Application has been made to the UK Listing Authority and to the London Stock Exchange plc (the "London Stock Exchange") for the whole of the issued ordinary share capital of Northumbrian Water Group plc (the "Company") to be admitted to the official list of the UK Listing Authority (the "Official List") and to trading on the London Stock Exchange's market for listed securities. It is expected that admission of the Ordinary Shares to the Official List will become effective, and that dealings in the Ordinary Shares will commence, at 8.00 a.m. on 23 September 2003.

A copy of this document, which comprises listing particulars relating to the Company prepared in accordance with the listing rules of the UK Listing Authority (the "Listing Rules") made pursuant to Section 74(4) of the Financial Services and Markets Act 2000, has been delivered for registration to the Registrar of Companies in England and Wales in accordance with Section 83 of the Financial Services and Markets Act 2000.

The directors of the Company (the "Directors"), whose names appear on page 3 of this document, accept responsibility for the information contained in this document. To the best of the knowledge and belief of the Directors (who have taken all reasonable care to ensure that such is the case), the information contained in this document is in accordance with the facts and does not omit anything likely to affect the import of such information.

No Ordinary Shares have been marketed to, nor are any available for purchase in whole or in part by, the public in the United Kingdom or elsewhere in connection with admission to the Official List.

THIS DOCUMENT DOES NOT CONSTITUTE AN OFFER OR INVITATION TO ANY PERSON TO SUBSCRIBE FOR OR PURCHASE ANY SECURITIES IN THE COMPANY OR ANY OTHER ENTITY.

NORTHUMBRIAN WATER GROUP PLC

(Incorporated in England and Wales under the Companies Act 1985 Registered Number 4760441)

Admission to the Official List and to trading on the London Stock Exchange's market for listed securities

Sponsor and Broker
Collins Stewart Limited

SHARE CAPITAL

(immediately following Admission)

Authorised			*Issued*	
Amount	*Number*		*Amount*	*Number*
£70,000,000	700,000,000	Ordinary Shares of 10p each	£51,862,384.50	518,623,845

Collins Stewart Limited ("Collins Stewart") is regulated by the Financial Services Authority and is acting exclusively for the Company and no-one else in connection with Admission. Collins Stewart will not regard any other person as its customer or be responsible to any other person for providing the protections afforded to customers of Collins Stewart nor for providing advice in relation to the transactions and arrangements detailed in this document. Collins Stewart is not making any representation or warranty, express or implied, as to the contents of this document.

Copies of this document will be available free of charge during normal business hours on any weekday (except Saturdays, Sundays and public holidays) at the offices of Collins Stewart, 9th Floor, 88 Wood Street, London EC2V 7QR from the date of this document until the date falling one month after Admission.

Risk factors in relation to the Business are brought to your attention in Part 3 of this document.

CONTENTS

DIRECTORS, COMPANY SECRETARY AND ADVISERS

Directors	Sir Frederick Holliday, *Non-Executive Chairman* John Cuthbert, *Managing Director* Christopher Green, *Finance Director* Sir Patrick Brown, *Non-Executive Director** Martin Nègre, *Non-Executive Director** Alain Chaigneau, *Non-Executive Director* Jacques Pétry, *Non-Executive Director* *Considered by the Board to be independent
Registered Office	Northumbria House Abbey Road Pity Me Durham DH1 5FJ
Company Secretary	Martin Parker
Sponsor and Broker to the Company	Collins Stewart 9th Floor 88 Wood Street London EC2V 7QR
Solicitors to the Company	Simmons & Simmons CityPoint One Ropemaker Street London EC2Y 9SS
Reporting Accountants and Auditors	Ernst & Young LLP Citygate St James' Boulevard Newcastle upon Tyne NE1 4JD
Solicitors to the Sponsor	Linklaters One Silk Street London EC2Y 8HQ
Principal Bankers to the Company	Deutsche Bank Winchester House 1 Great Winchester Street London EC2N 2DB
Registrars and Paying Agent	Capita Registrars The Registry Bourne House 34 Beckenham Road Beckenham Kent BR3 4TU

GLOSSARY OF TERMS

The following terms are used throughout this document.

"Appointed Activities"	means regulated water and sewerage activities carried out by a water company pursuant to an instrument of appointment under the WIA;
"DGWS"	means the Director General of Water Services who is appointed for a fixed term by the Secretary of State;
"Enforcement Order"	means an enforcement order, final enforcement order or provisional enforcement order, each as referred to and defined in the WIA;
"Enterprise Act"	means the Enterprise Act 2002;
"Environment Agency"	means the Environment Agency of England and Wales;
"IDOK"	means an interim determination of K as provided for in part 4 of condition B of the Licence;
"K"	means the adjustment factor set for each year by the DGWS by which charges made by Regulated Companies for water supply and sewerage services may be increased, decreased or kept constant relative to RPI;
"Licence" or "Instrument of Appointment"	means the instrument of appointment of NWL as a water undertaker and as a sewerage undertaker (as modified to incorporate changes to the structure of NWL) granted by the Secretary of State under Sections 11 and 14 of the Water Act 1989 (now Sections 6, 7, 11 and 12 of the WIA);
"Non-Appointed Activities"	activities other than Appointed Activities carried out by a water company regulated by Ofwat;
"Ofwat"	means the Office of Water Services (or any successor body) being the Office of the DGWS;
"Periodic Review"	means the periodic review of K (as that term is defined in the Instrument of Appointment as provided for in condition B of the Instrument of Appointment);
"Periodic Review Effective Date"	means the date with effect from which the new K (as the term is defined in the Instrument of Appointment) will take effect, following a Periodic Review;
"Periodic Review Period"	means the five year period commencing on a Periodic Review Effective Date;
"Regulated Company"	means a company holding an instrument of appointment as a water undertaking or water and sewerage undertaking under the WIA;
"Retail Price Index" or "RPI"	means the all items Retail Price Index for the United Kingdom published by the Office for National Statistics or at any future date such other index of retail prices as may have then replaced it for the purposes of the DGWS's determination of price limits for water and sewerage services;
"Special Administration"	means the insolvency process governing Regulated Companies under Sections 23 to 26 of the WIA;

"Special Administration Order"	means an order of the High Court under Sections 23 to 25 of the WIA under the insolvency process governing Regulated Companies;
"Special Administration Period"	means the period beginning with the presentation of a petition for Special Administration under Section 24 of the WIA and ending with the making of a Special Administration Order or the dismissal of the petition;
"Special Administrator"	means the person appointed by the High Court under Sections 23 to 25 of the WIA to manage the affairs, business and property of the Regulated Company during the period in which the Special Administration Order is in force;
"Substantial Effect Clause"	means a clause which may be contained in the licence of a Regulated Company and which is contained in the Licence at part 4 of condition B, pursuant to which the Regulated Company may, if so permitted by the conditions of its licence, request price limits to be re-set if the Appointed Activities either (1) suffers a substantial adverse effect which could not have been avoided by prudent management action or (2) enjoys a substantial favourable effect which is fortuitous and not attributable to a prudent management action;
"Water Bill"	means the Water Bill currently before Parliament which was introduced in the House of Lords on 19 February 2003; and
"WIA"	means the United Kingdom Water Industry Act 1991 (as amended by subsequent legislation including the Competition and Service (Utilities) Act 1992 and the Water Industry Act 1999).

DEFINITIONS

The following definitions apply throughout this document, unless the context otherwise requires:

"Act"	the Companies Act 1985 (as amended);
"Admission"	the admission of the Ordinary Shares to the Official List and to trading on the London Stock Exchange's market for listed securities;
"Affiliate"	in relation to a body corporate, any subsidiary undertaking or parent undertaking of such body corporate and any subsidiary undertaking of any such parent undertaking for the time being as those terms are defined by Section 258 of the Act;
"AIM"	the Alternative Investment Market of the London Stock Exchange;
"AIM Admission"	admission of the share capital of the Company to AIM, effective on 23 May 2003, pursuant to an admission document dated 21 May 2003;
"Articles"	the articles of association of the Company as at the date of this document;
"Atlantic"	Atlantic Water Limited;
"Atlantic Acquisition"	the acquisition of the entire issued share capital of Atlantic, the then holding company of NSL, by the Company effective on 23 May 2003;
"Atlantic Group"	Atlantic and its subsidiary undertakings;
"Board"	the board of Directors of the Company for the time being, including any duly constituted committee of the Directors;
"Business"	the business of the Group;
"Collins Stewart"	Collins Stewart Limited of 9th Floor, 88 Wood Street, London EC2V 7QR;
"Combined Code"	the combined code on the principles of good governance and code of best practice prepared by the Committee on Corporate Governance, chaired by Sir Ronald Hampel, published in June 1998 and appended to, but not forming part of the Listing Rules;
"Company" or "NWG"	Northumbrian Water Group plc incorporated with registered number 4760441;
"Competition Act"	the Competition Act 1998;
"Competition Commission"	the independent public body established by the Competition Act;
"Completion"	the completion of the Atlantic Acquisition;
"CREST"	the system of paperless settlement of trades and the holding of shares without share certificates administered by CRESTCo Limited in accordance with the Uncertificated Securities Regulations 1995 (SI 1995 No. 3272);
"Deutsche Bank"	Deutsche Bank AG London of Winchester House, 1 Great Winchester Street, London EC2N 2DB;
"Directors"	the directors of the Company, being Sir Frederick Holliday, John Cuthbert, Christopher Green, Sir Patrick Brown, Martin Nègre, Alain Chaigneau and Jacques Pétry, and "Director" shall mean any one of them;

"Draft Business Plan"	the draft business plan submitted by NWL to the DGWS on 15 August 2003 for the period 2005 to 2010, as part of the 2004 Periodic Review in 2004;
"EIB"	European Investment Bank;
"Final Business Plan"	the final business plan to be submitted by NWL to the DGWS in April 2004 for the period 2005 to 2010, as part of the next Periodic Review in 2004;
"Final Salary Scheme"	the Northumbrian Water Pension Scheme, being the principal pension scheme operated by the Group;
"Fitch"	Fitch Ratings Ltd.;
"Group"	the Company and its subsidiary undertakings;
"Listing Rules"	the listing rules of the UK Listing Authority;
"London Stock Exchange"	London Stock Exchange plc;
"Lyonnaise Europe"	Lyonnaise Europe plc;
"Model Code"	the Model Code for Securities Transactions by Directors for the time being as adopted by the Company in accordance with the Listing Rules;
"NEW"	North East Water Limited (in members' voluntary liquidation) of Fernwood House, Fernwood Road, Jesmond, Newcastle upon Tyne NE2 1TS;
"Northumbrian Water LTIP"	the proposed Northumbrian Water Group plc Long Term Incentive Plan 2003;
"Northumbrian Water SIP"	the proposed Northumbrian Water Group plc Share Incentive Plan 2003;
"NSL"	Northumbrian Services Limited (formerly OSUK), the immediate holding company of NWL;
"NSL 2006 Bonds"	the Eurobonds due 28 June 2006 bearing interest at the rate of 8.625 per cent.;
"NSL Group"	NSL and its subsidiary undertakings;
"NWL"	Northumbrian Water Limited, the principal subsidiary of NSL;
"NWL North"	NWL's water and sewerage operations serving the area set out in the Licence in the north east of England;
"NWL South"	NWL's water operations serving the area set out in the Licence in the south east of England;
"Official List"	the official list of the UK Listing Authority;
"Ofwat Consultation Paper"	the consultation paper published by Ofwat in June 2003 on the Atlantic Acquisition;
"Ofwat Position Paper"	the position paper published by Ofwat in August 2003 on the Atlantic Acquisition;
"Ordinary Shares"	the ordinary shares of 10p each in the share capital of the Company;
"OSUK"	Ondeo Services UK plc (now known as Northumbrian Services Limited);
"Placing"	the placing of 388,967,884 Ordinary Shares pursuant to the Placing Agreement, further details of which are set out in paragraph 11.1(D) of Part 7 of this document;

"Placing Agreement"	the placing agreement dated 16 May 2003 and entered into between the Company, Collins Stewart, Deutsche Bank, Ecofin Limited and another;
"Private Finance Initiative"	the Private Finance Initiative within the meaning given pursuant to the Construction Contracts (England and Wales) Exclusion Order 1998;
"Revised Combined Code"	the revised version of the Combined Code published in July 2003 and derived from a review of the role and effectiveness of non-executive directors by Derek Higgs and a review of audit committees by a group led by Sir Robert Smith;
"S&P"	Standard & Poor's, a division of The McGraw-Hill Companies, Inc.;
"Secretary of State"	the Secretary of State for the Environment;
"Shareholders"	the holders of Ordinary Shares;
"Share Incentive Schemes"	the Northumbrian Water LTIP and Northumbrian Water SIP;
"Sponsorship Agreement"	the agreement dated 18 September 2003 between Collins Stewart and the Company, relating to the Admission, further details of which are set out in paragraph 11.2(A) of Part 7 of this document;
"subsidiary"	as defined in Section 736 of the Act;
"subsidiary undertaking"	as defined in Section 258 of the Act;
"Suez"	Suez S.A. (formerly Suez Lyonnaise) of 16 rue de la Ville-L'Eveque, 75383 Paris, France;
"Suez Environnement"	Suez Environnement S.A. of 18 Square Edouard VII, 75009 Paris, France;
"Suez Group"	Suez and any subsidiary undertakings of Suez from time to time;
"Suez Lyonnaise"	Suez Lyonnaise des Eaux (now known as Suez S.A.) of 16 rue de la Ville-L'Eveque, 75383 Paris, France;
"UK" or "United Kingdom"	the United Kingdom of Great Britain and Northern Ireland; and
"UKLA" or "UK Listing Authority"	the Financial Services Authority acting in its capacity as the competent authority for the purposes of Part VI of the Financial Services and Markets Act 2000 and in exercise of its function in respect of the admission of securities to the Official List.

PART 1

Information on the Group

1. Introduction

The Company was incorporated on 12 May 2003 to acquire the entire issued ordinary share capital of Atlantic, which is the immediate holding company of NSL.

The Company acquired the entire issued ordinary share capital of Atlantic from certain Affiliates of Suez, a utility company listed on the Paris, Brussels, Zurich, Luxembourg and New York stock exchanges in consideration for (i) the payment of £880 million (the "Cash Payment") to those Affiliates, and (ii) the allotment of Ordinary Shares representing 25 per cent. of the share capital of the Company upon the AIM Admission. The Cash Payment comprised £344 million, being the net proceeds of the Placing, and £536 million of debt finance provided to the Company and underwritten by Deutsche Bank.

The Atlantic Acquisition completed and the Ordinary Shares were admitted to trading on AIM on 23 May 2003.

2. History and Overview of the Group

The Company, a leading UK water and sewerage business, owns both regulated and non-regulated operations in the water and sewerage sector in the UK together with other non-regulated businesses. NWL is the company's principal subsidiary, and its business comprises both Appointed Activities and Non-Appointed Activities. NWL's activities represented approximately 87 per cent. of the turnover of the NSL Group in the financial year ended 31 December 2002, and NSL's other non-regulated activities represented approximately 13 per cent. of the turnover of the NSL Group in that financial year. NWL is regulated by the DGWS, the Environment Agency and the Drinking Water Inspectorate. Details of the regulatory regime to which NWL is subject are set out in Part 2 of this document.

In 1989 the water industry in England and Wales was privatised following the passing of the Water Act 1989, and NWL's then holding company, Northumbrian Holdings Limited (at the time called Northumbrian Water Group plc), was listed on the Official List. In 1995, Suez, through Lyonnaise Europe, acquired Northumbrian Holdings Limited (at the time still known as Northumbrian Water Group plc). In 1996 a new holding company structure was put in place with the creation of NSL (which was then called Northumbrian Water Group plc) as the new holding company of Northumbrian Holdings Limited (which had by then changed its name from Northumbrian Water Group plc to Northumbrian Holdings plc, and which subsequently changed its name to Northumbrian Holdings Limited on its re-registration as a private limited company).

