 9.5% at  
**£147.1 million**

Profit before interest, tax and exceptional items\*  
**£5.5 million**

\*exceptional provision release of £2.7 million

### SYSTEMS

Total turnover for the Severn Trent Systems Group in 2003/2004 was £63.6 million, up 3.8% on the previous year. Profit before interest and tax was £5.0 million.

Aseriti supplies IT solutions and services for the private, public and utility sectors in the UK, USA and Australia.

In the UK it won a substantial contract to supply software and expertise to utility infrastructure provider Core Utility Solutions Ltd. It has managed and implemented substantial projects for Severn Trent Water and Severn Trent Plc. These included an IT solution to transfer information on the region's 62,000 mile pipe network from paper maps onto mobile computers. Its latest CIS solution was also delivered and installed to Severn Trent Water in preparation for competition.

In the US, South Maryland Electric Co-operative – one of the ten largest electric co-operatives in the US – went live with CIS-Open Vision in November 2003. CIS-Open Vision is also being used successfully by Snohomish Public Utilities Department, following its implementation in January 2003. In Australia, the energy utility Citipower, based in Victoria, went live with CIS-Open Vision for

269,000 customers in September 2003. Energy supplier ETSA, based in South Australia, went live with 765,000 customers in November 2003, and energy utility Alinta went live with the new upgrade of CIS-Open Vision in February 2004 with 480,000 customers. Alinta now has 99% of its retail customers on CIS-Open Vision, and uses the system to generate 8,000 bills per day.

Worksuite, the work management business of the Systems Group, was restructured into a stand-alone, wholly owned subsidiary. Based in Houston, its market is the UK and primarily North America, where it enjoys a leadership position. The company completed major new sales to FPL, Enbridge and Northeast Utilities. It also advanced its large-scale deployments of its integrated office, web and wireless technology at FPL, National Grid and a Scottish Power affiliate in the UK.

### PROPERTY, ENGINEERING CONSULTANCY AND INSURANCE

Total turnover from these businesses in 2003/2004 was £83.5 million (£73.0 million). Profit before interest and tax was £3.2 million (£5.5 million). The reduction in profits reflects the result from Haswells, the Group's engineering consultancy business.

#### Property

Severn Trent Property was originally set up to exploit the development potential of land surplus to Severn Trent Water's requirements. It also undertakes projects on sites acquired from third parties.

In 2003/2004 good progress was made on virtually all current projects. At Thorpe Park, Leeds – the largest out-of-town office park in the north of England – further buildings were completed for WS Atkins plc, Boxwood plc and the University of Leeds. Major infrastructure, which will give direct access onto the M1 motorway, is now completed.

At Daventry International Rail Freight Terminal, planning permission to extend the project by up to 2 million sq ft was granted during autumn 2003. During the year, a major regional sorting hub was completed for Royal Mail. Remaining undeveloped land within the first phase of the project was sold to another developer.

At Warwick, work has commenced at Tournament Fields, adjacent to Junction 15 of the M40. The site has planning permission for office and business use; infrastructure, including roads and drainage, is under construction.

#### Engineering

Charles Haswell & Partners offers consultancy services in a wide range of engineering and environmental disciplines. In 2003, two awards paid tribute to the company's expertise. New Civil Engineer and the Association of Consulting Engineers recognised it as the top medium-sized consulting engineer in 2003. Secondly, it was joint winner of the British Geotechnical Society's Fleming Award, for its work on design and construction of a section of the Dublin Port Tunnel Project.

Other activity in 2003/2004 included working with Yorkshire Water Services as a key member of its Eastern Area Wastewater Capital Solution Team. It also made a major contribution to the successful delivery of Severn Trent Water's capital programme.

Charles Haswell & Partners introduced its Environmental Management System in 2003/2004 which is accredited to the ISO 14001:2001 standard.

#### Insurance

Derwent Insurance, based in Guernsey, Severn Trent's captive insurer provides insurance cover to Severn Trent group companies.

## CORPORATE RESPONSIBILITY

Severn Trent's corporate vision is to be at the forefront of the environmental services industry. Our corporate values of environmental leadership, service and quality are enshrined in our Code of Business Principles and Conduct. They define our business culture and guide our strategies.

### Our policy

We strive to be a responsible corporate citizen and recognise that Severn Trent has an important role to play in achieving sustainable development for society as a whole. As part of this commitment, we seek to conserve natural resources and to support the communities in which we operate.

Our role as an environmental services company means that our activities are of intrinsic benefit to society, however, our ability to achieve business success also makes a significant contribution to building a sustainable future. As well as delivering shareholder value, we support the wider community in ways that range from the employment opportunities we offer to our charitable donations.

### Vision, values and principles

We aspire to high standards of corporate behaviour as we pursue our vision of leadership in the environmental services industry. To set an ethical framework for our activities, we have published our values and a code of business principles, which are available on our website at [www.severntrent.com](http://www.severntrent.com).

### Environment

The goal of environmental leadership influenced work at every level in 2003/2004. Projects ranged from auditing Biffa's landfill sites against its Biodiversity Action Plan, to detailed planning on how our businesses will adapt to the existing effects of climate change. Mitigation of our own environmental impact is also central, and a

major achievement in this area is our electricity generation from renewable resources.

### Workplace

We are committed to providing a safe working environment for our employees and all other people that come into contact with the company and in 2003/2004 the number of reportable health and safety incidents declined. We also seek to ensure equality of opportunity through a diverse workforce.



### Recognised leadership

Severn Trent has been named as the leading utility in the Dow Jones Sustainability Index for the third consecutive year

### Community

Severn Trent's community affairs programme focuses on environmental education, the built environment and the natural environment. Investment takes cash and non-cash forms, and we are a member of the PerCent Club of businesses, which donate at least 1% of pre-tax profits to the community. Employee volunteering is an important part of this.

### Marketplace

In all areas of Severn Trent's business in 2003/2004 our commitment to corporate responsibility also led to success in the marketplace. For example, Severn Trent's levels of service were recognised in its leading position among water and sewerage companies in Ofwat's Overall Performance Assessment in 2003. The Laboratories business's work on emerging new environmental and health risks, such as toxic mould, is being rewarded with continuing growth. Biffa's experience in the Isle of Wight, where it diverted over 45% of the island's waste from landfill, is a good platform for offering integrated waste management services to local authorities.

Further commentary on Severn Trent's commitment to corporate responsibility in 2003/2004 is available in the company's annual Stewardship Report.



### Environmental solutions

Our objective is to provide services that solve environmental problems, respond to new environmental expectations and deliver sustainable development

## FINANCIAL REVIEW

### Group results

Group turnover was £2,015.1 million (£1,852.0 million), an increase of 8.8% over last year. The growth in turnover was mainly due to the contribution of the non-regulated businesses, which benefited from the acquisitions made in the year. The turnover of the non-regulated businesses increased by 12.7% to £1,161.4 million (£1,030.6 million), representing 54.8% (52.9%) of the Group total (before the elimination of inter segment trading). Turnover from water and sewerage increased by 4.2% to £956.7 million (£917.9 million).

Goodwill amortisation was £29.8 million (£25.2 million). There was a net exceptional profit of £11.6 million (loss of £40.8 million) – see below.

Group profit before interest, tax, goodwill amortisation and exceptional items was up 7.5% to £440.6 million (£409.8 million). The water and sewerage business was up by 3.8% to £337.9 million (£325.5 million). The Group's non-regulated businesses in total were up 18.1% to £123.4 million (£104.5 million), representing 26.8% (24.3%) of the Group total (before unrealised profit on inter segment trading and corporate overheads).

