

NORTHUMBRIAN WATER GROUP PLC
THE REMUNERATION COMMITTEE
TERMS OF REFERENCE

References to “the Committee” in these Remuneration Committee Terms of Reference shall mean the Remuneration Committee of Northumbrian Water Group plc.

References to “the Board” shall mean the Board of Directors of Northumbrian Water Group plc.

References to “NWG” or the “Company” shall mean Northumbrian Water Group plc.

References to “Group” shall mean the Company and its subsidiaries.

1. Membership

- (i) The Committee shall comprise of at least four members, each of whom shall be appointed by the Board.
- (ii) At least three members of the Committee shall be non-executive directors of NWG who are independent of management and free from any business or other relationship which could interfere with the exercise of their independent judgement. The Chairman of the Company, whilst not considered independent for this purpose, may also be a member of the Committee.
- (iii) The Board shall appoint the Committee Chairman and determine the period for which they shall hold office. The Chairman of the Company shall not be appointed as Chairman of the Committee, but may be appointed as a member of the Committee.
- (iv) Care shall be taken to minimise the risk of any conflict of interest that might be seen to give rise to an unacceptable influence. Where possible, the Chairman and members of the Committee shall be rotated on a regular basis.

2. Secretary

The Company Secretary or his nominee shall act as the Secretary of the Committee.

3. Quorum

The quorum necessary for the transaction of business shall be two independent non-executive directors. A duly convened meeting of the Committee at which a quorum is present shall be competent to exercise all or any of the authorities, powers and discretions vested in or exercisable by the Committee.

4. Meetings

The Committee shall meet not less than once a year and at such other times as the Chairman of the Committee shall require.

5. Notice of Meetings

- (i) Meetings of the Committee shall be called by the Secretary of the Committee.
- (ii) Unless otherwise agreed, notice of each meeting confirming the venue, time and date together with an agenda of items to be discussed and supporting papers (where relevant), shall be forwarded to each member of the Committee and any other person required to attend, no fewer than five working days prior to the date of the meeting.
- (iii) The Managing Director shall have the right to address any meeting of the Committee; others may be called upon or shall be able to speak by prior arrangement with the Chairman of the Committee.

6. Reports and Minutes of Meetings

- (i) The Chairman of the Committee will report to the Board the main items of business addressed at each meeting of the Committee.
- (ii) The Secretary shall minute the proceedings and resolutions of all Committee meetings, including the names of those present and in attendance.
- (iii) Minutes of Committee meetings shall be circulated to all non-executive directors of the Company.

7. Annual General Meeting

The Chairman of the Committee shall attend the Annual General Meeting prepared to respond to any shareholder questions on the Committee's activities.

8. Duties

The Committee shall:

- (i) Determine and agree with the Board the framework or broad policy for the Remuneration of the Chairman of the Company, the Managing Director, Finance Director, and all other executive directors of the Company, and such other members of the executive management of the Company or its subsidiaries as it is designated to consider from time to time by the Board;
- (ii) Ensure that no director or manager shall be involved in any decisions as to his or her own remuneration. The Committee will also review and

recommend to the Board the remuneration of the Company Secretary, in order to assure and maintain his independence;

- (iii) Ensure that the policy developed is sufficient to attract, retain and motivate directors and management of the quality required to run the Company and the Group successfully, but avoids paying more than is necessary for this purpose or rewarding poor performance;
- (iv) In determining such policy, take into account all factors which it deems necessary. The objective of such policy shall be to ensure that members of the executive management of the Company and its subsidiaries are provided with appropriate incentives to encourage enhanced performance and are, in a fair and responsible manner, rewarded for their individual contributions to the success of the Company. The Committee shall also liaise with the Nomination Committee to ensure that the remuneration of newly appointed executives is within the Company's overall policy;
- (v) Determine targets for any performance related pay schemes operated by the Company and ask the Board, when appropriate, to seek shareholder approval for any long term incentive arrangements;¹
- (vi) Within the terms of the agreed policy, determine the total individual remuneration package of the Chairman of the Company and each executive director including, where appropriate, bonuses, incentive payments and share options;
- (vii) Consult with the Chairman and/or Managing Director when determining the remuneration packages for other executive directors;
- (viii) Determine the policy for and scope of pension arrangements, service agreements, termination payments and compensation commitments for all executive directors;
- (ix) If considered appropriate, make recommendations to the Remuneration Committee of Northumbrian Water Limited on the salary and terms of the executive directors and Chairman of Northumbrian Water Limited;
- (x) In determining such packages and arrangements, give due regard to the comments and recommendations of the Combined Code (in particular Schedule A) as well as the UK Listing Authority's Listing Rules and associated guidance;
- (xi) Review and compare, from time to time, the remuneration packages of executive directors of other listed water and utility companies and companies in the same index;

¹ A long term incentive is defined as an arrangement, whereby a payment either in shares or in cash, is paid to an Executive at least two years after he was invited into the scheme and is not based on that year's performance.

- (xii) Ensure that provisions regarding disclosure of remuneration including pensions, as listed in the Directors' Remuneration Report Regulations 2002, are fulfilled; and
- (xiii) Make whatever recommendations to the Board it deems appropriate and consider and approve the report to shareholders to be included in the Company's Annual Report and Accounts.

9. Authority

- (i) The Committee is authorised by the Board to seek any information it requires from any employee of the Company in order to perform its duties.
- (ii) In connection with its duties the Committee is authorised by the Board to select, set the terms of reference for and appoint remuneration consultants, at the Company's expense. When appointing consultants, the Committee shall have regard to the independence of such consultants and whether or not they have any other connection with the Company.
- (iii) The Committee can seek the advice and assistance of any of the Company's executives, subject to its duty in paragraph 8(ii) above. It shall also ensure that any such role of an executive is clearly separated from their role within the business, in order to avoid conflicts of interest.

10. Matters Outside of the Committee's Responsibility

- (i) The remuneration of non-executive directors shall be a matter for the executive members of the Board, in consultation with the Chairman of the Company.
- (ii) The Remuneration Committee of Northumbrian Water Limited is authorised to set the remuneration of the executive directors and Chairman of Northumbrian Water Limited and to determine the salary and other terms and conditions of service of the senior management of Northumbrian Water Limited and to approve any contract of employment or related contract with any such manager.
- (iii) The Chairman will check and authorise the Managing Director's expenses and the Finance Director of the Company will check and authorise the expenses of the Chairman of the Company.