In 1996 North East Water plc (also owned at the time by Lyonnaise Europe) was merged with NWL. Then in 2000, Essex and Suffolk Water plc (owned at the time by NSL) was merged with NWL, and at the same time a single layer of management was created, responsible for NSL and NWL.

Although the businesses of NWL, North East Water plc and Essex and Suffolk Water plc have now been fully integrated, NWL still trades under the historical names of Northumbrian Water in the north and Essex and Suffolk Water in the south.

3. The Group's Regulated Business

Northumbrian Water Limited

The turnover of NWL for the 12 month period ended 31 December 2002, amounted to approximately £439.2 million, of which approximately £423.6 million related to Appointed Activities and approximately £15.6 million related to Non-Appointed Activities. NWL serves three geographically non-contiguous areas (Essex and Suffolk in the south east of England and Northumbria in the north east of England) providing diversification in terms of customers, which comprise both household and non-household users.

NWL is a licensed water and sewerage undertaker operating within the regulatory framework established under the WIA. NWL's principal activities comprise the supply of potable water by both NWL North and NWL South and the collection, treatment and disposal of sewage and sewage sludge by NWL North. NWL North also has a raw water system for industrial customers in Teesside which is part of its Appointed Activities.

On an aggregate basis, NWL:

- serves an area of approximately 12,200 km^2;
- supplies potable water to a population of approximately 4.3 million; and
- provides sewerage services to a population of approximately 2.6 million.

Appointed Activities

NWL North

The NWL North business serves an area of approximately 9,400 km^2 as set out in the Licence, supplying potable water and sewerage services to a population of approximately 2.6 million. As at 31 March 2003 its key assets as notified to Ofwat included:

- 16 impounding reservoirs;
- 21 wells and boreholes;
- 37 principal water treatment works;
- 231 water boosting pumping stations;
- 16,789 km of water mains;
- 677 sewage pumping stations;
- 428 sewage treatment works; and
- 15,484 km of sewers.

NWL South

The NWL South business serves an area of approximately 2,800 km^2 as set out in the Licence, supplying potable water to a population of approximately 1.7 million. As at 31 March 2003, its key assets as notified to Ofwat included:

- 2 impounding reservoirs;
- 25 wells and boreholes;
- 30 principal water treatment works;
- 90 water booster pumping stations; and
- 8,425 km of water mains.

NWL South is a water only business; sewerage services in this region are provided by Thames Water and Anglian Water. NWL provides billing services for Thames Water and for Anglian Water, although the billing services for the latter are restricted to some local authority and housing association properties.

Non-Appointed Activities

Within NWL the main Non-Appointed Activity is the operation of the Kielder reservoir for the regulation of river flows on behalf of the Environment Agency. Other Non-Appointed Activities include leisure and recreation, fisheries and a property solutions business which provides information services to solicitors. Non-Appointed Activities represented three per cent. of turnover of the NSL Group for the 12 month period ended 31 December 2002.

4. The Group's Non-Regulated Businesses

The Group's principal non-regulated businesses (which differ from Non-Appointed Activities in that they are not carried out by NWL, being the Regulated Company) are conducted by various entities, all being subsidiaries of the Company except for Ayr Environmental Services Limited which is an associate of the Company. The figures set out below for each of these respective entities have been extracted from the consolidation schedules used to prepare the audited consolidated accounts of the NSL Group. Shareholders should read the full text of this document and not rely solely on the information set out below.

Entec UK Limited

Entec UK Limited is an environmental and engineering consultancy. Its turnover for the 12 month period ended 31 December 2002 was approximately £33.4 million.

Fastflow Pipeline Services Limited

Fastflow Pipeline Services Limited provides network renewal and refurbishment services, focussed mainly on no-dig technologies. Its turnover for the 12 month period ended 31 December 2002 was approximately £18.4 million.

Analytical & Environmental Services Limited

Analytical & Environmental Services Limited is an analytical business that provides sampling and analysis of air quality, contaminated land, water and waste water. Its turnover for the 12 month period ended 31 December 2002 was approximately £11.7 million.

Lyonnaise des Eaux (Gibraltar) Limited

Lyonnaise des Eaux (Gibraltar) Limited operates a governmental concession, on behalf of the Government of Gibraltar, to operate and maintain Gibraltar's water and sewerage network and, amongst other things, supply water to customers. The Government of Gibraltar has a 33 per cent. minority shareholding in this business. Its turnover for the 12 month period ended 31 December 2002 was approximately £7.9 million.

Ayr Environmental Services Limited

Ayr Environmental Services Limited is a company established to undertake a BOOT ("Build-Own-Operate-Transfer") project under the Private Finance Initiative to provide waste water treatment at three new plants in the west of Scotland as well as associated sludge treatment and disposal (the "Ayrshire Project"). Its turnover for the 12 month period ended 31 December 2002 was approximately £5.2 million. However, as this company is accounted for as an associate its contribution to the consolidated turnover of the NSL Group was zero. This long term project is in the final stages of commissioning.

Caledonian Environmental Services plc

Caledonian Environmental Services plc is a company established to undertake a BOOT project under the Private Finance Initiative to provide waste water treatment at a new plant in the east of Scotland as well as associated sludge treatment and disposal (the "CES Project"). Its turnover for the 12 month period ended 31 December 2002 was approximately £1.0 million. There is currently a delay in achieving final completion of this project which gives rise to a right of termination under the terms of certain project documents by certain parties including Caledonian Environmental Services plc. However, all relevant parties are currently negotiating a solution intended to avoid the risk of termination and with a view to the satisfactory completion of the project in the first quarter of 2004.

A proportion of the turnover of Entec UK Limited, Fastflow Pipeline Services Limited and Analytical & Environmental Services Limited has been generated by trade within the NSL Group.

5. Financial Information

The trading record of NSL, which until the Atlantic Acquisition was the immediate holding company of the NSL Group, which is extracted without adjustment from the accountants' report set out in Part 4 of this document, is summarised below and only includes key pieces of information. Shareholders should read the full text of this document and not rely solely on the information summarised in this section.

	Year ended 31 December (£'m)			*Three month period to 31 March*
	2000	*2001*	*2002*	*2003*
	£m	*£m*	*£m*	*£m*
Turnover	497.5	489.4	504.0	128.1
Operating profit	183.6	155.9	165.3	39.7
Exceptional profit on disposal of associate	—	29.4	—	—
Other	4.1	4.3	2.1	1.3
Net interest payable	(81.8)	(79.7)	(75.2)	(21.4)
Profit before tax	105.9	109.9	92.2	19.6
Taxation	(19.5)	(11.2)	(0.5)	(3.4)
Profit after tax	86.4	98.7	91.7	16.2
Minority Interest	(0.1)	(0.6)	0.1	(0.3)
Dividends	(57.0)	(59.6)	(62.3)	—
Retained profit	29.3	38.5	29.5	15.9

Deferred taxation

The NSL Group's effective tax rates have historically been low reflecting the availability of capital allowances. In 2002, the NSL Group adopted the Financial Reporting Standard No. 19 "deferred taxation" which accounts for deferred tax on a full provisioning basis having discounted future tax assets and liabilities to reflect the time value of money. The results as shown above and in the accountants' report in Part 4 of this document reflect the consistent application of this policy for the three years and three months ended 31 March 2003. Listed companies will, from 2005, be required to prepare financial statements under International Accounting Standards which currently prohibit the use of discounting in calculating deferred tax liabilities. As a consequence, the future post tax profitability of the Group may be affected along with that of other companies in the sector.

Debt financing

As at 31 December 2002 the NSL Group had net debt of approximately £1,116 million. On 23 May 2003 Deutsche Bank provided a debt facility of £935 million to the Company, of which £536 million was used to finance the Atlantic Acquisition. Immediately following Completion of the Atlantic Acquisition, the net debt of the Group increased. For further details see Part 6 of this document.

As a result of the increased level of debt within the Group brought about by the Atlantic Acquisition, S&P downgraded the corporate credit rating of NWL (the "Credit Rating Downgrade"). S&P's confirmed corporate credit rating for NWL is now BBB.

NWL has sufficient cash flows to support its debt obligations and the Board does not anticipate a need for the Group to raise money from the debt market until after the Periodic Review which is expected to be completed in November 2004. However, in keeping with the Company's ongoing review of its credit quality and financial position, the Company is considering, amongst other options, raising further debt capital against the revenues generated by its Kielder reservoir operations and using the proceeds to repay existing debt under the Amended and Restated Facilities Agreement (further details of this are set out in paragraph 11.1(E) of Part 7 of this document).

On 29 July 2003, the remaining debt facility of £686 million underwritten by Deutsche Bank was syndicated to a new group of lenders under the terms of the Amended and Restated Facilities Agreement (see paragraph 11.1(E)) of Part 7 of this document for further details).

The EIB has waived its right to the immediate repayment of loans to the aggregate value of £376 million, resulting from the change of ownership of NWL pursuant to the Atlantic Acquisition. The EIB will reassess the situation with regard to the credit standing of the Group on 30 April 2004 and determine whether to extend the waiver. In any event, the Company has a back-up facility in place until 23 May 2005 to cover this amount should the EIB require repayment of the loans (further details of this are set out in paragraph 11.1(E) of Part 7 of this document).

Ofwat, in the Ofwat Position Paper, addressed issues raised in response to the Ofwat Consultation Paper on NWL's credit rating. Your attention is drawn to paragraph 4 of Part 2 of this document where more details on this issue are set out.

Pension Scheme Valuation

The most recent actuarial valuation of the Final Salary Scheme (as defined in paragraph 10.1 of Part 7 of this document) was carried out as at 31 December 2001 and showed that the scheme had an overall surplus of approximately £37 million. The trustees of the scheme have received actuarial advice that, if the results of this actuarial valuation were projected forward to 30 June 2003, using the 31 December 2001 assumptions, the scheme would have had an overall deficit as at that date of approximately £36 million.

However, the trustees of the scheme have received further actuarial advice that, were the valuation to be carried out using the assumptions appropriate to the market conditions as at 30 June 2003, the fund would have had an overall deficit as at that date of approximately £81 million.

NWL submitted its Draft Business Plan to Ofwat in August 2003 which included proposals to increase contribution rates with effect from January 2006, following the acutarial valuation which will be carried out as at 31 December 2004. These proposals will seek to address the deficits over the remaining life of the relevant employees. NWL will reassess its proposals before submitting its Final Business Plan in April 2004.

Further details of the scheme are set out in paragraph 10 of Part 7 of the document.

6. Current Trading and Prospects

Since the date of the audited accounts for NSL (which until the Atlantic Acquisition was the immediate holding company of the NSL Group) for the year ended 31 December 2002, there has been no significant change in the Group's Business, trading or prospects save for the Atlantic Acquisition, Placing, related financing and Credit Rating Downgrade.

The trading performance of the Group up until the date of this document has been satisfactory and in line with the Directors' expectations. The Directors are not aware of any factors that would have a material adverse impact on the trading performance of the Group for the financial period ending 31 March 2004, save for the costs in relation to the Atlantic Acquisition, Placing and related financing.

The Directors therefore believe the prospects for the Group for at least the current financial year are favourable.

The Group intends to maintain its focus on delivering a quality service to its customers, whilst seeking to deliver further efficiencies in its performance. The Directors believe that NWL remains on target to deliver its investment obligations by the end of the current regulatory period. NWL submitted its Draft Business Plan to Ofwat in August 2003 and expects to submit its Final Business Plan in April 2004. The outcome of the Periodic Review process, which is expected to be finalised in November 2004, is likely to have a significant impact on the future financial performance of the Group. NWL also submitted an IDOK application to Ofwat on 11 September 2003. If the IDOK application is successful, Ofwat will allow NWL to increase its prices to customers in April 2004. This will reduce any potential further increase in prices which may arise following the next Periodic Review (for further details on the IDOK application and Periodic Review, your attention is drawn to paragraph 3 of Part 3).

Ofwat published its Levels of Service Report (the "Levels of Service Report") for 2002-2003 on 4 September 2003. Ofwat's Overall Performance Assessment ("OPA") for water and sewerage companies ranks NWL eighth out of ten, and the company received four Ofwat stars for quality of service.

In the Levels of Service Reports for each of 2000-01 and 2001-02, NWL was ranked in first place in the OPA and it received seven stars. The Directors believe that NWL's lower ranking and loss of stars is attributable mainly to a number of sewer flooding incidents which were beyond NWL's control and which resulted form unusually heavy rainfall. The Directors do not believe that NWL's ranking in the Levels of Service Report constitutes a material worsening of NWL's performance insofar as such performance is within the control of management.

7. Reasons for Admission to the Official List

The AIM Admission provided a means of access to the equity financing required for the purpose of the Atlantic Acquisition. Since the Atlantic Acquisition it has been the Company's intention to seek Admission as soon as reasonably practicable.

The Directors believe that the Company will be well placed to achieve greater liquidity in its shares as a company whose shares are admitted to the Official List and to trading on the London Stock Exchange.

8. Directors and Company Secretary

Sir Frederick Holliday, Non-Executive Chairman, aged 67

Sir Fred was appointed as Chairman of the Company on 23 May 2003. He has been Chairman of NWL since 2000 and a director of Northumbrian Holdings Limited (then called Northumbrian Water Group plc) since 1991, becoming Chairman in 1993. Sir Fred was also appointed as a director of NSL (then called Northumbrian Water Group plc) in 1996. Sir Fred had a distinguished academic career during which he was Vice-Chancellor of Durham University from 1980 to 1990. He was also a director of Shell UK from 1980 to 1989 and Chairman of the Go-Ahead Group plc until October 2002. Sir Fred is also the Chairman of Brewin Dolphin Holdings plc and is Vice President of the British Trust for Ornithology and the Freshwater Biological Association.

John Cuthbert, Managing Director, aged 50

John Cuthbert holds an MBA from Durham University Business School and qualified as an accountant with Peat Marwick Mitchell, now part of KPMG. John joined the water industry in 1991 and was appointed Managing Director of North East Water in 1993 following the merger between Newcastle and Gateshead Water plc and Sunderland and South Shields Water plc, the first merger in the privatised regime and a position he held during the Periodic Review in 1995. Following the acquisition of Northumbrian Holdings Limited (at the time called Northumbrian Water Group plc) in 1995, John transferred within the group to become Managing Director of Essex and Suffolk Water plc. Having completed the Periodic Review in 1999 and following the merger with Essex and Suffolk Water plc, John took over as Managing Director of NWL in 2001.

Christopher Green, Finance Director, aged 48

Chris Green qualified as a chartered accountant with Arthur Young, now Ernst & Young. Chris joined Northumbrian Holdings Limited (at the time called Northumbrian Water Group plc) in 1990, helping to diversify the group's activities including the development of a substantial waste management subsidiary over a five year period from 1992. He was appointed Finance Director in 1997, overseeing the merger of NWL and Essex and Suffolk Water plc in 2000 and the raising of over £700 million through debt capital markets to fund their capital expenditure programme. Chris became Finance Director of the Company on 23 May 2003.

Sir Patrick Brown, Non-Executive Director, aged 63

Sir Patrick Brown held various positions in the Department of Transport and the Department of the Environment between 1972 and 1990, in which year he became the Second Permanent Secretary and Chief Executive of the Property Services Agency (Department of the Environment). In 1991 he became the Permanent Secretary for the Department of Transport, a post he held until 1997. In 1999 he became a non-executive director of Go-Ahead plc, and he became Chairman of the Go-Ahead Group plc in 2002, a post which he currently holds. He became a non-executive director of the Company on 12 May 2003.

Martin Nègre, Non-Executive Director, aged 56

Martin Nègre is the Chairman of Ecofin Water & Power Opportunities plc, an investment trust focussed on utilities. Martin was, until June 2001, the Chief Executive Officer of NSL (then known as Northumbrian Water Group plc), then a subsidiary of Suez Lyonnaise, and Suez's Chief Corporate Representative in the United Kingdom. Prior to coming to the United Kingdom, Martin was with Suez for seven years, as International Director in Paris and then Asia-Pacific President in Hong Kong and Singapore. Before that, Martin spent 21 years as a senior executive of Alsthom and then GEC Alsthom, the Anglo/French engineering company, where he was the Chief Executive of the power generation division. He became a non-executive director of the Company on 12 May 2003.