Group profit before interest, tax and exceptional items was £410.8 million (£384.6 million). Group profit before interest and tax was £422.4 million (£343.8 million).

After interest charges of £168.0 million (£159.4 million), Group profit before tax, goodwill amortisation and exceptional items was up 8.9% at £272.6 million (£250.4 million). Group profit before tax and exceptional items was £242.8 million (£225.2 million) an increase of 7.8%. Group profit before tax was £254.4 million (£184.4 million).

The total tax charge for the year was £69.6 million (£84.3 million) of which current tax represented £33.3 million (£24.8 million) and deferred tax was £36.3 million (£59.5 million). Minority interests were £0.7 million (£0.9 million). Profit after tax and minority interests was £184.1 million (£99.2 million).

Basic earnings per share were 53.5 pence (28.9 pence). Adjusted basic earnings per share (before exceptional items and deferred tax) were 61.4 pence (58.1 pence), an increase of 5.7%.

Operating activities generated a net cash inflow of £733.1 million. The main cash outflows were capital expenditure and financial investment of £487.5 million, equity dividends of £157.7 million, acquisitions of £170.6 million and net financing costs of £148.3 million. The increase in net debt was £243.5 million.

Net debt at 31 March 2004 was £2,749.1 million (£2,505.6 million). Gearing, reflecting the provision for deferred tax, was 124% (113%). The group's net interest charge was covered 4.4 times (4.4 times) by profit before interest, tax, depreciation, goodwill amortisation and exceptional items.

### Exceptional items

There was a net exceptional profit in the year of £11.6 million, comprising the net of:

- A £19.8 million profit from the sale of fixed assets, arising from the sale of land and property by Severn Trent Water. Given its magnitude, the profit from the sale of fixed assets was not treated as exceptional in 2002/2003 (£6.7 million);
- A £2.7 million credit from the release of part of the exceptional charge made in 2001/2002 in respect of certain of Systems' CIS-Open Vision contracts in the USA;
- A charge of £10.9 million in waste management for Hales' integration costs.

In 2002/2003, there was an exceptional charge of £40.8 million, comprising the net cost of a £46.8 million write down for impairment in the net book value of some businesses within Services and a £6.0 million credit from the release of part of the exceptional charge made in 2001/2002 in respect of certain of Systems' CIS-Open Vision contracts in the USA.

### Taxation

The charge for current tax was £33.3 million (£24.8 million), of which £2.4 million was attributable to exceptional items. The current tax charge of £30.9 million, attributable to profit after interest and goodwill amortisation but before tax and exceptional items is an effective rate of 12.7% (11.0%). The current tax rate has benefited from an adjustment in respect of prior periods.

### Pensions

SSAP24, the applicable standard for Severn Trent, uses the results of the last formal actuarial valuations to determine the pension charge in the Group's accounts. This principle has been followed in determining the Group's pension charge for 2003/2004.

The Group has four defined benefit pension schemes, viz: the Severn Trent Water Pension Scheme (STWPS) which is by far the largest of the Group's defined benefit pension schemes, the Severn Trent Mirror Image Pension Scheme (STMIPS), the UK Waste Pension Scheme (UKWPS) and the Severn Trent Senior Staff Pension Scheme (STSSPS).

Formal actuarial valuations have been undertaken for the STMIPS as at 31 March 2003 and for the UKWPS as at 6 April 2003. Given the deterioration in the funding position of these two schemes since their previous formal actuarial valuations, there is an additional pension charge (net of amounts allocated to own work capitalised) of £4.1 million for the Group in 2003/2004 reflecting the results of these valuations.

The Group's pension charge in 2003/2004 in respect of the STWPS and the STSSPS is based on their formal actuarial valuations as at 31 March 2001 when these funds had a combined surplus of around £46 million. Formal actuarial valuations of the STWPS and the STSSPS are currently being undertaken as at 31 March 2004 in accordance with the normal triennial pattern of valuations. Given the deterioration in the funding position of these two schemes since their last formal actuarial valuations, these valuations and the analogous assessment of the Group's unfunded pension liabilities for senior staff are expected to result in a significant additional pension charge for the Group in 2004/2005. Based on SSAP 24, this additional pension charge (net of amounts allocated to own work capitalised), is provisionally estimated to be of the order of around £30 million to £35 million, with broadly around two thirds to three quarters of this amount expected to be attributable to Severn

Trent Water. Given the preliminary nature of these estimates, it is quite possible that the actual additional pension charge, as a result of these valuations, could be materially different from these estimates.

On an FRS17 basis, the estimated net position (before deferred tax) of the Group's defined benefit pension schemes and the Group's unfunded pension liabilities for senior staff was a deficit of approximately £368 million as at 31 March 2004, as compared to a deficit of approximately £325 million as at 31 March 2003. Although the value of assets has increased over the last year, liabilities have increased by a greater amount reflecting, inter alia, the updating of mortality assumptions (to be in line with current experience and to include an allowance for expected further improvements) and a reduction in the real discount rate. Net of deferred tax, the estimated net deficit on an FRS17 basis as at 31 March 2004 was approximately £257 million. On an FRS17 basis the funding level has improved from around 70% at 31 March 2003 to 72% at 31 March 2004.

As at 31 March 2004 the Group's defined benefit pension schemes had total assets of approximately £937 million, of which around 73% was invested in equities.

#### Treasury management

The Group's treasury affairs are managed centrally and in accordance with its Treasury Procedures Manual and Policy Statement. The treasury operation's primary role is to manage liquidity, funding, investment and the group's financial risk, including risk from volatility in interest and (to a lesser extent) currency rates and counterparty credit risk. Its activities are subject to a set of controls commensurate with the magnitude of the borrowings and investments under its management. A Treasury Committee (appointed by the Board) determines matters of Treasury policy and its approval is required for certain treasury transactions.

It is the Group's strategy to access a broad range of sources of finance to obtain both the quantum required and the lowest cost compatible with the need for continued availability.

On 5 April 2004 Severn Trent put in place a new £700 million Revolving Credit Facility (RCF). This facility replaced two existing facilities – a £600 million RCF and a £160 million bilateral facility. The new RCF comprises two elements: a £200 million tranche maturing in 364 days with a one year term-out option, and a £500 million tranche having a five year maturity.

The Group uses financial derivatives solely for the purposes of managing risk associated with financing its normal business activities. The Group does not hold or issue derivative financial instruments for financial trading purposes. The group uses a limited number of currency swaps and interest rate swaps to redenominate external borrowings into the currencies and interest rate coupon required for group purposes.

The Group's policy for the management of interest rate risk requires that no less than 50% of the Group's borrowings should be at fixed interest rates, or hedged through the use of interest rate swaps or forward rate agreements. At 31 March 2004, interest rates for some 70% of the Group's net debt of £2,749 million were so fixed, at a weighted average interest rate of 6.1% for a weighted average period of 17.9 years. In addition, the group has a £50 million forward start interest rate swap (floating to fixed) that commences during 2004/2005.

The Group's business does not involve significant exposure to foreign exchange transactions. Cross currency swaps are employed to exchange foreign currency borrowings for sterling. The Group also has investments in various assets denominated in foreign currencies, principally the US dollar and the Euro. The Group's current policy is to hedge an element of the currency translation risk associated with certain foreign currency denominated assets.