Alain Chaigneau, Non-Executive Director, aged 51

Alain Chaigneau was a non-executive director of NWL from 1 April 2000 to 23 May 2003. He was appointed in June 1999 as Executive Vice-President, Finance & Administration of Suez (then known as Lyonnaise des Eaux). He is currently Senior Executive Vice-President and Chief Financial Officer of Suez Environnement, having held a number of directorships within the Suez Group since 1984. Prior to joining Suez in 1984, Alain worked for the French Treasury Department (Ministry of Economic Affairs). He became a non-executive director of the Company on 23 May 2003.

Jacques Pétry, Non-Executive Director, aged 48

Jacques Pétry was a non-executive director of NSL from 14 October 2002 to 23 May 2003. He is Chairman and Chief Executive of Suez Environnement and Executive Vice-President of Suez, in charge of water and waste operations. Jacques is also a non-executive director of NWL, a post taken up at the same time as his appointment to NSL. He has been a non-executive director of Lyonnaise Europe since 24 April 2002.

Company Secretary

Martin Parker, Company Secretary, aged 44

Martin graduated in law in 1980 and was admitted as a solicitor in 1983, when he joined Harbottle & Lewis. He moved in-house with Northern Engineering Industries plc in 1987 (now part of Rolls Royce plc) and joined Northumbrian Holdings Limited (at the time called Northumbrian Water Group plc) in 1990, concentrating on acquisitions, overseas projects and contracts with industrial customers. He was appointed Head of Group Legal Services in 1998, Company Secretary and Head of Legal Affairs for NWL in 2000 and Company Secretary of the Company on 23 May 2003.

9. Corporate Governance

The Combined Code provides that non-executive directors should comprise not less than one third of the board and that the majority of non-executive directors should be independent of management. The Revised Combined Code provides that at least half the board, excluding the chairman, should comprise non-executive directors determined by the board to be independent. Although the Revised Combined Code will only apply to the Company in respect of reporting years commencing on or after 1 November 2003, the Board is committed to achieving high standards of corporate governance and will accordingly, subject to the following, endeavour to comply with the principles and provisions of the Revised Combined Code from Admission.

The Board considers that Sir Patrick Brown and Martin Nègre are independent non-executive directors.

The Revised Combined Code sets out factors which may be relevant to a board's assessment of the independence of a non-executive director, including whether he has been an employee of the company or group in question at any time in the previous five years or has had a material business relationship with the company in the previous three years in his capacity as a director or senior employee of a body which has had a material business relationship with the company. Martin Nègre was until April 2001 the Chief Executive Officer of NSL (as an employee of Suez Lyonnaise, being a member of the Suez Group), and until May 2001 a director of Lyonnaise Europe. The Board has carefully considered the position of Martin Nègre and has determined that he is independent in character and judgement and that his past and existing relationships and circumstances are not likely to affect his judgement. The Board has also given consideration to the fact that the Company is no longer controlled by the Suez Group and Martin Nègre was not, during the relevant period for the test of independence set out in the Revised Combined Code, an employee of an existing member of the Group.

Further, the Board intends to appoint an additional two non-executive directors to the Board, who will be independent non-executive directors. The Board intends to identify candidates with suitable skills and experience to fill these roles in due course following Admission.

Accordingly, upon Admission, the Company will not be compliant with certain elements of the Combined Code or the Revised Combined Code in respect of the composition of the Board and the composition of the Remuneration Committee and will not be compliant with the Revised Combined Code in respect of the composition of the Audit Committee.

However, given the Board's determination of Martin Nègre's independence, following Admission and upon the appointment of the two additional independent non-executive directors, the Company will be able to comply with both the Combined Code and the Revised Combined Code in respect of the composition of the Board, the Remuneration Committee and the Audit Committee.

The Company will hold at least six board meetings each year. The Board is responsible for formulating, reviewing and approving the Group strategy, budgets, major items of capital expenditure and acquisitions. The Company has adopted the Model Code.

The various committees of the Board which have been established and a summary of their recently revised terms of reference are set out below.

Audit Committee

The Audit Committee meets at least three times a year and comprises at least three members, the majority of which shall be independent non-executive directors. This committee is responsible for the functions recommended by the Revised Combined Code including:

- reviewing the annual financial statements and interim reports prior to approval, focussing on changes in accounting policies and practices, major judgmental areas, significant audit adjustments, going concern and compliance with accounting standards, London Stock Exchange and legal requirements;
- considering the appointment of the auditors and their remuneration and the scope of any non-auditing services;
- meeting with the external auditors to discuss the scope of the audit, issues arising from their work and any matters the auditors wish to raise;
- reviewing the Group's corporate review procedures and any statements on internal control prior to endorsement by the Board; and
- approving and monitoring the internal audit programme.

Remuneration Committee

The Remuneration Committee comprises at least three members, the majority of which shall be independent non-executive directors and has the following key duties:

- reviewing and recommending the remuneration, pension entitlements and other benefits of the executive directors and, as appropriate, other senior executives of the Group; and
- reviewing the operation of share option schemes and the granting of such options.

Nomination Committee

The Nomination Committee comprises at least three members, the majority of which shall be independent non-executive directors, and is responsible for considering the Board structure and all potential appointments to the Board and for making suitable proposals to the Board in relation to potential appointments.

Standing Committee

The Standing Committee comprises all Directors, a quorum being one executive director and one non-executive director, and deals with the Company's business between Board meetings.

Ethics and Environment Committee

The Ethics and Environment Committee comprises at least two Directors and other members co-opted from the Group. It establishes best practice and compliance across the Group on ethical and environmental matters as well as preparing and implementing a programme of environmental audits in relation to the Group's activities.

Treasury Committee

The Treasury Committee comprises at least three members selected from all Directors and is responsible for reviewing and recommending treasury policies to the Board as well as monitoring the current economic enviroment and the likely future financing requirements of the Group.

10. Share Incentive Schemes

The Company stated, at the time of the AIM Admission, that a key element of the Company's reward strategy would be the establishment of share incentive schemes which would align the interests of participants in the schemes with Shareholders, as well as encourage employee share ownership and facilitate the retention of key staff.

The Directors have carried out a comprehensive review of the share incentive schemes available to the Company and have decided, subject to obtaining Shareholder approval, to establish two new schemes: the Northumbrian Water SIP – a share incentive plan under which all employees would be eligible to benefit, and the Northumbrian Water LTIP – a long term incentive plan under which it is intended that senior management only would benefit. In making their decision, the Directors have had regard to, amongst other things, the guidelines published by the Association of British Insurers. Shareholder approval for the establishment of the plans will be sought at an Extraordinary General Meeting of the Company which is expected to be held later in 2003.

11. Dividend Policy

The Directors intend to retain distributable profits only when they expect the Company to earn above average returns from the deployment of the funds retained.

It is the Directors' intention to pay an interim and a final dividend in each financial year.

12. Taxation

General information relating to UK taxation with regard to Admission is summarised in paragraph 15 of Part 7 of this document. A Shareholder who is in any doubt as to his tax position, or is subject to tax in a jurisdiction other than the UK, should consult his or her professional advisers.

13. Risk Factors

Certain risk factors in relation to the Business are brought to your attention in Part 3 of this document.

14. Further Information

Your attention is drawn to the additional information set out in Part 7 of this document.

PART 2

Regulation and Compliance

1. Regulatory Framework

The economic activities of Regulated Companies are regulated pursuant to the WIA, as amended, and the conditions of their instruments of appointment.

The DGWS is appointed under the WIA and is the economic regulator for the water and sewerage industry in England and Wales. In addition, water and sewerage companies are also subject to regulation by, *inter alia*, the Environment Agency and the Drinking Water Inspectorate.

The DGWS and Secretary of State have a primary duty to exercise and perform their powers and duties conferred or imposed under the WIA in a manner they consider best calculated to secure that:

- the functions of Regulated Companies are properly carried out throughout England and Wales; and
- Regulated Companies are able (in particular, by securing reasonable returns on their capital) to finance the proper carrying out of their functions.

Subject to this, they have further duties as regards customers, promoting efficiency, economy and competition. For example, the DGWS is responsible for, *inter alia*, setting limits on charges and monitoring and enforcing licence obligations.

NWL is the Regulated Company in the Group and is subject to a general duty to develop and maintain an efficient and economical system of water supply and to make arrangements in relation to the provision of water supplies in its licensed area. Also, it has specific supply duties, including duties to supply water for domestic purposes to premises within the areas set out in the Licence and which are connected to a water main and to connect new premises to a water main. With regard to NWL North, where it is licensed to conduct water and sewerage activities, it also has a general duty to provide, improve, extend and maintain a system of public sewers capable of draining its region effectively and to make provision for the emptying of sewers and for dealing effectively with their contents.

2. Price Control

One way in which Ofwat regulates sewerage and water charges is by capping the average increase in charges which a company can impose in any year. Ofwat carries out a Periodic Review and sets price caps every five years. In relation to pricing, on 25 November 1999 Ofwat published its final determination of price limits for the period 2000 to 2005. The allowable weighted average increase in charges is expressed by RPI+K, with RPI being the movement of the Retail Prices Index and K being a plus or minus factor for each individual water company. In NWL's case the K factor for the regulatory years 2003/04 and 2004/05 is zero per cent., although this could be increased for 2004/05 if NWL's recent application for an IDOK is accepted by Ofwat.

Ofwat has published the methodology it proposes to use for the Periodic Review in 2004 of prices for the period 2005 to 2010. In this report it concludes that it will continue to use the RPI+K approach for the Periodic Review in 2004 as modified to suit the characteristics of the water industry. In November 2004 Ofwat will publish its final determination of price limits for the period 2005 to 2010. Following the publication of the final price limits, water companies can accept that determination or ask Ofwat to refer their determination to the Competition Commission for the price determinations to be reviewed (for further details on price controls see paragraph 3.5 below).

3. Licence

The Licence was originally granted to NWL in August 1989. This was subsequently modified, in particular to include the area covered by North East Water plc in 1996 following the merger of North East Water plc with NWL, and the area covered by Essex and Suffolk Water plc in 2000 following the merger of Essex and Suffolk Water plc with NWL. It specifies the geographical areas served and imposes conditions on NWL which include limits on charges to customers and restrictions on the financial activities of NWL.

Under the WIA, the conditions of the Licence may be modified by the DGWS either: (i) with the consent of NWL, or (ii) without NWL's consent following a reference to the Competition Commission which concludes that there are effects adverse to the public interest which can be remedied or prevented by modifications. Licence modifications could also result, in certain circumstances, from a merger or market investigation reference to the Competition Commission. The Secretary of State has a power to veto certain proposed modifications agreed by the DGWS and NWL. Finally, legislation can create powers for the making of modifications without the consent of Regulated Companies. The Water Bill currently before Parliament provides the DGWS with powers to make unilateral modifications, following consultation with Regulated Companies, to give effect to the new competition arrangements and to provide for the payment of fees to cover the expenses of the new Consumer Council for Water (see also paragraph 5 of Part 2 of this document).

Any modification to the Licence could have a material impact on NWL.

A failure by NWL to comply with the Licence, as modified from time to time, or with certain statutory obligations may lead to the making of an Enforcement Order by the DGWS or the Secretary of State which could have an adverse impact on NWL. Failure by it to comply with any Enforcement Order (as well as certain other defaults) may lead to the making of a Special Administration Order (as set out below).

The area of appointment of NWL can also be varied to give effect to an inset appointment (as set out below).

3.1 Termination of the Licence

Under the WIA and the conditions of the Licence there are only certain circumstances in which NWL could cease to hold its Licence for all or part of its licensed area, and these are if:

- NWL consented to such a change; or
- the Secretary of State has given 25 years' notice to terminate; or
- NWL is in Special Administration, and the Special Administrator opts to transfer the business and licence to a successor; or
- an "inset" appointment is granted over part of NWL's area to another company (see below for further details).

The termination or transfer of the Licence could have a material adverse impact on NWL.

Where a Regulated Company breaches its licence the Secretary of State and DGWS have a duty to enforce the relevant condition by an Enforcement Order. Where a Regulated Company persistently seriously breaches its licence or when it is or is likely to be unable to pay its debts, for example, the Secretary of State or the DGWS (with the consent of the Secretary of State) can apply to a court to make a Special Administration Order appointing a Special Administrator to run the company until the property, rights, liabilities and licence of the existing company are transferred to a new company.

So far, no compulsory licence terminations or Special Administration Orders have been made in connection with any Appointed Activities of any Regulated Company in England and Wales. There is therefore no precedent to indicate how such processes would work in practice and the extent to which creditors' interests would be protected.

If the Secretary of State or the DGWS were to make an appointment or variation replacing NWL as the regulated water and sewerage undertaker for its currently appointed area, it would have a duty to ensure (so far as consistent with its other duties under the WIA) that the interests of NWL's creditors were not unfairly prejudiced by the terms on which the successor Regulated Company (or Companies) replacing NWL could accept transfers of property, rights and liabilities from NWL.

3.2 Enforcement Orders

Certain duties of Regulated Companies are enforceable by the Secretary of State or the DGWS or both. The conditions of each licence (and other duties) are enforceable by the DGWS alone whilst other duties, including those relating to water quality, are enforceable by the Secretary of State.

Where the Secretary of State or the DGWS is satisfied that a Regulated Company is contravening, or has contravened and is likely to do so again, its licence, or a relevant statutory or other requirement, either the Secretary of State or the DGWS must make a final enforcement order to secure compliance with that condition or requirement, save that, where it appears to the Secretary of State or the DGWS more appropriate to make a provisional enforcement order, he may do so. In determining whether a provisional enforcement order should be made, the Secretary of State or DGWS shall have regard to the extent to which any person is likely to sustain loss or damage as a consequence of such breach before a final enforcement order is made. The Secretary of State or the DGWS will confirm a provisional enforcement order if satisfied that the provision made by the order is needed to ensure compliance with the condition or requirement which is in breach.

There are exceptions to the Secretary of State's and the DGWS's duty to make an enforcement order or to confirm a provisional order:

- where the contraventions were, or the apprehended contraventions are, of a trivial nature;
- where the company has given, and is complying with, an undertaking to secure or facilitate compliance with the condition or requirement in question;
- where duties in the WIA preclude the making or confirmation of the order; or
- where the DGWS is satisfied that the most appropriate way of proceeding is under the Competition Act.

3.3 Special Administration Orders

The WIA contains provisions enabling the Secretary of State or the DGWS, with the consent of the Secretary of State, to secure the general continuity of water supply and sewerage services. In certain specified circumstances, the High Court may, on the application of the Secretary of State or, with his consent, the DGWS, make a Special Administration Order in relation to a Regulated Company and appoint a Special Administrator. These circumstances include:

- where there has been, or is likely to be, a breach by a Regulated Company of its principal duties to supply water or provide sewerage services or of a final or provisional enforcement order and, in either case, the breach is serious enough to make it inappropriate for the Regulated Company to continue to hold its licence;
- where the Regulated Company is, or is likely to be, unable to pay its debts;
- where, in a case in which the Secretary of State has certified that it would be appropriate, but for Section 25 of the WIA, for him to petition for the winding up of the Regulated Company under Section 440 of the Companies Act 1985, it would be just and equitable, as mentioned in that Section, for the Regulated Company to be wound up if it did not hold a licence; and
- where the Regulated Company is unable or unwilling adequately to participate in arrangements certified by the Secretary of State or the DGWS to be necessary by reason of, or in connection with, the appointment of a new Regulated Company upon termination of the existing Regulated Company's licence.

In addition, on an application being made to a Court, whether by the Regulated Company itself or by its directors, creditors or contributories, for the compulsory winding up of the Regulated Company, a Court would not be entitled to make a winding up order; however, if satisfied that it would be appropriate to make such an order if the company was not a Regulated Company, a Court shall instead make a Special Administration Order.