In August 2003 Moody's Investor Services and Standard & Poor's lowered the long term credit rating of Severn Trent Plc and Severn Trent Water Limited.

Long term ratings	Severn Trent Water Limited	Severn Trent Plc
Moody's	A2	A3
Standard & Poor's	A	A-

#### International Accounting Standards

The Group will be required to prepare its financial statements under International Accounting Standards (IAS) for the year ending 31 March 2006, with the Group's first published results under IAS being the 2005/2006 Interim Results.

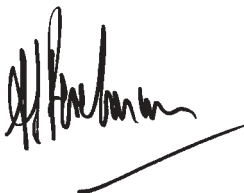
The Group has commenced a programme of work to prepare for the adoption of IAS. An initial review has been undertaken to identify the differences between IAS and existing UK standards and Group accounting policies. A central project management team has been formed to coordinate the transition process, with working groups from individual subsidiaries involved in the work, with a view also to determining any additional data that may be required to be collected.

Some of the prospective standards are still under review by the International Accounting Standards Board and, in addition, the Group's work in reviewing the impact of existing IAS is still ongoing. Hence, at this time, no definitive information on the impact on the Group of the adoption of IAS is being provided. However, it seems likely that the adoption of IAS will increase the volatility of the Group's reported results and impact its balance sheet.

Potentially significant changes arising from the adoption of IAS are currently thought to include accounting for financial instruments, retirement benefits, fixed assets and renewals accounting, deferred tax and business combinations.

#### Supplementary information

For supplementary information including the group's preliminary results presentation, see the Severn Trent website ([www.severntrent.com](http://www.severntrent.com)).



**Alan Perelman**  
Group Finance Director

## BOARD OF DIRECTORS

**Board Committees**

Membership of Board Committees is as detailed below:

**Audit Committee**

J B Smith (Chairman)  
M L Cassoni  
F A Osborn  
Secretary – P P Davies

**Charitable Contributions Committee**

B Duckworth (Chairman)  
R M Walker  
Secretary – P P Davies

**Corporate Responsibility Committee**

R M Walker (Chairman)  
T D G Arculus  
M J Bettington  
R S Brydon Jannetta  
B Duckworth  
L F Graziano  
J W Oatridge  
F A Osborn  
Secretary – P P Davies

**Executive Committee**

R M Walker (Chairman)  
T D G Arculus  
J K Banyard  
M J Bettington  
P P Davies (and Secretary)  
B Duckworth  
P J Gavan  
J W Oatridge  
A S Perelman  
P K Tandon

**Remuneration Committee**

M C Flower (Chairman)  
M L Cassoni  
J D G McAdam  
Secretary – P P Davies

**Nominations Committee**

T D G Arculus (Chairman)  
M C Flower  
J D G McAdam  
F A Osborn  
Secretary – P P Davies

**Treasury Committee**

M L Cassoni (Chairman)  
T D G Arculus  
T E Jack  
A S Perelman  
J B Smith  
R M Walker  
M R Wilson  
Secretary – P P Davies

**Senior independent non-executive Director**

M C Flower

**Group General Counsel and Company Secretary**

P P Davies, LL.B. Solicitor

**David Arculus** MA MSc Chairman (58)\*

Mr Arculus joined the Board in May 1996 as a non-executive Director and was appointed Chairman on 29 July 1998. He is a non-executive Director of Barclays PLC and was recently appointed as a non-executive Director of mmO<sub>2</sub>. From 2002 to May 2004 he was Chairman of Earls Court & Olympia Group Ltd and from 1998 to October 2001 he was Chairman of IPC Group Ltd. Until 1997 he was Group Managing Director of Emap Plc, the international media company, where he played a significant role in the growth of that company. Mr Arculus was formerly a journalist and a producer at the BBC. In April 2002, he was appointed by the Government to chair its Better Regulation Task Force.

**John Banyard** BScEng FEng FICE FCIWEM (59)

Mr Banyard joined the Board in January 1998. He is an executive Director of Severn Trent Water Ltd with responsibility for asset management. He is also a Director of UK Water Industry Research Ltd, a member of the Court of Cranfield University and the Royal Academy of Engineering Visiting Professor of Water Engineering at Loughborough University. Mr Banyard is a Chartered Civil Engineer and has worked in a number of engineering roles within the group since joining Severn Trent in 1974. He was elected a Fellow of the Royal Academy of Engineering in 1997. He is currently President of the Pipeline Industries Guild.

**Martin Bettington** BSc MechEng MBA (51)

Mr Bettington joined the Board in November 1994. He is the Managing Director of Severn Trent's waste management business, Biffa Waste Services Ltd. Mr Bettington was previously employed by BET Plc, Biffa's former holding company. He holds an MBA from Manchester Business School.

**Marisa Cassoni** BSc ACA (52)\*

Ms Cassoni joined the Board on 1 September 2001. She is currently Group Finance Director of Royal Mail plc, having previously been Group Finance Director at Britannic Assurance plc from 1998 to 2001. Ms Cassoni qualified as an accountant with Deloitte where she rose to be Corporate Finance Manager. She later moved to the Prudential Corporation, becoming Group Finance Director of the Prudential's UK Division in 1994.

**Brian Duckworth** BA FCCA FCIWEM FIWO (55)

Mr Duckworth joined the Board in November 1994. He has worked in various roles since joining Severn Trent in 1974 and was appointed Managing Director of Severn Trent Water Ltd on 1 April 1995. Mr Duckworth was appointed as a non-executive Director of Avon Rubber plc and Redrow Plc in 2002. He has served as the President of the Institution of Water Officers and Chairman of Water UK, the water industry's trade association.



**Martin Flower BA (57)\***

Mr Flower joined the Board in June 1996 and is the senior independent non-executive Director. At the end of May 2004 he retired as Chairman of Coats Ltd, where he had previously been Group Chief Executive.

**Martin Houston BSc MSc DIC (46)\***

Mr Houston joined the Board on 1 September 2003. He is currently Executive Vice President and Managing Director of BG Group's North American, Caribbean and Global Liquefied Natural Gas business and a member of the Group Executive Committee. He joined BG Group in 1983 and has held a number of technical and commercial roles with a predominantly international focus. He has a BSc in Geology from Newcastle University and an MSc in Petroleum Geology from Imperial College, London. He is a fellow of the Geological Society of London and sits on the board of SIGTTO (Society of International Gas Tanker & Terminal Operators Ltd).

**Colin Matthews MA CEng (48)\***

Mr Matthews joined the Board on 17 October 2003. He is a Chartered Engineer who has worked in Japan, France, Canada, and the UK. He worked for the (American) General Electric Company for nine years and subsequently spent five years at British Airways, first as Director of Engineering then as Director of Technical Operations, responsible for all aircraft maintenance, IT and procurement. He then joined the Board of Lattice Group Plc as Group Managing Director of Transco until its merger with the National Grid. He has held his current position as CEO of Hays Plc since November 2002. Mr Matthews holds a first class degree in Engineering from Cambridge University.

**John McAdam BSc PhD (56)\***

Dr McAdam joined the Board on 18 September 2000. He is Chief Executive and a member of the Board of ICI PLC. He joined ICI in 1997 following the acquisition of the Specialty Chemical Businesses from Unilever where he held a number of senior positions in Birds Eye Walls Ltd, Unichema International and Quest International. He was appointed Executive Vice President Coatings and Chief Executive of ICI Paints in 1998, and joined the Board of ICI PLC soon after when he also became responsible for Corporate Research & Technology. He took over as Chief Executive of ICI PLC in April 2003. He is a member of the University of Surrey Business Advisory Group.