During the period beginning with the presentation of the petition for Special Administration and ending with the making of a Special Administration Order or the dismissal of the petition (the "Special Administration Petition Period"), the Regulated Company may not be wound up, no steps may be taken to enforce any security except with the leave of the Court, and subject to such terms as the Court may impose, no other proceedings or other legal process may be commenced or continued against the Regulated Company or its property except with the leave of the Court.

Once a Special Administration Order has been made, any petition presented for the winding up of the company will be dismissed and any receiver appointed, removed. Whilst a Special Administration Order is in force, those restrictions imposed during the Special Administration Petition Period continue with some modifications; an administrative receiver can no longer be appointed (with or without the leave of the Court) and, where any action does require the Court's leave, the consent of the Special Administrator is acceptable in its place.

3.4 *Ring Fencing*

Under the Licence NWL is under an obligation to ensure, so far as is reasonably practicable, that in the event of a Special Administration Order being made in respect of NWL, the Special Administrator would have available sufficient rights and assets to manage the affairs, business and property of NWL to achieve the purposes of such order. Any asset or right to which this duty applies may not, without the consent of the DGWS, be transferred by NWL to any associated company as consideration for services provided to NWL by that associated company.

NWL is under a duty to act at all times in the manner best calculated to ensure that it has adequate (i) financial resources and facilities, and (ii) management resources, to enable it to carry out its Appointed Activities. The Licence requires that NWL's directors, when submitting NWL's accounts to Ofwat, provide the DGWS with a certificate stating that, in their opinion, NWL has available sufficient financial and management resources and facilities to enable it to carry out its Appointed Activities for at least the next 12 months. The directors are also required to inform the DGWS in writing of any reason why the most recent certificate provided by them could not be repeated.

NWL is under a duty at all times to conduct its Appointed Activities as if it were substantially its sole business. In particular, NWL should have regard that the composition of its board is such that its directors act independently of the parent company or controlling shareholder.

Under the Licence NWL is required to obtain legally enforceable undertakings in its favour from NWG as its ultimate parent company. These undertakings should provide, *inter alia,* that NWG will ensure that the board of NWL contains not less than three independent non-executive directors.

3.5. *Price Controls*

The Licence provides for the DGWS to determine in certain circumstances whether, and if so how, K should be changed between Periodic Reviews. An application for an IDOK may be made in respect of a Notified Item, a Relevant Change of Circumstance or a substantial adverse or favourable effect on NWL's business.

A "Notified Item" is any item notified by the DGWS to NWL as not having been allowed for in full or in part in K at the last Periodic Review. Notified Items put forward by the DGWS in the determination of price limits for the period 2000 to 2005 were: (i) the costs and revenues associated with any difference in the number of customers opting for metered supply from that assumed in the Periodic Review in 1999; (ii) any net increase in bad debt and debt collection costs arising from the loss of the power to disconnect residential customers for non-payment; and (iii) any additional administrative costs arising out of statutory obligations to offer protection from high metered bills to vulnerable groups of customers.

A "Relevant Change of Circumstance" is defined in NWL's Licence and includes (i) the application to NWL's business of a new or changed legal requirement, and (ii) any difference between the actual value received from disposals of land in a given year and the value allowed for in relation to such disposals by the DGWS in the previous Periodic Review.

A substantial adverse effect on NWL's assets, liabilities, financial position, profits or losses can form grounds for an IDOK where such effect would not have been avoided by prudent management action. A substantial favourable effect on NWL's business can form the basis of an IDOK where such effect is (i) fortuitous, and (ii) not attributable to prudent management action.

An IDOK can only be made where the materiality threshold specified in the Licence is reached. For a Notified Item or Relevant Change of Circumstance the materiality threshold is ten per cent. of NWL's annual turnover. For substantial adverse or favourable effects to qualify as material they must equal or exceed 20 per cent. of NWL's annual turnover.

3.6 *Restrictions on disposals of land*

Under the WIA, there is a prohibition on NWL disposing of its Protected Land except with the specific consent of, or in accordance with a general authorisation given by, the Secretary of State. A consent or authorisation may be given on such terms as the Secretary of State considers appropriate. A disposal includes the creation of any interest (including leases, licences, mortgages, easements and wayleaves) in or any right over land, and includes the creation of a charge. The Licence prescribes the information which must be provided to the DGWS prior to NWL entering into any obligation (whether conditional or unconditional) which requires or might require it to make a disposal of Protected Land.

"Protected Land" is defined in the WIA, and comprises any land, or any interest or right in or over land, which:

(A) was transferred to NWL under the Water Act 1989, or was held by NWL at any time during the financial year ending 31 March 1990;

(B) is or has at any time on or after 1 September 1989 been held by NWL for purposes connected with the carrying out of its functions as a water undertaker or sewerage undertaker; or

(C) has been transferred to NWL in accordance with the WIA from another company in relation to which that land was Protected Land.

3.7 *Billing*

NWL is under a duty to ensure that at all times there is in effect a charges scheme in accordance with Section 143 WIA, by which (i) it fixes the charges to be paid for supplies of water for domestic purposes, and (ii) it fixes the charges to be paid for connections.

NWL is entitled to have in effect two charging schemes, one in relation to NWL North and a second in relation to NWL South, and those schemes may be in different terms. Each scheme is reviewed annually.

4. Ofwat Consultation Paper

Ofwat issued a consultation paper in June 2003 in which it invited views on any issues resulting from the Atlantic Acquisition and specifically invited views on:

- the financing of NWL;
- the current arrangements for ring fencing of the regulated business;
- the new owner's capacity to control a regulated water business; and
- whether incentives for efficiency have changed.

On 19 August 2003, the Ofwat Position Paper was published in relation to the Atlantic Acquisition as it affected NWL. In the Ofwat Position Paper, Ofwat announced its intention to modify the Licence in order to bring the regulatory ring-fence in the Licence up to current standards. New conditions will be introduced to the Licence to require NWL to:

- use all reasonable endeavours to ensure that it, or any subsidiary as issuer of corporate debt on its behalf, maintains at all times an investment grade corporate credit rating; and
- maintain the listing of a financial instrument and use all reasonable endeavours to retain the listing of that financial instrument, the market price of which should react to the financial position of NWL's Appointed Activities, on the London Stock Exchange or another exchange of similar standing.

These conditions are substantially the same as those in the instruments of appointment of other Regulated Companies and NWL is currently in compliance with both these conditions.

Ofwat noted in the Ofwat Position Paper that a credit rating of BBB (as recently assigned to NWL by S&P) is not consistent with its view on the credit quality of water companies, which in its view must have ready access to capital markets. It considered that a credit rating of BBB for the industry as a whole is unlikely to be sustainable in the long term due to companies' continuing capital requirements. See paragraph 5 of Part 1 of this document for further details on NWL's credit rating.

Ofwat considered carefully whether any immediate regulatory action might have a positive impact on NWL's credit quality and financial position. In addition, it considered whether any immediate action is required to protect NWL's customers from any potential future deterioration in NWL's credit quality and financial position.

Ofwat concluded that NWL appears to have sufficient cash flows to support its debt. Ofwat noted that NWL had informed it that it has no need to raise money via the debt market until after the current Periodic Review. Price limits are expected to be determined in November 2004 for the period 2005-10.

Ofwat also noted that NWL had informed it that it is currently reviewing a number of options that might improve its credit quality and financial position. These options include:

- raising debt against the revenues generated by the Kielder reservoir (a non-regulated asset) and using the proceeds to repay existing debt (being debt under the Amended and Restated Facilities Agreement – for further details please see paragraph 11.1(E) of Part 7 of this document) guaranteed against the shares of NWL; and
- obtaining from the EIB an extension of its waiver of its right to redeem its current loans (amounting to £376 million) on any change of ownership of NWL. The EIB has agreed to this until April 2004 when it will review its position.

Ofwat further concluded that it seems unlikely that any immediate regulatory action, at least on its own, would benefit customers materially or achieve an early improvement in the credit rating of NWL. Ofwat took account here of the views taken by the credit rating agencies including the "stable outlook" assessment that S&P attached to its current confirmed credit rating.

The credit ratings of NWL reflect the cash flows required to service all of the Group debt, i.e. they take account of the debt held outside the regulatory ring-fence. This includes two parent company bond programmes, a £200 million NSL 2006 Bonds programme and a £350 million bond programme repayable in 2023.

The latter is guaranteed by NWL as the proceeds were used for its Appointed Activities. The proceeds from the former bond were not used in that way, but its holders are many of the same institutions. Furthermore, in the event of default on the NSL 2006 Bonds programme, the 2023 bond programme may as a result of a cross default provision, become repayable and hence the two are linked. This weakens the ring fence and Ofwat has stated in the Ofwat Position Paper that NWL must take all reasonable steps to break the links between the debt guaranteed by the Regulated Company and the non-guaranteed debt raised by its parent company. The Group is exploring ways in which this can be achieved.

Ofwat stated in the Ofwat Position Paper that the onus is now on NWL to take all reasonable steps that might be necessary to enable it to demonstrate to the market and to Ofwat that it has the ability to continue to finance itself into the future.

Ofwat has indicated in the Ofwat Position Paper that, should NWL not be able to demonstrate that all reasonable steps have been taken by June 2004, then it will consider whether further licence modifications might be appropriate. These may include a "cash lock-up" licence modification that would restrict the ability of NWL to make cash flows available to the wider group in the event of a deterioration in the company's financial position thus potentially affecting dividend growth within the Group.

5. Competition

5.1 *Competition Act*

The Competition Act contains prohibitions relating to anti-competitive agreements and conduct as well as powers of investigation and enforcement. These powers include powers for the DGWS to enforce directions in order to bring an infringement to an end and to impose fines of up to ten per cent. of UK group-wide turnover for each year of infringement up to a maximum of three years. Also, any agreement which infringes the Competition Act may be void and unenforceable and may give rise to claims for damages from third parties.

5.2 *The Water Bill*

The Water Bill will, if passed, *inter alia*, amend the WIA and contains proposals for a number of provisions which may affect the finances of Regulated Companies, including NWL.

It contains provisions which would create a new framework for competition in water supply, under which new types of "water supply licence" will be available to entrants wishing to use Regulated Companies' networks to transport water to customers (common carriage) or wishing to purchase wholesale water from undertakers for "retail" to customers.

However, the new market is to be limited to customers using in excess of 50 megalitres of water per annum. NWL believes that the passing of the Water Bill (as currently drafted) does not present a significant risk to its business in terms of potential lost revenue.

The Water Bill also proposes a new power for the DGWS and the Secretary of State to impose financial penalties on a Regulated Company for contraventions of its licence, statutory or other requirements including performance standards. Penalties may be up to ten per cent. of a Regulated Company's turnover, but they must be reasonable in the circumstances of the case. Each of the above enforcement authorities would be required to publish a statement of policy on the imposition of penalties, and to have regard to that statement when implementing the new provisions.

5.3 *Inset Appointments*

An inset appointment can be granted to a company seeking to provide water and/or sewerage services on a site which has yet to be developed, or to a large user of water and/or sewerage services within an existing Regulated Company's area, or where the incumbent Regulated Company consents to the variation. The threshold for large user insets in England is 100 megalitres of water per annum.

There are three existing inset appointments in the areas in which NWL is the incumbent Regulated Company. Only one of these relates to supplies to a customer which was an active customer of NWL prior to the inset appointment. The other two represent appointments to sites which have yet to be developed and therefore do not represent any lost revenue.

NWL is the appointee of one inset appointment in an area where it is not the incumbent Regulated Company where the appointment also relates to a site which has not yet been developed.

There are currently nine inset appointments in the UK and NWL is not aware of any further applications for inset appointments within the areas in which it is the incumbent Regulated Company.

PART 3

Risk Factors

This Part describes the risks that could materially affect the Business. The factors below should be considered in connection with any financial and forward-looking information in this document and the cautionary statements contained in paragraph 18.9 of Part 7 of this document.

The risks below are not the only ones that the Group faces, some risks are not yet known to the Group and some that the Group does not currently believe to be material could later turn out to be material. All of these risks could materially affect the Business, its turnover, operating profit, earnings, net assets and liquidity and capital resources.

1. Requirement for further funds

It should be noted that the Appointed Activities of NWL are likely to require further funding in the future to enable NWL to meet its ongoing capital expenditure programme. NWL will typically seek to raise such funds in the corporate debt market (see paragraph 4 of Part 2 of this document for further details). However, it is possible that such a funding requirement may be by way of the issue of further Ordinary Shares including an issue on a non pre-emptive basis. There is no commitment in place guaranteeing that any funds required in the future will be available and, if further equity finance is raised, existing shareholdings may be diluted. In addition, NWL's profitability may suffer should it not secure the expected capital efficiencies associated with its capital expenditure programme, or the programme falls behind schedule for other reasons. A failure of this nature may be factored into future Periodic Reviews by Ofwat and may also adversely affect NWL's ability to meet regulatory and environmental performance standards (which may result in sanctions by Ofwat).

In addition, following publication of the Ofwat Position Paper, NWL is obliged to take all reasonable steps that might be necessary to enable it to demonstrate to the market and to Ofwat that it has the ability to continue to finance itself in the future.

Ofwat has stated in the Ofwat Position Paper that, should NWL not be able to demonstrate that all reasonable steps have been taken by June 2004, it will consider whether further licence modifications might be appropriate such as a cash lock-up (for further details see paragraph 4 of Part 2 of this document).

The results of the Periodic Review for the period 2005 to 2010 will not be known until November 2004 and may impact on the Company's requirement for further funding (for further details see paragraph 3 of Part 3 of this document).

2. Requirement for operating cost savings

Implicit in the Periodic Reviews carried out by Ofwat is the need to make operating cost savings during the current five year regulatory period. NWL believes that it will deliver sufficient operating cost savings. However, should operational performance deteriorate, NWL's profitability would suffer and Ofwat may factor this performance into future Periodic Reviews.

3. The 2004 Periodic Review

Although Ofwat has announced it will retain the RPI+K approach to setting prices in the Periodic Review in 2004 for the period 2005 to 2010, the final outcome of this review will not be known until November 2004 and, in any event, is not within the control of the Company or NWL.

An adverse price determination may occur as a result of a number of factors including an inadequate allowed cost of capital or should regulatory assumptions concerning operating expenses, required capital expenditure or revenue forecasts, including assumed operating and capital expenditure efficiencies, prove to be incorrect.

A substantial portion of revenues of NWL is derived from industrial customers which are susceptible to global, national and regional changes in the economy.

Furthermore, a reduction in revenues deriving from industrial customers, to the extent not anticipated in the price setting process, is likely to have an adverse effect on the profits of the Business.

Should new financial obligations arise which have not been taken into account in the Periodic Review lead to an increase in the cost base of NWL it may not be possible to reflect such increases in prices charged to customers until the next Periodic Review.

Draft Business Plan

As part of the Periodic Review in 2004, NWL submitted the Draft Business Plan to the DGWS on 15 August 2003 for the period 2005 to 2010. The Final Business Plan is due to be submitted in April 2004. The Draft Business Plan has been prepared by NWL solely for the purposes of the Periodic Review and accordingly may be subject to substantial amendment in the future. The Draft Business Plan should not be relied upon by investors when seeking to make any decisions regarding any investment in the Company.

IDOK

Under the conditions of the Licence, an IDOK may be made between Periodic Reviews in specified circumstances, including when a change of circumstance has occurred which has or will have a substantial adverse effect or a substantial favourable effect on the business of that Regulated Company (a "Substantial Effect Clause").

On 11 September 2003 NWL applied to Ofwat for an IDOK. If successful, this will allow NWL to increase prices to its customers in real terms in the 2004/05 financial year. However, the Company cannot, as at the date of this document, predict by how much prices will increase if the IDOK application is successful. Ofwat will issue a draft decision for consultation in November and a final decision on possible price increases in December this year.