**Derek Osborn CB (63)\***

Mr Osborn joined the Board on 21 September 1998 and is a leading figure in the environmental world. He was Chairman of the UK Round Table on Sustainable Development from 1999 to 2000 and is now a member of the UK Commission on Sustainable Development. He has been Chairman of UNED UK since 1996 and was Chairman of the International Institute for Environment and Development from 1998 to 2002. He is Chairman of Jupiter Global Green Investment Trust and of the international advisory board of ERM CVS. Mr Osborn was Director General of Environment Protection in the Department of the Environment from 1990 to 1995 and Chairman of the Management Board of the European Environment Agency from 1995 to 1999.

**Alan Perelman MA MSc (56)**

Mr Perelman joined the Board in October 2001 and was appointed Group Finance Director in December 2001. Prior to this he was Group Finance Director at Whitbread from 1990 to 2001. Previous positions held were Group Finance Director at The Gateway Corporation and various positions at Rio Tinto both in the UK and overseas.

**John Smith FCCA, Hon. FRIBA (46)\***

Mr Smith joined the Board on 3 November 2003. He is a member of the H M Treasury's Public Services Productivity Panel, the Accounting Standards Board and the 100 Group of Finance Directors. He is a Fellow of the Chartered Association of Certified Accountants. After training with a firm of accountants, Mr Smith joined the British Railways Board, moving up over a period of 14 years to head up their corporate demerger team. In 1989 he moved to the BBC, becoming Director of Finance, Property and Business Affairs in 1997. Mr Smith has held a non-executive directorship with Vickers Plc, was a member of the advisory board of Zurich Financial Services UK and was a Director of the Royal Television Society.

**Robert Walker MA (59)**

Mr Walker joined the Board in May 1996 as a non-executive Director. He was appointed Deputy Chief Executive in July 1999 and became Group Chief Executive in August 2000. He has previously worked for Procter & Gamble, McKinsey & Company and PepsiCo Inc. where he was a Division President. Mr Walker is also a non-executive Director of Wolseley Plc and BAA Plc.

\*Non-executive Director

**Top row**

David Arculus  
Robert Walker  
Alan Perelman  
Brian Duckworth  
Martin Bettington  
Colin Matthews  
John McAdam

**Bottom row**

Martin Flower  
Marisa Cassoni  
Derek Osborn  
John Smith  
John Banyard  
Martin Houston

## INDEPENDENT AUDITORS' STATEMENT TO THE MEMBERS OF SEVERN TRENT PLC

We have examined the summary financial statement of Severn Trent Plc.

### Respective responsibilities of Directors and auditors

The directors are responsible for preparing the summarised annual review in accordance with applicable law. Our responsibility is to report to you our opinion on the consistency of the summary financial statement within the Annual Review 2004 with the annual financial statements, the directors' report and the remuneration report, and its compliance with the relevant requirements of Section 251 of the United Kingdom Companies Act 1985 and the regulations made thereunder. We also read the other information contained in the Annual Review 2004 and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the summary financial statement.

This statement, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 251 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this statement is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

### Basis of opinion

We conducted our work in accordance with Bulletin 1999/6, 'The auditors' statement on the summary financial statement' issued by the Auditing Practices Board for use in the United Kingdom.

### Opinion

In our opinion the summary financial statement is consistent with the annual financial statements, the directors' report and the remuneration report of Severn Trent Plc for the year ended 31 March 2004 and complies with the applicable requirements of Section 251 of the Companies Act 1985 and the regulations made thereunder.

### PricewaterhouseCoopers LLP

Chartered Accountants and Registered Auditors, Birmingham  
7 June 2004

## SUMMARY DIRECTORS' REPORT

### Principal activities

The principal activities of the group continued to be the supply of water and sewerage services, waste management and the provision of environmental services. These are described in more detail, together with a review of the group's business and future developments, on pages 8 to 14.

### Final Dividend

Subject to approval at the Annual General Meeting, the recommended final dividend of 29.27p (2003: 28.56p) net for each ordinary share will be paid on 1 October 2004 to shareholders on the register at the close of business on 18 June 2004. This, together with the interim dividend of 17.77p (2003: 17.34p) per share, which was paid on 6 April 2004, brings the total for the year to 47.04p (2003: 45.90p).

### Share capital

Resolutions will be proposed at this year's Annual General Meeting ("AGM") to renew the Directors' authority to:

- allot relevant securities (within the meaning of Section 80 of the Companies Act 1985);
- issue equity securities for cash without first having to offer these securities to existing shareholders; and
- make market purchases of the company's own ordinary shares.

Full details of these resolutions are included in the Notice of the AGM which is circulated to all shareholders.

### Substantial shareholdings

As at 7 June 2004 the company had been notified of the following substantial shareholding:

	Number of ordinary shares of 65% <sup>1</sup> p each	%
Legal & General Investment Management Limited	11,259,833	3.26

### Directors

A list of Directors and their background details appear on pages 18 and 19. Details of their service contracts and emoluments can be found in the Summary Remuneration Report on page 24 to 26.

Mr M J Houston, Mr C S Matthews and Mr J B Smith joined the Board as non-executive Directors on 1 September 2003, 17 October 2003 and 3 November 2003 respectively.

Mrs C Tritton and Mr E E Anstee retired from the Board on 30 July 2003 and 15 December 2003 respectively.

In accordance with the company's Articles of Association Messrs J K Banyard, B Duckworth, M J Houston, C S Matthews, F A Osborn, J B Smith and Dr J D G McAdam retire at the AGM and, being eligible, offer themselves for reappointment. The Nominations Committee supports and recommends the proposed reappointments.

The company has recently announced a number of changes regarding its Directors. It has been agreed that Mr T D G Arculus will step down as Chairman of the Board as he will soon be appointed Chairman of mMO<sub>2</sub>. However, in order to provide continuity to the Board during a time of change and also assist in the finalisation of Severn Trent Water's AMP4 determination, it was considered to be in the best interests of the company for him to remain in post until 31 December 2004. Mr R M Walker will retire as Group Chief Executive on 2 February 2005 and will be succeeded by Mr C S Matthews. Mr A S Perelman will retire as Group Finance Director on 31 August 2004 and will be replaced by Mr M R Wilson. Mr B Duckworth will step down from the Board at the end of August 2004. Mrs R S Brydon Jannetta will join the Board, as an executive Director, in September 2004.

### Corporate governance

The company attaches great significance to the maintenance of good corporate governance procedures and adherence to best practice recognising that they play their part in creating a framework which can provide increased benefits for shareholders.

Following the issue of a revised Combined Code on Corporate Governance (the "Revised Code") in July 2003, the company has carried out a review of its corporate governance arrangements and made changes as necessary and appropriate.

As the Revised Code became effective for accounting periods starting on or after 1 November 2003, this report has been prepared on the basis of the previous Combined Code on Corporate Governance (the "Code"). However it is anticipated that the company will be compliant with virtually all provisions of the Revised Code for the new financial year.

Throughout the year ended 31 March 2004 the company has been in compliance with the provisions set out in Section 1 of the Code.

### The Board

The Board currently consists of five executive Directors and eight non-executive Directors. The Board has reviewed the status of the non-executive Directors and has confirmed that, with the exception of Mr C S Matthews as Group Chief Executive Designate, it regards them as being independent. At the time of his appointment as Chairman of the company Mr T D G Arculus was considered to be independent. However, in accordance with the Revised Code, he is now deemed not to be independent.

### Employees

The group employed 15,973 people as at 31 March 2004 (2003: 14,890). Of these 5,099 (32%) were employed in the water business, 5,241 (33%) in the Biffa waste business and 4,781 (30%) in the Severn Trent Services businesses. The numbers in Biffa have increased as a result of the acquisition of Hales Waste in 2003. Approximately 29% of employees continue to be based outside the UK, mainly in the USA, Belgium and Italy.

The larger group companies now each have their own intranets which form a major communication channel with their employees in addition to in-house magazines and tool-box talks.

Group companies continue to maintain positive relationships with the recognised trade unions and with other elected representatives. The group's annual meetings of the European Consultative Council are a further opportunity to develop a dialogue with employee representatives and promote their better understanding of the future issues facing our businesses in Europe.

The group has undertaken a major review of its pension strategy with the objectives of reducing risk, maintaining affordability and demonstrating equity. As a result of this review three new pension options were made available to new employees from 1 April 2004.

The group's "Lifestyle" flexible benefits scheme continues to expand amongst UK based employees and with its introduction to Biffa staff in October 2004 will cover over 8,000 employees.

The group continues to focus on the development of employees at all levels. In Biffa there has been a significant effort in harmonising the driver training programme to incorporate the best from the Biffa and the Hales driver training schemes.

Three of the training programmes in Severn Trent Water received awards: The Institute of Leadership and Management Award for Excellence in Supervisory Management; and the Sector Skills Council award for both the BSc in Water and Environmental Management and the partnership with Warwick Business School.

All companies have the goal of making learning opportunities available and accessible to all employees. To this end many companies are making learning resource centres available in e-learning by intranet and internet providers. These activities are all complemented at senior manager level by the Leadership Development programme which covers the top 120 managers.

Group companies continue to meet legislative requirements of the countries in which they operate. In addition, they further operate in compliance with the group's Code of Business Principles and Conduct and disclosure (whistle-blowing) procedures.

### Diversity

Diversity policies are in place in each company in the group that reflect the requirements of the locations in which they operate and that also meet the aims of the company's Code of Business Principles and Conduct.

The company continues to monitor the data on the diversity of the current and potential workforce. The US businesses continue to demonstrate their lead in the group with the gender and ethnic diversity of their workforces.

On an ongoing basis, the company benchmarks its policies and practices in this area by taking guidance from best practice advisors such as the Employers Forum on Disability and Race for Opportunity. Progress is regularly monitored by the Corporate Responsibility Committee.

### Health and safety

This year the company has continued to develop a safety culture fully integrated into all aspects of the way the business is managed. To help ensure that the actions taken are consistent with best practice the main companies in the group have partnered with external experts to develop behavioural safety initiatives involving employees at all levels.

Work also continued on over-arching group standards which apply to all group companies wherever they operate and these standards will address all key risk areas.

Health and Safety is discussed at every Board meeting. In addition, the Board receives six-monthly reviews and other periodic reports from the managing directors of the operating companies.

### Auditors

The auditors' report on the full annual accounts of the group for the year ended 31 March 2004 was unqualified and did not contain a statement under either section 237(2) (accounting records or returns inadequate or accounts not agreeing with records and returns) or 237(3) (failure to obtain necessary information and explanations) of the Companies Act 1985.

A resolution proposing the reappointment of PricewaterhouseCoopers LLP as Auditors will be put to the AGM.

By order of the Board  
**P P Davies** LL.B. Solicitor  
 Group General Counsel and Company Secretary  
 7 June 2004

## SUMMARY GROUP PROFIT AND LOSS ACCOUNT

YEAR ENDED 31 MARCH 2004

	Continuing Operations		Total 2004	2003
	Acquisitions			
	£m	£m	£m	£m
<b>Turnover</b>	<b>1,919.9</b>	<b>95.2</b>	<b>2,015.1</b>	1,852.0
Operating costs before goodwill amortisation and exceptional items	(1,505.1)	(81.3)	(1,586.4)	(1,453.0)
Goodwill amortisation	(24.8)	(5.0)	(29.8)	(25.2)
Exceptional integration costs	–	(10.9)	(10.9)	–
Exceptional provision release	2.7	–	2.7	6.0
Exceptional impairment of goodwill and tangible fixed assets	–	–	–	(46.8)
<b>Total operating costs</b>	<b>(1,527.2)</b>	<b>(97.2)</b>	<b>(1,624.4)</b>	(1,519.0)
<b>Group operating profit/(loss)</b>	<b>392.7</b>	<b>(2.0)</b>	<b>390.7</b>	333.0
Share of operating profit of joint ventures and associates	11.9	–	11.9	10.8
Exceptional profit on disposal of fixed assets	19.8	–	19.8	–
Profit before interest, goodwill amortisation and exceptional items	<b>426.7</b>	<b>13.9</b>	<b>440.6</b>	409.8
Goodwill amortisation	(24.8)	(5.0)	(29.8)	(25.2)
Profit before interest and exceptional items	<b>401.9</b>	<b>8.9</b>	<b>410.8</b>	384.6
Exceptional costs	–	(10.9)	(10.9)	(46.8)
Exceptional profits	22.5	–	22.5	6.0
<b>Profit/(loss) before interest</b>	<b>424.4</b>	<b>(2.0)</b>	<b>422.4</b>	343.8
Net interest payable			(168.0)	(159.4)
Profit after interest before goodwill amortisation and exceptional items			<b>272.6</b>	250.4
Goodwill amortisation			(29.8)	(25.2)
Profit after interest before exceptional items			<b>242.8</b>	225.2
Exceptional items			<b>11.6</b>	(40.8)
<b>Profit on ordinary activities before taxation</b>			<b>254.4</b>	184.4
Taxation on profit on ordinary activities – current tax			(33.3)	(24.8)
– deferred tax			(36.3)	(59.5)
Total taxation			(69.6)	(84.3)
<b>Profit on ordinary activities after taxation</b>			<b>184.8</b>	100.1
Equity minority interests			(0.7)	(0.9)
<b>Profit for the financial year</b>			<b>184.1</b>	99.2
Dividends			(162.0)	(157.6)
<b>Retained profit/(loss) for the financial year</b>			<b>22.1</b>	(58.4)
<b>Earnings per share (pence)</b>				
Basic			<b>53.5</b>	28.9
Adjusted basic before exceptional items and deferred tax			<b>61.4</b>	58.1

**Important note:** The Annual Review and summary financial statement does not contain sufficient information to allow a full understanding of the results of the group and of the state of affairs of the company or of the group nor of the policies and arrangements concerning Directors' remuneration. For further details, the Annual Report and Accounts 2004, which includes the Directors' report and the Auditors' report on the financial statements, should be consulted.

A copy can be obtained, free of charge, by writing to the Company Secretary at 2297 Coventry Road, Birmingham B26 3PU. Alternatively it can be accessed on the website at [www.severntrent.com/reports2004](http://www.severntrent.com/reports2004). Shareholders can elect to obtain the full Annual Report and Accounts for all future financial years by contacting the company's registrars, Lloyds TSB Registrars whose details appear on page 27.