The main reasons behind the application were to reflect increased costs or reduced revenue on the part of NWL in connection with increased customer bad debt, additional costs arising from new obligations (e.g. providing treatment solutions in relation to increasing levels of pesticides found in the raw water in certain operating areas of the Regulated Business), and lower than forecast demand for water by large scale users.

In the Draft Business Plan, NWL assumed that no real price increase would apply in the 2004/05 financial year. This is in line with the existing price limit for that year (K of zero). The Final Business Plan will take into account the outcome of the IDOK.

There is however no assurance that any adjustment will be made pursuant to the IDOK sought by NWL, or that any adjustment made pursuant to the IDOK will provide adequate revenue compensation to NWL.

If the DGWS does not make an IDOK within three months of NWL's application for an IDOK or if NWL wishes to dispute an IDOK made in relation to it by the DGWS, NWL has the right to require the DGWS to refer the matter to the Competition Commission for determination. There is no assurance however that the Competition Commission's determination of the relevant adjustment(s) will provide adequate revenue compensation to NWL.

Deviations from DGWS's Projections

Subject to the provisions covering IDOK applications under condition B of the Licence, the RPI+K price cap limits the annual "weighted average increase" in the standard charges of NWL. This, in turn, is calculated by reference to the "tariff basket formula", which is constructed so as to provide some compensation in respect of certain risks (for example, high rateable value customers opting for a meter). However, generally NWL is not protected, in respect of each Periodic Review Period, against revenue loss arising from any deviations during that Periodic Review Period from projections, including demographic changes affecting NWL's customer base, the loss of a major customer, unexpected movements in volumes consumed/discharged by customers, and loss through inset appointments.

Accordingly, at Periodic Reviews, the DGWS factors into his projections assumptions relating to numbers of customers and volumes consumed/discharged. Until the following Periodic Review, NWL bears the risk that actual numbers of customers and volumes consumed/discharged will fall short of the assumptions reflected in the RPI+K price cap. Since actual out-turn revenues are used as the basis for the setting of price limits in the subsequent five year period, any deviation from revenue projections in the previous five year period may be reflected in such price limits.

In addition, it is important for the Company to ensure that the DGWS is given sufficient information at the time of such Periodic Review to ensure that capital expenditure projections are accurate and that NWL then implements such capital expenditure programme in an efficient manner and in accordance with assumptions made regarding performance so as to remain within the parameters of the Periodic Review determination.

4. Economic and Market Fundamentals

A substantial deficit exists in the overall position of the Final Salary Scheme. This may require an increase in future contributions by the Company that may not be recognised by Ofwat in future Periodic Reviews. In addition, the size of any funding deficit is exposed to movements in the debt and equity markets and long term investment returns may remain lower than the rate assumed by the actuaries in their pension scheme valuations. Therefore, there can be no future guarantees this deficit will reduce over time.

Further, any reduction in interest rates may adversely affect the financial impact of any deferred tax charge until the time that the generally anticipated International Accounting Standards review is concluded.

NWL's revenue is linked to the underlying RPI and as such is subject to fluctuations in line with general economic trends.

NWL's revenue is also dependent to a significant extent on the continuance of the presence of the manufacturing and petrochemical industries in its customer base and any decline in such industries will have a corresponding effect on this revenue.

5. Dividends

Dividend growth in the Ordinary Shares will rely on underlying growth in the Business and, in particular, the dividend policy mentioned in paragraph 11 of Part 1 of this document should not be construed as a dividend forecast. Any change in the tax treatment of dividends or interest received by the Company may reduce the level of yield received by Shareholders. The market value of the Ordinary Shares can fluctuate and may not always reflect their underlying asset value. There can be no guarantee that the Company's objectives will be achieved. Dividend growth may be affected by modifications to the Licence (see paragraphs 3 and 4 of Part 2 of this document for more details).

6. Taxation

Any change in the Group's tax status or in taxation legislation could affect the Company's ability to provide returns to Shareholders or alter post tax returns to Shareholders. Statements in this document concerning the taxation of investors in shares are based on current tax law and practice which is subject to change. The taxation of an investment in the Company depends on the individual circumstances of Shareholders (see paragraph 15 of Part 7 of this document for more details).

7. Environmental

The Group is exposed to environmental risks given the nature of its operations and an environmental situation could arise in the future which could affect the Company's profits and its ability to pay dividends. As mentioned below, water supplies may be exposed to pollution, including pollution from the development of naturally occurring compounds and contamination resulting from man-made sources. Should any such pollution or contamination occur in respect of NWL's water supply, and it is unable to substitute a water supply from an uncontaminated water source, or to adequately and cost-effectively treat the contaminated water source, there may be an adverse effect on its operating results or financial position. Some of these costs may potentially be partly recoverable through future Periodic Reviews. In addition, NWL could be held liable for human exposure to dangerous substances in its water supplies or other environmental damage. While the Group maintains insurance policies in relation to liabilities likely to be associated with these risks, there can be no guarantee that all costs of any such claims would be covered or that coverage will continue to be available in the future. Moreover insurance cover is not available at a commercially acceptable premium in respect of gradual contamination.

NWL is at risk both from the effects of water shortages, caused by prolonged periods of drought, and from the effects of flooding.

If there are supply shortfalls caused by prolonged periods of drought, additional costs may be incurred by NWL in order to provide emergency reinforcement to supplies in areas of shortage. Restrictions on water use may adversely affect revenues from metered customers and may, in very extreme circumstances (which have never been experienced by NWL), lead to significant compensation having to be paid to customers who suffer interruptions in supply.

The financial costs of measures taken to deal with flooding could also be significant and may adversely impact on NWL's operations and financial condition. The fact that it is not always possible to forecast the occurrence of flooding sufficiently far in advance makes forward planning and the making of provision for the effects of flooding difficult. However, the Draft Business Plan includes a proposal for the introduction of a programme of flood prevention measures at various sites to mitigate the risk of flooding.

Pursuant to the decision of the Court of Appeal in February 2002 in the case of Peter Marcic v Thames Water Utilities Ltd, a water and sewerage undertaker may be liable in nuisance to home owners who have been the subject of repeated flooding where the company has failed to take reasonable steps to abate the nuisance. The court found that this duty is applicable even when the undertaker did not cause the nuisance or could not abate the nuisance without disproportionate expenditure. The Regulated Companies therefore potentially face an increased risk of claims for compensation for damage caused by flooding. The financial impact of compensation awards made pursuant to such claims could be significant, as could the costs of measures taken, where appropriate, to mitigate the risk of flooding. NWL has currently made no provisions for any claims based on the Marcic case and if compensation awards are not recoverable through adjustments to the price cap formula, insurance or otherwise, this could have a material adverse effect on the financial condition of NWL and the Group.

Further, under the Marcic case, a failure or omission by a statutory sewerage undertaker to conduct works to fulfil its statutory duty of drainage in a particular area may constitute a breach of certain rights arising under the Human Rights Act 1998 (the "HRA"), which came into effect on 2 October 2000, and could entitle a claimant to compensation for damage suffered subsequent to the date on which the HRA came into effect. The House of Lords is due to hear this case on appeal in October 2003.

Depending on developments in case law, sewerage undertakers may in future have to negotiate contracts with the owners of watercourses in order to be able to discharge into them. The additional costs involved are expected to be significant.

There can be no assurance as to whether or not existing weather patterns will have an adverse effect on the operations or financial condition of NWL, or that existing weather patterns will continue in the future. It is not possible to accurately assess the impact that any climate change may have on the operations or financial condition of NWL and the Group.

8. Borrowings

Shareholders should be aware that, whilst the use of borrowings enhances capital growth in the Ordinary Shares when the return on the underlying assets is rising, it will have the opposite effect where the underlying return is falling, further reducing the return on the Ordinary Shares. In addition, should the fall in underlying asset value or headline financial numbers breach any of the terms of its financial agreements, the Group may be required to repay such borrowings in whole or in part together with any attendant cost. Borrowing costs may increase as a result of adverse changes in interest rates and the corporate credit ratings of NWL and/or the Company (for further details of NWL's credit rating, see paragraph 5 of Part 1 and paragraph 4 of Part 2 of this document).

9. Key Personnel

In order to develop, support and maintain the Business, the Group must recruit and retain highly skilled employees with particular expertise. The implementation of the Group's strategic business plans could be undermined by a failure to recruit or retain key personnel, the unexpected loss of key senior employees, failures in the Group's succession planning, or a failure to invest in the development of key skills. Additionally, unless skills are supported by a sufficient infrastructure to enable knowledge and skills to be passed on, the Group risks losing accumulated knowledge if key employees leave the Group.

10. Regulatory compliance

As mentioned previously, the Business is subject to regulation in the UK by, *inter alia*, the DGWS. In addition, the various environmental protection and health and safety laws and regulations which govern the Business establish, amongst other things, standards for drinking water and discharges into the environment which affect the Group's operations. The Group's operations also require various environmental permissions from regulatory authorities. Regulatory authorities may from time to time make enquiries of companies within their jurisdiction regarding compliance with regulations governing the operation of water companies. Whilst the Group believes it dedicates sufficient resources to its compliance programme, and endeavours to respond to such enquiries in an appropriate way and takes corrective action when warranted, the Group does face the risk that Ofwat or another governmental or regulatory body could find that it has failed to comply with applicable regulations or has not successfully undertaken corrective action. In this case, regulatory proceedings could be taken. Regulatory proceedings could also result in adverse publicity to, or negative perceptions regarding, the Group as well as diverting management's attention from the day to day management of the Business. A significant regulatory action against any member of the Group could have a material adverse effect on its Business, results or operations and/or financial condition (see paragraph 3 of Part 2 of this document for further details).

11. New legislation

English law governs matters with respect to such things as authorising companies to conduct business, restricting certain transactions between affiliates and generally regulating the operation of the Business (see paragraph 5 of Part 2 of this document). The Group cannot accurately predict the impact of such changes in the future on the Business. Many laws and regulations are complex and change regularly an example of which are the proposed changes to the WIA contained in the Water Bill (for further details see paragraph 5 of Part 2 of this document). These laws, and the enforcement of them, have tended to become more stringent in recent years. Additionally, from time to time, interpretation of existing laws may change and the introduction of new legislation may adversely affect the Group. The Group cannot accurately predict the impact of new judicial or regulatory interpretation of existing laws or future laws on its Business, results of operations and financial condition. New judicial or regulatory interpretation of existing laws or future laws could have a material adverse effect on the Group's reputation and/or its Business, results of operations and/or financial condition.

12. Litigation

The Group faces the risk of litigation in connection with the Business. In general, liability for litigation is difficult to assess or quantify; recovery may be sought for very large and/or indeterminate amounts and the existence and magnitude of liability may remain unknown for substantial periods of time. Although the Group is not party to any material litigation at present, substantial legal liability in the future could have a material adverse effect on its Business, results of operations and/or financial condition.

13. Failure of information systems

The Group's ability to maintain financial controls and provide high-quality customer service to customers depends, in part, on the efficient and uninterrupted operation of its management information systems, including its computer systems. The Group's computer systems are vunerable to damage or interruption from floods, fires, power loss, telecommunication failures and similar events. These systems may also be subject to sabotage, vandalism and similar misconduct. The same is true of third-party service and software providers on which the Group depends. Further, there is no assurance that systems will function as designed. Any damage to or failure of the systems could result in interruptions to the Group's financial controls and customer service. Such interruption could have a material adverse effect on the Group's Business, results of operations and/or financial condition.

14. Customer debt

NWL is responsible for the billing, cash collection and debt management activities for its sewerage and water customers. Under the WIA, both the disconnection of a water supply for non-payment and the limiting of a water supply with the intention of seeking to enforce payment are prohibited for certain premises (including private dwellings). NWL is therefore exposed to certain risks in respect of non-recovery of debt, which risks may cause the Group's profitability to suffer (although Ofwat does make allowance in the price limits for a proportion of debt deemed to be irrecoverable). There can be no assurance that the Company will not suffer losses from NWL's inability to fully recover its debts.

15. Trading in foreign countries

The Group's operations are concentrated in the United Kingdom. However, the Business also operates in other markets (for example Gibraltar). Overseas operations are subject to many uncertainties, stemming from political, economic and other issues, including:

- currency exchange risk and exchange controls;
- taxation policies, including increases in taxes and royalties, retrospective tax claims and currency repatriation restrictions and nationalisation, re-negotiations or modification of existing agreements;
- potential political interference in rapidly developing regulatory frameworks;
- the risk of civil unrest, acts of terrorism, border disputes or war;
- UK laws and policies affecting foreign trade, taxation and investment; and
- the possibility of legal disputes being made subject to the jurisdiction of foreign courts and the potential inability to subject foreign nationals to the jurisdiction of the United Kingdom courts.

The Group cannot give assurances that the current situation will not change in ways which would adversely affect the Business.

PART 4

Accountants' Report on NSL

The accountants' report in Part 4 of this document has been prepared for NSL, which was acquired by the Company, through the acquisition of NSL's immediate parent company Atlantic on 23 May 2003. Atlantic was incorporated (on 18 February 2003) solely for the purpose of acquiring the shares of NSL and had not traded, or entered into any transactions other than the issue of shares, prior to the acquisition of NSL. The trade and assets acquired through the acquisition of Atlantic reside within NSL and its subsidiaries (and had done so throughout the three years ended 31 December 2002 and three months ended 31 March 2003).

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18 September 2003

Dear Sirs

1. Introduction

We report on the financial information set out below. This financial information has been prepared for inclusion in the listing particulars dated 18 September 2003 of Northumbrian Water Group plc.

Basis of preparation

The financial information set out on pages 33 to 70 is based on the audited consolidated financial statements of Northumbrian Services Limited ("NSL") for each of the three years ended 31 December 2000, 2001 and 2002 and the audited non statutory financial statements for the 13 weeks ended 31 March 2003, and has been prepared on the basis set out on page 40 after making such adjustments as we considered necessary. Throughout the period 1 January 2000 to 31 July 2001, NSL was named Northumbrian Water Group plc, and then throughout the period 1 August 2001 to 31 March 2003, NSL was named Ondeo Services UK plc. It adopted its present name on 19 June 2003.

Responsibility

The audited financial statements used to derive the financial information set out below are the responsibility of the directors of NSL who approved their issue.

The directors of Northumbrian Water Group plc are responsible for the contents of the listing particulars dated 18 September 2003, in which this report is included.

It is our responsibility to compile the financial information set out in our report from the financial statements referred to above, to form an opinion on the financial information and to report our opinion to you.

Basis of opinion

We conducted our work in accordance with the Statements of Investment Circular Reporting Standards issued by the Auditing Practices Board. Our work included an assessment of evidence relevant to the amounts and disclosures in the financial information. The evidence included that previously obtained by us relating to the audit of the financial statements for the periods ended 31 December 2002 and 31 March 2003 underlying the financial information for those periods. It also included an assessment of significant estimates and judgements made by those responsible for the preparation of the financial statements underlying the financial information and whether the accounting policies are appropriate to the entity's circumstances, consistently applied and adequately disclosed.

We planned and performed our work so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial information on pages 33 to 70 is free from material misstatement whether caused by fraud or other irregularity or error.

Opinion

In our opinion, the financial information gives, for the purposes of the listing particulars dated 18 September 2003, a true and fair view of the state of affairs of NSL as at the dates stated and of its profits, cash flows and recognised gains and losses for the periods then ended.

2. Profit and Loss Accounts

	Notes	Year ended 31 December 2000 £m	2001 £m	2002 £m	Three months ended 31 March 2003 £m
Turnover: Group and share of joint ventures		501.9	494.1	511.0	129.6
Less share of joint ventures' turnover		(4.4)	(4.7)	(7.0)	(1.5)
Group turnover	2	497.5	489.4	504.0	128.1
Operating costs	3(a)	(313.9)	(333.5)	(338.7)	(88.4)
Operating profit	2	183.6	155.9	165.3	39.7
Share of associated undertakings' operating profit		2.8	3.3	0.6	1.0
Share of joint ventures' operating profit		1.0	1.0	1.3	0.3
		3.8	4.3	1.9	1.3
Total operating profit: Group and share of joint venture and associates		187.4	160.2	167.2	41.0
Exceptional profit on disposal of associate	5	—	29.4	—	—
Profit on ordinary activities before investment income, interest and taxation		187.4	189.6	167.2	41.0
Investment income		0.3	—	0.2	—
Net interest payable	4	(81.8)	(79.7)	(75.2)	(21.4)
Profit on ordinary activities before taxation	2	105.9	109.9	92.2	19.6
Tax on profit on ordinary activities	8	(19.5)	(11.2)	(0.5)	(3.4)
Profit on ordinary activities after taxation		86.4	98.7	91.7	16.2
Minority interest		(0.1)	(0.6)	0.1	(0.3)
Profit for the financial period		86.3	98.1	91.8	15.9
Dividends paid and proposed	9	(57.0)	(59.6)	(62.3)	—
Retained profit for the financial period	24	29.3	38.5	29.5	15.9
Earnings per share		18.5p	21.0p	19.7p	3.4p

There is no difference between the results as stated above and their historical cost equivalents.

All results relate to continuing activities.

The earnings per share figures above have been calculated on the number of shares of NSL in issue throughout the period as set out in Note 23. The NWG Group, of which NSL Group represents a significant part, was formed on 23 May 2003 and has a significantly different capital and funding structure from the NSL Group. Accordingly, the earnings per share figures above will not be comparable to those of the NWG Group.

3. Statements of total recognised gains and losses

	Notes	Year ended 31 December 2000 £m	2001 £m	2002 £m	Three months ended 31 March 2003 £m
Profit for the financial period					
Group		87.5	96.6	89.5	16.0
Associates		(1.7)	1.0	1.6	(0.2)
Joint ventures		0.5	0.5	0.7	0.1
Profit for the financial period attributable to the members of the parent company		86.3	98.1	91.8	15.9
Exchange differences		—	—	0.2	—
Total recognised gains in the financial period		86.3	98.1	92.0	15.9

4. Balance Sheets

	Notes	As at 31 December 2000 £m	As at 31 December 2001 £m	As at 31 December 2002 £m	As at 31 March 2003 £m
Fixed assets					
Tangible assets	10	2,315.2	2,435.9	2,559.4	2,590.7
Investments					
Investments in joint ventures:					
– share of gross assets	11	9.0	11.2	11.0	12.7
– share of gross liabilities		(7.3)	(9.2)	(8.0)	(9.6)
		1.7	2.0	3.0	3.1
Investment in associate	11	2.0	2.0	3.1	2.9
Other investments	11	0.6	0.6	1.0	0.4
		2,319.5	2,440.5	2,566.5	2,597.1
Current assets					
Stocks	13	6.7	6.4	7.5	5.6
Debtors: receivable within one year	14	122.4	127.1	546.0	528.1
Debtors: receivable after more than one year	14	21.5	19.8	18.1	17.7
Investments		0.2	0.2	0.1	0.1
Cash at bank and short term deposits	15	84.2	399.5	84.0	53.6
		235.0	553.0	655.7	605.1
Creditors: amounts falling due within one year	16	(423.2)	(382.5)	(259.7)	(227.5)
Net current (liabilities)/assets		(188.2)	170.5	396.0	377.6
Total assets less current liabilities		2,131.3	2,611.0	2,962.5	2,974.7
Creditors: amounts falling due after more than one year	17	(967.7)	(1,292.8)	(1,602.6)	(1,603.8)
Provisions for liabilities and charges	21	(178.2)	(173.9)	(177.9)	(170.6)
Accruals and deferred income	22	(115.9)	(119.6)	(128.2)	(130.3)
		(1,261.8)	(1,586.3)	(1,908.7)	(1,904.7)
Net assets		869.5	1,024.7	1,053.8	1,070.0
Capital and reserves					
Called up share capital	23	466.2	466.2	466.2	466.2
Share premium account	24	217.9	217.9	217.9	217.9
Group reconstruction relief reserve	24	—	107.6	107.6	107.6
Profit and loss account	24	182.4	229.7	259.4	275.3
Equity shareholders' funds	25	866.5	1,021.4	1,051.1	1,067.0
Minority equity interest		3.0	3.3	2.7	3.0
Total capital and reserves		869.5	1,024.7	1,053.8	1,070.0

5. Cash Flow Statements

	Notes	Year ended 31 December 2000 £m	2001 £m	2002 £m	Three months ended 31 March 2003 £m
Net cash inflow from operating activities	(a)	244.9	243.6	235.8	20.9
Dividends from joint ventures and associates					
Dividends from joint ventures		0.2	0.2	0.2	—
Dividends from associates		0.1	0.1	0.2	—
Net cash inflow from dividends from joint ventures and associates		0.3	0.3	0.4	—
Returns on investments and servicing of finance					
Interest received		3.9	4.8	13.7	1.3
Interest paid		(73.6)	(69.8)	(91.7)	(27.6)
Interest paid on hire purchase contracts and finance leases		(3.6)	(2.8)	(1.6)	(0.5)
Dividends paid to minority interests		(0.3)	—	—	(0.5)
Net cash outflow from returns on investments and servicing of finance		(73.6)	(67.8)	(79.6)	(27.3)
Taxation					
Taxation paid on ordinary activities		(20.2)	(3.1)	(4.4)	(1.0)
Net cash outflow from taxation		(20.2)	(3.1)	(4.4)	(1.0)
Capital expenditure and financial investments					
Purchase of tangible fixed assets		(300.4)	(206.4)	(206.5)	(51.5)
Purchase of associate companies		(1.0)	—	—	—
Proceeds on disposal of tangible fixed assets		2.1	1.1	1.2	1.5
Capital grants received		10.0	7.3	11.6	2.8
Net cash outflow from capital expenditure and financial investments		(289.3)	(198.0)	(193.7)	(47.2)
Acquisitions and disposals					
Proceeds on disposal of associate		—	132.3	0.5	—
Proceeds on disposal of subsidiary undertaking (see note 12)		—	—	0.3	—
Net cash transferred on sale of subsidiary		—	—	(0.4)	—
Purchase of minority interests in subsidiary undertakings		—	—	(0.2)	—
Net cash inflow from acquisitions and disposals		—	132.3	0.2	—
Equity dividends paid		(55.9)	(58.3)	(60.9)	—
Cash (outflow)/inflow before management of liquid resources		(193.8)	49.0	(102.2)	(54.6)
Management of liquid resources					
Purchase of short term deposits		(636.2)	(1,610.0)	(1,342.7)	(358.2)
Disposal of short term deposits		679.0	1,444.1	1,531.8	362.9
Deposits with parent company	(b)	14.2	(12.4)	(401.3)	21.6
Net cash inflow/(outflow) from management of liquid resources		57.0	(178.3)	(212.2)	26.3
Financing					
New long term borrowings received	(b)	154.2	458.0	326.4	2.0
Borrowings repaid	(b)	(6.3)	(164.6)	(135.0)	(0.2)
Payment of principal under hire purchase contracts and finance leases	(b)	(4.7)	(3.8)	(3.2)	(1.1)
Net cash inflow from financing		143.2	289.6	188.2	0.7
Increase/(decrease) in cash in the period		6.4	160.3	(126.2)	(27.6)
Reconciliation of net cash flow to movements in net borrowings					
Increase/(decrease) in cash in the period		6.4	160.3	(126.2)	(27.6)
Cash inflow from financing		(143.2)	(289.6)	(188.2)	(0.7)
Cash (inflow)/outflow from management of liquid resources		(57.0)	178.3	212.2	(26.3)
(Increase)/decrease in net borrowings resulting from cash flows	(b)	(193.8)	49.0	(102.2)	(54.6)
Inception of new finance lease contracts	(b)	(3.1)	(3.2)	(5.4)	(1.4)
(Increase)/decrease in net borrowings in the period		(196.9)	45.8	(107.6)	(56.0)
Net borrowings at start of the period		(857.5)	(1,054.4)	(1,008.6)	(1,116.2)
Net borrowings at end of the period	(b)	(1,054.4)	(1,008.6)	(1,116.2)	(1,172.2)

Net borrowings is the sum of all borrowings net of cash and short term deposits.

Notes to the Cash Flow Statements

(a) Net cash inflow from operating activities

	Notes	Year ended 31 December 2000 £m	2001 £m	2002 £m	Three months ended 31 March 2003 £m
Operating profit	2	183.6	155.9	165.3	39.7
Depreciation of tangible fixed assets	3(b)/10	70.5	81.2	85.6	21.9
Profit on disposal of tangible fixed assets	3(b)	(0.4)	(0.6)	(1.0)	(0.4)
Write off of investment		—	—	—	0.6
Other non cash movements		0.2	—	(0.3)	—
Amortisation of capital grants	22	(3.4)	(3.6)	(3.0)	(0.7)
Movement in other provisions		(7.5)	3.0	(6.2)	(8.7)
Decrease/(increase) in stocks		1.7	0.3	(1.2)	1.9
Decrease/(increase) in debtors		14.9	9.4	(13.7)	(3.3)
(Decrease)/increase in creditors		(14.7)	(2.0)	10.3	(30.1)
Net cash inflow from operating activities		244.9	243.6	235.8	20.9

(b) Analysis of net borrowings

	As at 1 January 2000 £m	Cash flow £m	Other non cash changes £m	As at 31 December 2000 £m
Cash at bank	24.8	14.6	—	39.4
Bank overdrafts	(24.2)	(8.2)	—	(32.4)
Cash	0.6	6.4	—	7.0
Borrowings due after one year	(903.1)	(154.2)	157.8	(899.5)
Borrowings due within one year	(11.0)	6.3	(157.8)	(162.5)
Finance leases	(59.1)	4.7	(3.1)	(57.5)
Financing	(973.2)	(143.2)	(3.1)	(1,119.5)
Deposits with parent company	27.5	(14.2)	—	13.3
Cash deposits	87.6	(42.8)	—	44.8
Liquid resources	115.1	(57.0)	—	58.1
Total	(857.5)	(193.8)	(3.1)	(1,054.4)

Notes to Cash Flow Statements

	As at 1 January 2001 £m	*Cash flow £m*	*Other non cash changes £m*	*As at 31 December 2001 £m*
Cash at bank	39.4	149.4	—	188.8
Bank overdrafts	(32.4)	10.9	—	(21.5)
Cash	7.0	160.3	—	167.3
Borrowings due after one year	(899.5)	(458.0)	132.8	(1,224.7)
Borrowings due within one year	(162.5)	164.6	(132.8)	(130.7)
Finance leases	(57.5)	3.8	(3.2)	(56.9)
Financing	(1,119.5)	(289.6)	(3.2)	(1,412.3)
Deposits with parent company	13.3	12.4	—	25.7
Cash deposits	44.8	165.9	—	210.7
Liquid resources	58.1	178.3	—	236.4
Total	(1,054.4)	49.0	(3.2)	(1,008.6)

	As at 1 January 2002 £m	*Cash flow £m*	*Other non cash changes £m*	*As at 31 December 2002 £m*
Cash at bank	188.8	(126.4)	—	62.4
Bank overdrafts	(21.5)	0.2	—	(21.3)
Cash	167.3	(126.2)	—	41.1
Borrowings due after one year	(1,224.7)	(326.4)	18.8	(1,532.3)
Borrowings due within one year	(130.7)	135.0	(22.8)	(18.5)
Finance leases	(56.9)	3.2	(5.4)	(59.1)
Financing	(1,412.3)	(188.2)	(9.4)	(1,609.9)
Deposits with parent company	25.7	401.3	4.0	431.0
Cash deposits	210.7	(189.1)	—	21.6
Liquid resources	236.4	212.2	4.0	452.6
Total	(1,008.6)	(102.2)	(5.4)	(1,116.2)

	As at 1 January 2003 £m	*Cash flow £m*	*Other non cash changes £m*	*As at 31 March 2003 £m*
Cash at bank	62.4	(25.7)	—	36.7
Bank overdrafts	(21.3)	(1.9)	—	(23.2)
Cash	41.1	(27.6)	—	13.5
Borrowings due after one year	(1,532.3)	(2.0)	0.4	(1,533.9)
Borrowings due within one year	(18.5)	0.2	(0.4)	(18.7)
Finance leases	(59.1)	1.1	(1.4)	(59.4)
Financing	(1,609.9)	(0.7)	(1.4)	(1,612.0)
Deposits with parent company	431.0	(21.6)	—	409.4
Cash deposits	21.6	(4.7)	—	16.9
Liquid resources	452.6	(26.3)	—	426.3
Total	(1,116.2)	(54.6)	(1.4)	(1,172.2)

Notes to Cash Flow Statements

(c) Analysis of cash balances

	As at 1 January 2000 £m	*Trading for the year £m*	*As at 31 December 2000 £m*
Cash at bank and short term deposits	112.4	(28.2)	84.2
Less short term deposits with maturity dates greater than one day	(87.6)	42.8	(44.8)
	24.8	14.6	39.4
Bank overdrafts	(24.2)	(8.2)	(32.4)
	0.6	6.4	7.0

	As at 1 January 2001 £m	*Trading for the year £m*	*As at 31 December 2001 £m*
Cash at bank and short term deposits	84.2	315.3	399.5
Less short term deposits with maturity dates greater than one day	(44.8)	(165.9)	(210.7)
	39.4	149.4	188.8
Bank overdrafts	(32.4)	10.9	(21.5)
	7.0	160.3	167.3

	As at 1 January 2002 £m	*In respect of disposal of subsidiary £m*	*Trading for the year £m*	*As at 31 December 2002 £m*
Cash at bank and short term deposits	399.5	(0.1)	(315.4)	84.0
Less short term deposits with maturity dates greater than one day	(210.7)	—	189.1	(21.6)
	188.8	(0.1)	(126.3)	62.4
Bank overdrafts	(21.5)	—	0.2	(21.3)
	167.3	(0.1)	(126.1)	41.1

The cash position in respect of the disposal of subsidiary, £0.1 million, represents a net of £0.3 million cash consideration and cash at bank and in hand disposed £0.4 million.

	As at 1 January 2003 £m	*Trading for the period £m*	*As at 31 March 2003 £m*
Cash at bank and short term deposits	84.0	(30.4)	53.6
Less short term deposits with maturity dates greater than one day	(21.6)	4.7	(16.9)
	62.4	(25.7)	36.7
Bank overdrafts	(21.3)	(1.9)	(23.2)
	41.1	(27.6)	13.5

6. Notes to the Financial Information

1. Accounting Policies

The financial information has been prepared in accordance with applicable United Kingdom law and accounting standards. A summary of the more important accounting policies, which have been applied consistently, is set out below.

(a) *Basis of accounting*

The financial information has been prepared under the historical cost convention and on the going concern basis.

(b) *Basis of consolidation*

The financial information includes NSL and all its subsidiary undertakings together ("the NSL Group"). The results of subsidiaries acquired during the period are included from the date of their acquisition. The results of subsidiaries disposed of during the financial period are included to the date of their disposal. Intra-group sales and profits are eliminated fully on consolidation. Where, for commercial reasons, the accounting reference date of a subsidiary is a date other than that of NSL, management accounts made up to the NSL's accounting reference date have been used.

(c) *Associated undertakings and joint ventures*

The NSL Group's share of profits less losses of associated undertakings and joint ventures is included in the consolidated profit and loss account and the NSL Group's share of their net assets/liabilities is included in the consolidated balance sheet. Joint ventures are accounted for using the gross equity method. Goodwill arising on the acquisition of associates and joint ventures is accounted for in accordance with the accounting policy set out below.

(d) *Goodwill*

Goodwill arising on the acquisition of subsidiary undertakings, businesses, associates and joint ventures, representing the excess of the fair value of the consideration given over the fair value of the identifiable assets and liabilities acquired, is capitalised and written off on a straight line basis over its useful economic life up to a maximum of 20 years. Provision is made for any impairment. Goodwill arising on acquisitions in the period ended 22 December 1998 and prior was written off to reserves in accordance with the accounting standard then in force. As permitted by the current accounting standard, the goodwill previously written off to reserves has not been re-instated in the balance sheet. In the event of the subsequent disposal of the business to which it related, goodwill will be taken to the profit and loss account.