## SUMMARY GROUP BALANCE SHEET

AT 31 MARCH 2004

	2004 £m	2003 £m
<b>Fixed assets</b>	<b>5,807.1</b>	5,480.6
<b>Current assets</b>	<b>648.5</b>	583.1
<b>Creditors: amounts falling due within one year</b>	<b>(1,223.7)</b>	(1,219.2)
<b>Net current liabilities</b>	<b>(575.2)</b>	(636.1)
<b>Total assets less current liabilities</b>	<b>5,231.9</b>	4,844.5
<b>Creditors: amounts falling due after more than one year</b>	<b>(2,440.6)</b>	(2,101.6)
<b>Provisions for liabilities and charges</b>	<b>(572.0)</b>	(523.1)
<b>Net assets</b>	<b>2,219.3</b>	2,219.8
<b>Capital and reserves</b>	<b>2,216.9</b>	2,217.6
Minority shareholders' interest (equity)	<b>2.4</b>	2.2
	<b>2,219.3</b>	2,219.8

Signed on behalf of the Board who approved the accounts on 7 June 2004.

**David Arculus**  
Chairman

**Alan Perelman**  
Group Finance Director

## SUMMARY GROUP CASH FLOW STATEMENT

YEAR ENDED 31 MARCH 2004

	2004		2003	
	£m	£m	£m	£m
<b>Net cash inflow from operating activities</b>		<b>733.1</b>		682.7
<b>Dividends received from associates and joint ventures</b>		<b>1.9</b>		1.6
<b>Returns on investments and servicing of finance</b>		<b>(148.3)</b>		(146.7)
<b>Taxation</b>		<b>(19.5)</b>		(14.3)
<b>Capital expenditure and financial investment</b>		<b>(487.5)</b>		(454.0)
<b>Acquisitions</b>		<b>(170.6)</b>		(11.5)
<b>Equity dividends paid</b>		<b>(157.7)</b>		(157.5)
<b>Net cash outflow before use of liquid resources and financing</b>		<b>(248.6)</b>		(99.7)
<b>Management of liquid resources</b>		<b>(45.2)</b>		(6.5)
<b>Financing</b>				
Increase in debt	<b>283.1</b>		114.1	
Issue of shares	<b>5.6</b>		3.3	
		<b>288.7</b>		117.4
<b>(Decrease)/increase in cash</b>		<b>(5.1)</b>		11.2

## SUMMARY REMUNERATION REPORT

### Remuneration Committee

The Remuneration Committee determines, on behalf of the Board, the company's policy on the remuneration of executive Directors and the Chairman of the Board. The Committee also determines the remuneration policy for the next band of approximately 10 senior executives.

The policy framework for remunerating all senior executives is consistent with the approach taken for executive Directors.

The Committee is comprised exclusively of independent non-executive Directors of the company. The members of the Committee during the year were:

M C Flower (Chairman)  
T D G Arculus (resigned 31 March 2004)  
J D G McAdam  
M L Cassoni (appointed 27 February 2004)

The Committee members have no personal financial interest, other than as shareholders, in the matters to be decided.

The constitution and operation of the Committee comply with the Combined Code on Corporate Governance of the Financial Services Authority (the 'Code'). In setting performance related remuneration the Committee has regard to the provisions set out in Schedule A to the Code.

### Advisers

To ensure that the company's remuneration practices are market competitive, the Committee has access to detailed external research on market data and trends from experienced specialist consultants.

The Group Chief Executive and Mr J W Oatridge, Group Services Director (and the Chairman of the Board with effect from 1 April 2004) also provide advice and are invited to attend meetings to respond to specific questions raised by the Committee. This specifically excludes any matter concerning their own remuneration. The Company Secretary acts as Secretary to the Committee.

### Remuneration policy

The company's ongoing remuneration policy for executive Directors is to review regularly and update as appropriate the framework to provide remuneration in a form and amount which will attract, retain, motivate and reward high calibre individuals. To achieve this, the remuneration package is based on the following principles:

- Incentives are aligned with the interests of shareholders and seek to reward the creation of long-term value;
- Reward elements are designed to reinforce the link between performance and reward. Performance related elements should form a significant proportion of the total remuneration package and at maximum for 2004/2005 vary between 135% and 160% of basic pay;
- The total compensation package for on-target performance should be fully competitive in the relevant market;
- Packages are structured flexibly to meet critical resource needs and retain key executives.

The Committee seeks to take a prudent and responsible approach taking into account the interests of shareholders, customers, employees and the local community.

### Personal shareholdings

The company has, with effect from 26 April 2004, adopted guidelines which expect executive Directors to have a minimum holding of ordinary shares in the company. The Group Chief Executive is expected to hold shares to the value of 1.5 x salary and other executive Directors 1 x salary, to be acquired over a transitional period. Through a variety of share schemes, all employees are encouraged to hold shares in the company.

### External directorships

Executive Directors are encouraged to take on external non-executive directorships, though normally only one other FTSE 100 appointment. In order to avoid any conflicts of interest all such appointments are subject to the approval of the Nominations Committee. Directors are normally only able to retain the fees arising from one such appointment.

### Chairman and other non-executive Directors

The remuneration policy for non-executive Directors, other than the Chairman, is determined by the Board, within the limits set out in the Articles of Association.

Remuneration comprises an annual fee for acting as a non-executive Director of the company and additional fees for acting as:

- Chairman of a Board Committee;
  - Senior non-executive Director;
  - Trustee of a company pension scheme;
  - Non-executive Director of a subsidiary company.
- Non-executive Directors are not eligible to participate in incentive plans nor is any pension provision made except as detailed in relation to Mr Arculus.

Non-executive Directors receive payment of part of their fees in the form of ordinary shares in the company which, from May 2004, have to be retained for the period of their appointment.

The non-executive Directors do not have service contracts or consultancy agreements with any group company.

### Remuneration arrangements for executive Directors

The remuneration arrangements for executive Directors comprise the following elements:

- Base salary and benefits;
- Annual bonus plan;
- Long Term Incentive Plan;
- Post-retirement benefits.

Details of each of the above elements are as follows:

#### Base salaries and benefits

Base salaries are a fixed cash sum payable monthly. The company's policy is to set the salary for each executive Director within a range having regard to the market median for similar roles in large publicly quoted companies. Salaries for individual Directors are reviewed annually by the Remuneration Committee recognising individual performance and contribution and developments in the relevant employment market.

The non-salary benefits for executive Directors comprise the use of a motor car, fuel, private medical insurance, life assurance and an incapacity benefits scheme.

### Annual bonus plan

Executive Directors are eligible for annual bonuses to encourage improved performance, measured by reference to both financial and non-financial factors. Performance targets are established by the Committee. The maximum amount payable under the bonus scheme in 2003/2004 was 50% of base salary. The performance requirements are stretching and involve an assessment of up to ten parameters for each executive Director. Annual bonus payments are not taken into account in calculating pension entitlements. The actual bonuses awarded by the Committee for the year ended 31 March 2004 are shown in the table of Directors' emoluments on page 29. For the 2004/2005 financial year the bonus potential for the Group Chief Executive will be 60% and for the Managing Director of Biffa (Mr M J Bettington) will be 75%. The bonus potential for other executive Directors remains at 50%.

### Long-term incentives

A Long Term Incentive Plan ('LTIP') for executive Directors was approved by shareholders at the 1997 Annual General Meeting and amended with shareholder approval at the 2001 Annual General Meeting.

The performance for the 2001, 2002 and 2003 LTIPs is measured by reference to a combination of Total Shareholder Return ('TSR') and Economic Profit ('EP') targets.