(e) *Turnover*

Turnover, which excludes value added tax, represents the income receivable in the ordinary course of business for goods and services provided.

(f) *Tangible fixed assets and depreciation*

Tangible fixed assets, including assets in the course of construction, comprise infrastructure assets (being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls) and other assets (including properties, overground plant and equipment):

(i) Infrastructure assets

Infrastructure assets comprise a network of physical overground and underground systems. Expenditure on infrastructure assets relating to increases in capacity or enhancements to the network and on maintaining the operating capability of the network, in accordance with defined standards of service, is treated as additions which are included at cost. Costs include internal and external costs to bring the asset into use. The depreciation charge for infrastructure assets is the estimated average amount of expenditure required to maintain the operating capability of the network, which is based on independently certified asset management plans, adjusted to reflect differences between estimated and actual expenditure over each five year regulatory period.

(ii) Other assets

Other assets are included at cost less accumulated depreciation and any provision for impairment. Freehold land is not depreciated. Other assets are depreciated evenly over their estimated economic lives, which are principally as follows: freehold buildings, 30 to 60 years; short leasehold land and buildings, 25 years or lease term if shorter; operational structures, plant and machinery, 4 to 80 years; fixtures, fittings, tools and equipment, 4 to 10 years.

(iii) Assets in the course of construction

Assets in the course of construction are not depreciated until commissioned.

(g) *Grants and contributions*

Revenue grants are credited to the profit and loss account in the period to which they relate. Capital grants and contributions relating to tangible fixed assets are treated as deferred income and amortised in the profit and loss account over the expected useful economic lives of the qualifying assets. Specifically, in the case of infrastructure assets, the expected useful economic lives have been determined by reference to the physical replacement cycle of those assets.

(h) *Fixed asset investments*

Fixed asset investments are stated at their purchase cost, less any provision for impairment.

(i) *Hire purchase and leasing*

Where assets are financed by hire purchase or leasing arrangements which transfer substantially all the risks and rewards of ownership to the NSL Group, the assets are treated as if they had been purchased and the corresponding capital cost is treated as a liability. Rentals or leasing payments are treated as consisting of a capital element and finance costs, the capital element reducing the outstanding liability and the finance costs being written off to the profit and loss account over the period of the hire purchase contract or lease in proportion to the reducing outstanding liability. Rental costs arising under operating leases are expensed in the period they are incurred.

(j) *Stocks*

Stores are stated at cost less any provisions necessary to recognise damage and obsolescence. Work in progress and finished goods are valued at the lower of cost and net realisable value. Cost includes labour, materials, transport and an element of overheads.

(k) *Pension costs*

The cost of providing pension benefits is charged to the profit and loss account so as to spread the cost over the expected average service lives of employees. Differences between the amounts funded and amounts charged to the profit and loss account are treated as prepayments or provisions in the balance sheet. Pension surpluses/deficits arising on acquisition are recognised as an asset/liability on the balance sheet, in accordance with FRS 7.

(l) *Taxation*

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events have occurred at that date that will result in an obligation to pay more, or a right to pay less or to receive more, tax, with the following exceptions:

- provision is made for deferred tax on gains arising from the revaluation (and similar fair value adjustments) of fixed assets, and gains on disposal of fixed assets that have been rolled over into replacement assets, only to the extent that, at the balance sheet date, there is a binding agreement to dispose of the assets concerned. However, no provision is made where, on the basis of all available evidence at the balance sheet date, it is more likely than not that the taxable gain will be rolled over into replacement assets and charged to tax only where the replacement assets are sold;

- provision is made for deferred tax that would arise on remittance of the retained earnings of overseas subsidiaries, associates and joint ventures only to the extent that, at the balance sheet date, dividends have been accrued as receivable;
- deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax is calculated at the tax rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date. Deferred tax is discounted using the post tax yields to maturity that could be obtained at the balance sheet date on government bonds with maturity dates similar to those of the deferred tax assets and liabilities.

(m) *Research and development*

Research and development expenditure is charged to the profit and loss account in the period in which it is incurred.

(n) *Foreign currencies*

Assets and liabilities of subsidiaries in foreign currencies are translated into sterling at rates of exchange ruling at the end of the financial period and the results of foreign subsidiaries are translated at the average rate of exchange for the period. Differences on exchange arising from the re-translation of the opening net investment in subsidiary and associate companies, and from the translation of the results of those companies at average rate, are taken to reserves. All other foreign exchange differences are taken to the profit and loss account in the period in which they arise.

(o) *Derivative financial instruments*

The NSL Group utilises interest rate swaps, forward rate agreements and forward exchange contracts as derivative financial instruments. A derivative instrument is considered to be used for hedging purposes when it alters the risk profile of an underlying exposure of the NSL Group in line with the NSL Group's risk management policies. Interest rate swap agreements are used to manage interest rate exposures. Amounts payable or receivable in respect of these derivatives are recognised over the period of the contracts as adjustments to net interest payable in the profit and loss account. Forward exchange contracts are valued at the period end rates of exchange. Resultant gains and losses are offset against foreign exchange gains or losses on the related borrowings or, where the instrument is used to hedge a committed future transaction, are deferred until the transaction occurs.

(p) *Liquid resources*

Liquid resources comprise external deposits and deposits with the parent company.

2. Segmental Analysis

(a) *Analysis by class of business and by geographical origin*

Turnover – Year ended 31 December 2000

	UK *£m*	*Rest of Europe, Middle East and Far East* *£m*	*Rest of World* *£m*	*Total* *£m*	*Inter Segment* *£m*	*External Turnover* *£m*
UK Water	446.6	—	—	446.6	(0.5)	446.1
International Water	0.5	7.2	—	7.7	—	7.7
Related Services	73.1	2.7	2.5	78.3	(34.6)	43.7
Total	520.2	9.9	2.5	532.6	(35.1)	497.5

Turnover – Year ended 31 December 2001

	UK £m	*Rest of Europe, Middle East and Far East £m*	*Rest of World £m*	*Total £m*	*Inter Segment £m*	*External Turnover £m*
UK Water	436.1	—	—	436.1	(0.8)	435.3
International Water	0.3	7.4	—	7.7	—	7.7
Related Services	70.2	6.0	2.3	78.5	(32.1)	46.4
Total	506.6	13.4	2.3	522.3	(32.9)	489.4

Turnover – Year ended 31 December 2002

	UK £m	*Rest of Europe, Middle East and Far East £m*	*Rest of World £m*	*Total £m*	*Inter Segment £m*	*External Turnover £m*
UK Water	439.2	—	—	439.2	—	439.2
International Water	5.8	7.9	1.2	14.9	(0.6)	14.3
Related Services	73.8	5.7	2.6	82.1	(31.6)	50.5
Total	518.8	13.6	3.8	536.2	(32.2)	504.0

Turnover – Three months ended 31 March 2003

	UK £m	*Rest of Europe, Middle East and Far East £m*	*Rest of World £m*	*Total £m*	*Inter Segment £m*	*External Turnover £m*
UK Water	110.4	—	—	110.4	—	110.4
International Water	4.1	1.9	—	6.0	(0.2)	5.8
Related Services	17.6	1.4	—	19.0	(7.1)	11.9
Total	132.1	3.3	—	135.4	(7.3)	128.1

Operating Profit – Year ended 31 December 2000

	UK £m	*Rest of Europe, Middle East and Far East £m*	*Rest of World £m*	*Total £m*	*Central unallocated costs and provisions £m*	*Group operating profit £m*	*Share of associates' operating profit £m*	*Share of joint ventures' operating profit £m*	*Investment income £m*	*Except profit on disposal of associate £m*	*Net interest payable £m*	*Profit on ordinary activities before taxation £m*
UK Water	194.2	—	—	194.2								
International Water	(1.2)	0.2	(0.2)	(1.2)								
Related Services	(2.6)	0.7	0.1	(1.8)								
Total	190.4	0.9	(0.1)	191.2	(7.6)	183.6	2.8	1.0	—	—	(81.5)	105.9

Operating Profit – Year ended 31 December 2001

	UK £m	Rest of Europe, Middle East and Far East £m	Rest of World £m	Total £m	Central unallocated costs and provisions £m	Group operating profit £m	Share of associates' operating profit £m	Share of joint ventures' operating profit £m	Investment income £m	Except profit on disposal of associate £m	Net interest payable £m	Profit on ordinary activities before taxation £m
UK Water	160.5	—	—	160.5								
International Water	(2.6)	0.8	(0.3)	(2.1)								
Related Services	0.2	0.6	0.2	1.0								
Total	158.1	1.4	(0.1)	159.4	(3.5)	155.9	3.3	1.0	—	29.4	(79.7)	109.9

Operating Profit – Year ended 31 December 2002

	UK £m	Rest of Europe, Middle East and Far East £m	Rest of World £m	Total £m	Central unallocated costs and provisions £m	Group operating profit £m	Share of associates' operating profit £m	Share of joint ventures' operating profit £m	Investment income £m	Except profit on disposal of associate £m	Net interest payable £m	Profit on ordinary activities before taxation £m
UK Water	162.2	—	—	162.2								
International Water	1.8	0.9	(1.3)	1.4								
Related Services	(1.2)	0.4	0.2	(0.6)								
Total	162.8	1.3	(1.1)	163.0	2.3	165.3	0.6	1.3	0.2	—	(75.2)	92.2

Operating Profit – Three months ended 31 March 2003

	UK £m	Rest of Europe, Middle East and Far East £m	Rest of World £m	Total £m	Central unallocated costs and provisions £m	Group operating profit £m	Share of associates' operating profit £m	Share of joint ventures' operating profit £m	Investment income £m	Except profit on disposal of associate £m	Net interest payable £m	Profit on ordinary activities before taxation £m
UK Water	40.5	—	—	40.5								
International Water	(0.2)	—	—	(0.2)								
Related Services	0.6	0.1	—	0.7								
Total	40.9	0.1	—	41.0	(1.3)	39.7	1.0	0.3	—	—	(21.4)	19.6

The central unallocated costs and provisions include those costs that relate to the performance of the holding company's functions.

(b) *Analysis of external turnover by geographical destination*

	Year ended 31 December			*Three months ended 31 March*
	2000 £m	*2001 £m*	*2002 £m*	*2003 £m*
UK	474.8	467.9	482.2	123.6
Rest of Europe, Middle East and Far East	17.9	19.8	19.5	4.3
Rest of World	4.8	1.7	2.3	0.2
External turnover	497.5	489.4	504.0	128.1

(c) *Net assets*

As at 31 December 2001

	Subsidiary undertakings £m	*Share of associated undertakings £m*	*Net operating assets £m*	*Unallocated net liabilities £m*	*Net assets £m*
UK Water	2,030.6	—	2,030.6		
International Water	55.5	—	55.5		
Related Services	(28.1)	4.0	(24.1)		
Total	2,058.0	4.0	2,062.0	(1,037.3)	1,024.7

As at 31 December 2002

	Subsidiary undertakings £m	*Share of associated undertakings £m*	*Net operating assets £m*	*Unallocated net liabilities £m*	*Net assets £m*
UK Water	2,142.9	—	2,142.9		
International Water	55.2	—	55.2		
Related Services	(13.9)	6.1	(7.8)		
Total	2,184.2	6.1	2,190.3	(1,136.5)	1,053.8

As at 31 March 2003

	Subsidiary undertakings £m	*Share of associated undertakings £m*	*Net operating assets £m*	*Unallocated net liabilities £m*	*Net assets £m*
UK Water	2,217.4	—	2,217.4		
International Water	56.9	—	56.9		
Related Services	(17.7)	5.4	(12.3)		
Total	2,256.6	5.4	2,262.0	(1,192.0)	1,070.0

Net operating assets comprise tangible fixed assets, stocks, debtors and creditors which relate to segmental operating activities. Unallocated net liabilities comprise other fixed asset investments, current investments, cash and short term deposits, borrowings, current taxation balances, dividends and other common assets and liabilities.

The net assets of the NSL Group are almost entirely situated in the United Kingdom.

3. (a) **Operating Costs**

	Year ended 31 December			*Three months ended 31 March*
	2000	*2001*	*2002*	*2003*
	£m	*£m*	*£m*	*£m*
This is stated after charging/(crediting):				
Materials and consumables	23.4	27.6	27.8	5.6
Manpower costs (see note 7)	100.0	101.3	109.8	26.4
Own work capitalised	(26.2)	(26.2)	(28.9)	(6.4)
Depreciation of tangible fixed assets	70.5	81.2	85.6	21.9
Other operating charges	150.9	153.2	147.4	41.6
Other operating income	(4.7)	(3.6)	(3.0)	(0.7)
Total operating costs	313.9	333.5	338.7	88.4

Own work capitalised includes both employment and other costs charged to capital schemes.

(b) **Operating profit**

	Year ended 31 December			*Three months ended 31 March*
	2000	*2001*	*2002*	*2003*
	£m	*£m*	*£m*	*£m*
This is stated after charging/(crediting):				
Auditors' remuneration				
– audit*	0.2	0.2	0.2	—
– non-audit services*	0.1	0.1	0.1	—
Depreciation				
– owned	62.9	77.2	81.1	20.8
– under hire purchase contracts and finance leases	7.6	4.0	4.5	1.1
Costs of research and development	5.6	5.3	5.5	1.4
Operating leases				
– plant and machinery	0.8	0.6	0.2	—
– other	3.2	1.3	1.2	0.3
Profit on disposal of tangible fixed assets	(0.4)	(0.6)	(1.0)	(0.4)
Amortisation of capital grants	(3.4)	(3.6)	(3.0)	(0.7)

* Amounts charged for auditors' remuneration in 2001 and 2000 were payable to Andersens.

4. Net Interest Payable

	Year ended 31 December			*Three months ended 31 March*
	2000	*2001*	*2002*	*2003*
	£m	*£m*	*£m*	*£m*
Interest payable on debentures, bank and other loans and overdrafts	73.9	83.2	91.7	25.7
Amortisation of discount, fees and loan issue costs	—	0.3	(0.3)	—
Amounts receivable on derivative contracts	—	(1.2)	(3.1)	(0.1)
Interest payable on hire purchase contracts and finance leases	3.6	2.8	2.8	0.5
Group interest payable	77.5	85.1	91.1	26.1
Share of associates' interest payable	7.6	0.7	0.8	0.6
Share of joint ventures' interest payable	0.3	0.3	0.3	0.1
Total interest payable	85.4	86.1	92.2	26.8
Interest receivable from parent undertaking	(3.6)	(6.4)	(17.0)	(5.4)
Net interest payable	81.8	79.7	75.2	21.4
Disclosed as:				
Net interest payable:				
Group	73.9	78.7	74.1	20.7
Associates	7.6	0.7	0.8	0.6
Joint ventures	0.3	0.3	0.3	0.1
	81.8	79.7	75.2	21.4

5. Exceptional Profit on Disposal of Associate

NSL disposed of its 35 per cent. holding in SITA Holdings UK Limited on 29 June 2001 and the profit before tax of £29.4 million in the prior year financial statements was stated after charging £116.4 million of goodwill previously written off to reserves.

	Year ended 31 December 2001
	£m
Sale proceeds	132.3
Goodwill previously written off to the Group reconstruction relief reserve	(107.6)
Goodwill previously written off to the profit and loss reserve	(8.8)
Investment in associate	(1.0)
Provision	14.5
Exceptional profit before tax	29.4
Tax arising on disposal	(9.0)
Exceptional profit after tax	20.4

6. Directors' Remuneration and Interests

	Year ended 31 December			Three months ended 31 March
	2000	*2001*	*2002*	*2003*
	£000	*£000*	*£000*	*£000*
Emoluments	616	466	377	103

	2000	*2001*	*2002*	*2003*
	No.	*No.*	*No.*	*No.*
Members of defined benefits scheme	3	3	2	1

The amounts in respect of the highest paid directors are as follows:

	2000	*2001*	*2002*	*2003*
	£000	*£000*	*£000*	*£000*
Emoluments	172	146	229	69
Accrued defined benefit entitlement	—	—	65	69

During 2001 three directors exercised share options (2000: nil).