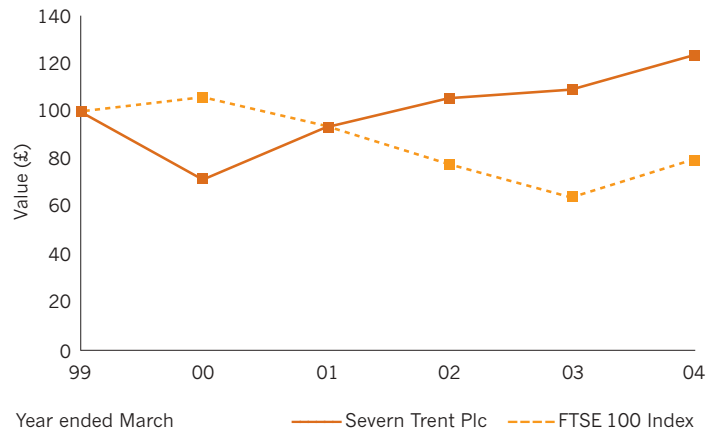
The maximum allocation that may be made to an individual executive Director in any year is such number of shares as have a market value equal to 100% of base salary. Shares are allocated annually by the Committee but are not released to executive Directors for a period of three years thereafter, provided that the TSR has achieved a prescribed ranking in comparison with a number of selected comparator companies and that the EP targets have also been met. The performance criteria are specific to each Award. For the performance periods effective from 1 April 2001, 1 April 2002 and 1 April 2003, Mr R M Walker received an allocation of shares equivalent to 100% of his salary and the remaining executive Directors received allocations equivalent to 70% of their salaries. For the 2004 award this will remain unchanged other than for Messrs J K Banyard and B Duckworth who will both receive an allocation of 85% of their salaries.

For the 2001 and 2002 Awards the comparator group consists of: AWG Plc, Kelda Plc, Pannon Group Plc, Shanks Plc, United Utilities Plc and Waste Recycling Group Plc. For the 2003 Award, the comparator group additionally contains Northumbrian Water Plc.

For the executive Directors the 2001, 2002 and 2003 LTIP awards will be triggered if the company's TSR performance is at the median or above and the EP meets the scaled targets set. EP is calculated by reference to a post tax rate of return of 7.5%. It is envisaged that an LTIP award will be made in 2004 and this will be subject to similar performance targets.

The performance period for allocations of shares made in 2001 ended on 31 March 2004. The Remuneration Committee has determined, based on the company's TSR and EP performance over the three year performance period, that the executive Directors are entitled to 100% of the shares allocated.

### Total shareholder return



Source: Thomson Financial.

This graph looks at the value, by 31 March 2004, of £100 invested in the company on 31 March 1999 compared with the value of £100 invested in the FTSE 100 Index. The FTSE 100 was chosen as the comparator because the company is a constituent of that index.

The other points plotted are the values at intervening financial year-ends.

### Post-retirement benefits

The company's policy is to offer all executive Directors membership of the Senior Staff Pension Scheme (the 'Scheme'). All current executive Directors participate in the Scheme.

The Scheme is a funded Inland Revenue approved final salary occupational pension scheme which provides:

- A normal retirement age of 60 years;
- An overall pension at normal retirement age of two-thirds of final pensionable salary, subject to the completion of 20 years' pensionable service;
- Life cover of 4 x pensionable earnings;
- A pension payable in the event of retirement on grounds of ill health;
- A spouse's pension on death.

The company has a future obligation in respect of Mr R M Walker and Mr A S Perelman, both of whom joined this Scheme after 1 June 1989 and are therefore subject to the Inland Revenue earnings cap (2003/2004: £99,000), to pay the difference between their pension entitlement based upon the relevant portion of their salary and the maximum amount payable had the cap not been in place. The obligation is unfunded.

### Forward-looking statement

The Committee will keep the existing remuneration arrangements, as detailed in this report, under review during the next year to ensure that the company's reward programmes remain competitive and provide appropriate incentives. No significant changes to the reward arrangements for executive Directors are anticipated. However, as usual there will be individual reviews of base salary, annual bonus and LTIP awards. The performance targets for incentive arrangements will also be reviewed to ensure alignment with the group strategy and the Committee also intends to review the ongoing operation of the LTIP in the course of the forthcoming financial year.

## SUMMARY REMUNERATION REPORT

CONTINUED

### Directors' service agreements and letters of engagement

The current policy of the Committee is that executive Directors are employed on contracts subject to no more than 12 months' notice, in accordance with current corporate governance best practice.

The executive Directors are required to give not less than six months' notice of termination (12 months in the case of the Group Chief Executive).

The current executive Directors, other than Mr M J Bettington, are all scheduled to leave on, or before, 31 March 2005, therefore, by that date the above contractual arrangements will cease. Going forward, it is intended that the appointments for all new executive Directors, and also in the case of Mr Bettington, will be on the basis of 12 months' notice by either party.

The new service agreements will also provide for a maximum damages payment in the case of redundancy or termination in breach of the agreement by the company of up to 175% of base salary which was calculated as a conservative pre-estimate of the value of salary, fixed benefits and on target bonus. Any damages payments will not be made automatically and will be subject to phasing and mitigation. It will also take into account a view of the extent of poor performance on the part of the executive Director. The liquidated damages payment will not include awards which have been made under the company's LTIP over which the Committee retains absolute discretion. There are no specific contractual payments or benefits which would be triggered in the event of a change in control of the company.

### Directors' emoluments

The emoluments of the Chairman, the executive Directors and fees payable to the non-executive Directors are as follows:

	Basic salary and fees			Benefits in kind <sup>3</sup>	Annual bonus £000	Other <sup>4</sup> £000	Total 2003/04 £000	Total 2002/03 £000
	Cash £000	Shares <sup>2</sup> £000	Total £000					
<b>Chairman and other non-executive Directors</b>								
T D G Arculus (Chairman)	124.2	10.0	134.2	23.2	–	6.0	163.4	154.8
E E Anstee (resigned 15.12.03)	23.6	1.3	24.9	–	–	1.7	26.6	32.9
M L Cassoni	37.9	2.8	40.7	–	–	1.6	42.3	29.4
M C Flower	48.8	2.8	51.6	–	–	0.8	52.4	44.4
M J Houston	15.7	1.8	17.5	–	–	–	17.5	–
C S Matthews <sup>1</sup>	13.6	–	13.6	–	–	–	13.6	–
J D G McAdam	26.4	2.8	29.2	–	–	0.9	30.1	27.9
F A Osborn	43.0	2.8	45.8	–	–	1.0	46.8	50.2
A H Simon (resigned 26.07.02)	–	–	–	–	–	–	–	11.5
J B Smith <sup>1</sup>	14.4	–	14.4	–	–	–	14.4	–
C Tritton (resigned 30.07.03)	10.0	0.8	10.8	–	–	0.1	10.9	32.9
<b>Executive Directors</b>								
J K Banyard	190.0	–	190.0	22.2	91.2	0.3	303.7	279.8
M J Bettington	292.5	–	292.5	21.2	132.0	–	445.7	333.8
B Duckworth	255.0	–	255.0	24.0	122.4	0.1	401.5	362.0
A S Perelman	350.0	–	350.0	28.8	164.5	0.1	543.4	512.2
R M Walker	480.0	–	480.0	35.6	230.4	0.1	746.1	611.5
<b>Total emoluments</b>	<b>1,925.1</b>	<b>25.1</b>	<b>1,950.2</b>	<b>155.0</b>	<b>740.5</b>	<b>12.7</b>	<b>2,858.4</b>	<b>2,483.3</b>

1 Mr C S Matthews' total fees are paid directly to his employer. Total fees for Mr J B Smith represent fees due but not yet paid.

2 With the exception of Messrs C S Matthews and J B Smith, all non-executive Directors received a proportion of their total fees by way of shares in the company. The gross value of those awards is included in the table above. Non-executive Directors who were either appointed or resigned during the year received time apportioned awards where applicable. The number of shares received by each non-executive Director during the year was: Mr T D G Arculus – 824; Ms M L Cassoni – 228; Mr M C Flower – 228; Dr J D G McAdam – 228; Mr F A Osborn – 228; Mr M J Houston – 133; Mr E E Anstee – 114; and Mrs C Tritton – 70.

3 Benefits in kind for executive Directors comprise the use of a motor car, fuel, private medical insurance, life assurance and an incapacity benefits scheme.

4 Other emoluments represent expenses chargeable to UK income tax paid to Directors.

Signed on behalf of the Board who approved the Remuneration Report on 7 June 2004

### M C Flower

Chairman of the Remuneration Committee

## SHAREHOLDER INFORMATION

### Key dates in 2004

#### Dividends – ordinary shares

16 June 2004	Ex-dividend date for final dividend
18 June 2004	Record date for final dividend
1 October 2004	Payment of final dividend

#### Shareholder communications

27 July 2004	Annual General Meeting at the National Exhibition Centre, Birmingham
November 2004	Announcement of half year results

### Annual General Meeting

The Annual General Meeting will be held at 2.30pm on Tuesday 27 July 2004 at the National Exhibition Centre, Birmingham. The Notice of the Meeting and a form of proxy are enclosed with this Review.

### Registrars

Lloyds TSB Registrars are the company's share registrars and they will deal with any queries you may have regarding:

- Shareholdings
- Dividends
- Lost share certificates
- Change of name or address
- Death of a shareholder
- Request for the full Report and Accounts

If you wish to have your dividends paid directly into your bank or building society account you should contact the registrars and they will send you a dividend mandate form. Alternatively, you will find a form of mandate attached to your last dividend mailing which you may complete and return to the registrars. Please note you will still receive tax vouchers at your usual address.

Their contact details are:

Lloyds TSB Registrars  
The Causeway  
Worthing  
West Sussex BN99 6DA

You can also ring them on the Severn Trent dedicated telephone line: 0870 600 3967.

Alternatively, if you have access to the Internet, you can look directly at details of your shareholder account by visiting [www.shareview.co.uk](http://www.shareview.co.uk). This is a service offered by Lloyds TSB Registrars that enables you to check your holdings in many UK companies and helps you to organise your investments electronically. You can register for this free portfolio service by logging onto [www.shareview.co.uk](http://www.shareview.co.uk) and following a simple registration process.

### Electronic proxy appointments

For this year's Annual General Meeting you may, if you wish, register the appointment of a proxy electronically by logging onto the website [www.sharevote.co.uk](http://www.sharevote.co.uk). You will need your voting reference numbers (the three 8 digit numbers shown on your form of proxy). Alternatively if you have registered for a Shareview portfolio, log onto your portfolio at [www.shareview.co.uk](http://www.shareview.co.uk) and click on Company Meetings. Please note that any electronic communication that is found to contain a computer virus will not be accepted.

Crest members may appoint a proxy electronically via Lloyds TSB Registrars (ID 7RA01).

### Low cost dealing service

Lloyds TSB Registrars also offer a low cost dealing service for

anyone who wishes to buy or sell Severn Trent Plc shares by telephone, Internet or post. To obtain further information see contact details in the left-hand column.

### Unsolicited mail

We are obliged, whenever requested, to provide copies of our shareholder register to any third parties so it is quite likely that you may receive unsolicited mail from time to time.

You can limit the amount of unsolicited mail you receive by contacting:

The Mailing Preference Service  
Freepost 22  
London W1E 7EZ

### Forward-looking statements

This document contains certain 'forward-looking statements' with respect to Severn Trent's financial condition, results of operations and business and certain of Severn Trent's plans and objectives with respect to these items.

Forward-looking statements are sometimes, but not always, identified by their use of a date in the future or such words as 'anticipates', 'aims', 'due', 'could', 'may', 'should', 'expects', 'believes', 'intends', 'plans', 'targets', 'goal' or 'estimates'. By their very nature forward-looking statements are inherently unpredictable, speculative and involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future.

There are a number of factors that could cause actual results and developments to differ materially from those expressed or implied by these forward-looking statements. These factors include, but are not limited to, changes in the economies and markets in which the group operates; changes in the regulatory and competition frameworks in which the group operates; the impact of legal or other proceedings against or which affect the group; and changes in interest and exchange rates.

All written or verbal forward-looking statements, made in this document or made subsequently, which are attributable to Severn Trent or any other member of the group or persons acting on their behalf are expressly qualified in their entirety by the factors referred to above. Severn Trent does not intend to update these forward-looking statements.

### Not an offer

This document is not an offer to sell, exchange or transfer any securities of Severn Trent Plc or any of its subsidiaries and is not soliciting an offer to purchase, exchange or transfer such securities in any jurisdiction. Securities may not be offered, sold or transferred in the United States absent registration or an applicable exemption from the registration requirements of the US Securities Act of 1933 (as amended).

### [www.severntrent.com](http://www.severntrent.com)

Shareholders are likely to find the Financial Performance section of particular interest, containing a range of shareholder information such as detailed coverage of our share price, dividend payments, key dates, our registrars as well as corporate, financial and environmental news releases and City presentations.

Our Annual Review and Annual Report and Accounts are available on the website, accessed directly via [www.severntrent.com/reports2004](http://www.severntrent.com/reports2004)

We are constantly looking at how best to provide the information our stakeholders need quickly and cost effectively. We also seek to minimise the resources used wherever possible.

If you are a shareholder you can 'do your bit'. If you currently receive the full Annual Report and Accounts why not consider switching to the Annual Review only? You can still view or download a copy of the full Annual Report and Accounts on-line at [www.severntrent.com/reports2004](http://www.severntrent.com/reports2004). You can also elect not to receive paper copies of the Annual Report and other shareholder documents. Instead you will receive an email containing a link to a website, where electronic copies of the documents can be viewed or downloaded.

Please call Lloyds TSB Registrars on 0870 600 3967 to request the Annual Review only or to register for e-delivery.

You can find out more about Severn Trent and the businesses within our group by visiting our websites.

[www.severntrent.com](http://www.severntrent.com) provides information about the group, including our corporate responsibility activity and shareholder information.

You can find out about the products and services we offer by visiting our business sites:

[www.stwater.co.uk](http://www.stwater.co.uk)  
[www.biffa.co.uk](http://www.biffa.co.uk)  
[www.stl-inc.com](http://www.stl-inc.com)  
[www.stl-analytical.co.uk](http://www.stl-analytical.co.uk)  
[www.severntrentservices.com](http://www.severntrentservices.com)  
[www.stwaterinternational.com](http://www.stwaterinternational.com)  
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[www.stutilityservices.co.uk](http://www.stutilityservices.co.uk)  
[www.severntrentproperty.com](http://www.severntrentproperty.com)  
[www.haswell.co.uk](http://www.haswell.co.uk)



For more information about Severn Trent Plc  
and its businesses see our website  
[www.severntrent.com](http://www.severntrent.com)

The paper used in the production of this report, Zanders Megamatt,  
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and sustainable forests. In addition the printing process is taken into  
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