7. Employee Information

The total employment costs of all employees (including directors) of the NSL Group were:

	Year ended 31 December			Three months ended 31 March
	2000	*2001*	*2002*	*2003*
	£m	*£m*	*£m*	*£m*
Wages and salaries	84.4	85.7	94.0	22.3
Social security costs	7.5	7.3	7.7	1.9
Other pension costs	8.1	8.3	8.1	2.2
Total employment costs	100.0	101.3	109.8	26.4
Total employment costs were charged as follows:				
Capital schemes and infrastructure renewals	25.7	24.3	27.4	6.0
Manpower costs	74.3	77.0	82.4	20.4
	100.0	101.3	109.8	26.4

The average monthly number of employees of the NSL Group during the year was:

	Year ended 31 December			Three months ended 31 March
	2000	*2001*	*2002*	*2003*
	Number	*Number*	*Number*	*Number*
UK Water	2,155	2,185	2,259	2,281
International Water	118	113	122	122
Related Services	1,207	1,141	1,182	1,141
	3,480	3,439	3,563	3,544

8. Tax on Profit on Ordinary Activities

(a) *Analysis of tax charge for the periods:*

	Year ended 31 December 2000 £m	*2001 £m*	*2002 £m*	*Three months ended 31 March 2003 £m*
Current tax:				
UK corporation tax on profits for the period at 30%	5.3	10.0	6.2	1.3
Adjustment in respect of prior years	0.1	(7.7)	(14.4)	—
Share of associates' tax (credit)/charge	(3.1)	1.5	(1.8)	0.6
Share of joint ventures' tax charge	0.2	0.2	0.3	0.1
Total current tax charge/(credit) (see note 8b)	2.5	4.0	(9.7)	2.0
Deferred tax:				
Origination and reversal of timing differences in the period (before discounting)	26.9	25.4	25.0	5.4
Adjustment in respect of prior years (before discounting)	0.2	4.2	10.9	(1.2)
	27.1	29.6	35.9	4.2
Increase in discount	(10.1)	(22.4)	(25.7)	(2.8)
Total deferred tax (see note 21)	17.0	7.2	10.2	1.4
Tax on profit on ordinary activities	19.5	11.2	0.5	3.4

(b) *Factors affecting the tax charge/(credit) for the periods:*

	Year ended 31 December 2000 £m	*2001 £m*	*2002 £m*	*Three months ended 31 March 2003 £m*
Profit on ordinary activities before taxation	105.9	109.9	92.2	19.6
Profit on ordinary activities multiplied by standard rate of UK corporation tax (30%) (2002, 2001 and 2000: 30%)	31.8	33.0	27.7	5.9
Effects of:				
Expenses not deductible for tax purposes	1.0	2.1	2.2	0.7
Not taxable income	(3.2)	—	—	—
Depreciation in respect of non-qualifying items	1.2	1.1	1.1	0.3
Capital allowances in excess of depreciation	(29.5)	(25.0)	(26.1)	(5.9)
Other timing differences	2.1	(0.9)	0.6	0.4
Pension revaluation surplus	0.5	0.5	0.5	0.1
Disposal of investments in subsidiaries/associates	—	0.2	(0.1)	—
Differences in associates'/joint ventures' tax	(1.5)	0.7	(1.2)	0.5
Adjustment to tax charge in respect of prior years	0.1	(7.7)	(14.4)	—
Total current tax charge/(credit) (see note 8a)	2.5	4.0	(9.7)	2.0

(c) *Factors that may affect future tax charges:*

The NSL Group expects to continue to incur high levels of capital expenditure and, accordingly, it expects to be able to claim capital allowances in excess of depreciation at a similar level to the current year.

Deferred tax is provided on a discounted basis using post-tax yields on UK government gilts. The charge for deferred tax may therefore be influenced by future fluctuations in gilt rates.

In addition, there are tax losses of approximately £9.0 million (2002: £9.0 million, 2001: £9.8 million) available to be carried forward and set against future profits arising in territories outside the United Kingdom.

9. Dividends

	Year ended 31 December			*Three months ended 31 March*
	2000	*2001*	*2002*	*2003*
	£m	*£m*	*£m*	*£m*
Interim paid of nil pence (2002: 6.68 pence, 2001: 6.39 pence, 2000: 6.115 pence) per £1 ordinary share	28.5	29.8	31.1	—
Second interim proposed of nil pence (2002: 6.68 pence, 2001: 6.39 pence, 2000: 6.115 pence) per £1 ordinary share	28.5	29.8	31.2	—
	57.0	59.6	62.3	—

10. Tangible Fixed Assets

	Freehold land and buildings £m	*Short leasehold land and buildings £m*	*Infra-structure assets £m*	*Operational structures, plant and machinery £m*	*Fixtures, fittings, tools and equipment £m*	*Assets in the course of construction £m*	*Total £m*
Cost:							
At 31 December 2001	128.4	5.2	1,172.1	1,321.4	156.1	171.2	2,954.4
Additions	—	—	—	0.4	1.6	207.4	209.4
Schemes commissioned	0.6	—	95.1	150.2	6.1	(252.0)	—
Reclassification	(39.4)	—	37.6	20.3	(32.5)	13.5	(0.5)
Disposals	(0.4)	—	(16.8)	(0.3)	(4.1)	—	(21.6)
At 31 December 2002	89.2	5.2	1,288.0	1,492.0	127.2	140.1	3,141.7
Additions	—	—	—	0.1	0.2	53.9	54.2
Schemes commissioned	4.1	—	53.2	2.1	14.2	(73.6)	—
Reclassification	—	—	—	—	—	—	—
Disposals	—	—	(5.4)	(0.3)	—	—	(5.7)
At 31 March 2003	93.3	5.2	1,335.8	1,493.9	141.6	120.4	3,190.2
Depreciation:							
At 31 December 2001	27.1	1.4	89.7	309.5	90.8	—	518.5
Charge for the year	0.9	0.1	29.0	48.1	7.5	—	85.6
Reclassification	(1.3)	—	—	0.5	0.3	—	(0.5)
Disposals	(0.2)	—	(16.9)	(0.3)	(3.9)	—	(21.3)
At 31 December 2002	26.5	1.5	101.8	357.8	94.7	—	582.3
Charge for the period	0.6	0.1	7.2	12.3	1.6	—	21.8
Reclassification	1.2	—	—	(1.6)	0.4	—	—
Disposals	—	—	(4.3)	(0.3)	—	—	(4.6)
At 31 March 2003	28.3	1.6	104.7	368.2	96.7	—	599.5
Net book amounts:							
at 31 December 2001	101.3	3.8	1,082.4	1,011.9	65.3	171.2	2,435.9
at 31 December 2002	62.7	3.7	1,186.2	1,134.2	32.5	140.1	2,559.4
at 31 March 2003	65.0	3.6	1,231.1	1,125.7	44.9	120.4	2,590.7

Operational structures, plant and machinery includes an element of land and buildings dedicated to those assets.

The net book amount of tangible fixed assets held under hire purchase contracts and finance leases was as follows:

The Group does not capitalise finance costs.

	As at 31 December 2001 £m	*2002 £m*	*As at 31 March 2003 £m*
Infrastructure assets	2.2	2.2	2.2
Operational structures, plant and machinery	27.9	25.4	25.4
Fixtures, fittings, tools and equipment	1.9	4.5	4.5
	32.0	32.1	32.1

11. Fixed Asset Investments

(a)

	Joint ventures £m	*Associated undertakings £m*	*Other investments £m*	*Total £m*
At 31 December 2001	2.0	2.0	0.6	4.6
Additions	—	—	0.4	0.4
Transfer from other debtors	0.5	—	—	0.5
Disposals	—	(0.5)	—	(0.5)
Share of profits	0.7	1.6	—	2.3
Dividends received	(0.2)	—	—	(0.2)
At 31 December 2002	3.0	3.1	1.0	7.1
Additions	—	—	—	—
Disposals	—	—	(0.6)	(0.6)
Share of profits	0.1	(0.2)	—	(0.1)
Dividends received	—	—	—	—
At 31 March 2003	3.1	2.9	0.4	6.4

All fixed asset investments are unlisted.

(b) *The NSL Group's interests in principal trading associates at 31 March 2003 were as follows:*

Name of undertaking	*Country of incorporation or registration and operation*	*Description of shares held*	*Proportion of nominal value of issued shares held by Group and Company %*	*Business Activity*
Water and Sanitation Services South Africa (PTY) Limited	South Africa	Ordinary shares of 1 Rand	50	Water and sewerage services
Ayr Environmental Services Limited	Scotland	Ordinary shares of £1	50	Water and sewerage services

Water and Sanitation Services South Africa (Pty) Limited was disposed of on 22 April 2003 for a consideration of £0.9 million.

(c) *Joint ventures*

The NSL Group holds 50 per cent. of the nominal value of issued ordinary £1 shares in Vehicle Lease and Service Limited (VLS), the NSL Group's principal joint venture arrangement. VLS was incorporated in England and Wales and undertakes the business of hiring, leasing and servicing of vehicles and plant.

(d) *The NSL Group's interests in principal subsidiaries at 31 March 2003 were as follows:*

Name of undertaking	*Country of incorporation or registration and operation*	*Description of shares held*	*Proportion of nominal value of issued shares held by Group and Company %*	*Business Activity*
Northumbrian Water Limited	England and Wales	Ordinary shares of £1	100	Water and sewerage services
Lyonnaise des Eaux (Gibraltar) Limited	Gibraltar	Ordinary shares of £1	67	Water and sewerage services
Entec UK Limited	England and Wales	Ordinary shares of £1	100	Environmental and engineering consultancy
Northumbrian Lyonnaise Technology and Research Centre Limited	England and Wales	Ordinary shares of £1	100	Research and development
Analytical & Environmental Services Limited	England and Wales	Ordinary shares of £1	100	Analytical laboratory and scientific services
Fastflow Pipeline Services Limited	England and Wales	Ordinary shares of £1	100	Infrastructure replacement and rehabilitation
Caledonian Environmental Services plc	Scotland	Ordinary shares of £1	75	Water and sewerage services
Northumbrian Water Finance plc	England and Wales	Ordinary shares of £1	100	Holding of finance instruments

The Directors consider that to give full particulars of all subsidiary and associated undertakings would lead to a statement of excessive length. The above information relates to those subsidiary and associated undertakings or NSL groups of undertakings whose results or financial position, in the opinion of the directors, principally affect the figures of the NSL Group.

12. Disposal of Subsidiary

On 23 December 2002, the NSL Group sold its investment in Imass Limited. The book and fair values of the related assets and liabilities disposed of were as follows:

	Sale of investment *£m*
Fixed assets	0.1
Stocks	0.1
Debtors	1.3
Cash at bank and in hand	0.4
Creditors due in less than one year	(1.6)
Net assets disposed of	0.3
Profit on disposal	0.4
	0.7
Satisfied by:	
Cash	0.3
Preference shares	0.4
	0.7
Net cash flow in respect of the disposal comprised:	
Cash consideration	0.3
Cash at bank and in hand disposed	(0.4)
Net cash outflow	(0.1)

13. Stocks

	As at 31 December 2001 *£m*	*2002* *£m*	*As at 31 March 2003* *£m*
Stores	3.1	3.2	3.6
Work in progress	3.3	4.3	2.0
	6.4	7.5	5.6

14. Debtors

	As at 31 December 2001 *£m*	*2002* *£m*	*As at 31 March 2003* *£m*
Amounts receivable within one year:			
Trade debtors	59.6	64.5	71.4
Amounts owed by parent company and fellow subsidiaries	30.7	432.0	411.6
Other debtors	9.2	8.7	9.7
Prepayments and accrued income	27.6	40.8	35.4
	127.1	546.0	528.1
Amounts receivable after more than one year:			
Pension surplus on acquisition (note 26)	19.8	18.1	17.7

Trade debtors are shown net of bills paid in advance.

15. Cash at Bank and Short Term Deposits

	As at 31 December 2001 £m	*2002 £m*	*As at 31 March 2003 £m*
Short term cash deposits	210.7	21.6	16.9
Cash at bank	188.8	62.4	36.7
	399.5	84.0	53.6

16. Creditors: Amounts falling due within one year

	As at 31 December 2001 £m	*2002 £m*	*As at 31 March 2003 £m*
Bank loans and overdrafts (see note 18)	44.1	39.7	41.6
Eurobond – due 1 February 2002 bearing interest rate of 9.25 per cent. (see note 18)	100.0	—	—
Debentures (see note 18)	8.0	—	—
Obligations under hire purchase contracts and finance leases (see note 19)	3.7	3.2	3.2
Trade creditors	10.1	8.8	13.4
Amounts owed to parent company and fellow subsidiaries	5.6	3.6	5.7
Amounts owed to associates	—	—	2.4
Other creditors	24.9	19.5	16.1
Taxation and social security	22.0	8.1	8.2
Dividends payable:			
equity shareholders	29.8	31.2	31.1
Accruals and deferred income	134.3	145.6	105.8
	382.5	259.7	227.5

The creditor for taxation and social security in the NSL Group includes corporation tax amounting to £3.9 million (2002: £3.3 million, 2001: £18.7 million).

Amounts owed to parent company and fellow subsidiaries in the NSL Group includes amounts payable for the provisional surrender of tax losses amounting to £3.1 million (2002: £3.2 million, 2001: £0.5 million).

17. Creditors: Amounts falling due after more than one year

	As at 31 December		As at 31 March
	2001	*2002*	*2003*
	£m	*£m*	*£m*
Loans (see note 18)	295.5	357.1	359.1
Debentures (see note 18)	14.3	14.3	14.3
Eurobond – due 28 June 2006 bearing interest rate of 8.625 per cent.	200.0	200.0	200.0
Eurobond – due 11 October 2017 bearing interest rate of 6.0 per cent.	301.0	300.8	300.8
Eurobond – due 6 February 2023 bearing interest rate of 6.875 per cent.	351.7	351.7	351.6
Eurobond – due 29 April 2033 bearing interest rate of 5.625 per cent.	—	246.5	246.5
Eurobond – due 31 March 2037 bearing interest rate of 6.627 per cent.	61.7	58.1	58.1
Amounts owed to parent company and fellow subsidiaries (see note 18)	0.5	3.8	3.5
Obligations under hire purchase contracts and finance leases (see note 19)	53.2	55.9	56.2
Other creditors	14.9	14.4	13.7
	1,292.8	1,602.6	1,603.8

At 31 March 2003, the NSL Group had the following interest swap arrangements: £15.0 million over a ten year period commencing on 10 May 1994 under which the NSL Group is required to pay interest at a rate linked to LIBOR and will receive interest at 9.00 per cent.; £10.0 million over a seven year period commencing on 16 December 1996 under which the NSL Group is required to pay interest at a rate linked to LIBOR and will receive interest at 7.45 per cent.; £10.0 million over a three year period commencing 31 January 2000 under which the NSL Group is required to pay interest at a rate linked to LIBOR and will receive interest at 7.165 per cent.; and £25.0 million over a three year period commencing on 7 December 2000 under which the NSL Group is required to pay interest at 5.61 per cent. and will receive interest at a rate linked to LIBOR.

18. Loans

	As at 31 December 2001 £m	2002 £m	As at 31 March 2003 £m
Loans are repayable as follows:			
Less than one year	130.7	18.5	18.7
Between one and two years	23.1	53.1	53.1
Between two and five years	305.6	259.1	260.8
In more than five years	896.0	1,220.1	1,220.0
	1,355.4	1,550.8	1,552.6
Disclosed as due:			
Within one year:			
Bank loans and overdrafts	44.1	39.7	41.6
Eurobonds	100.0	—	—
Debentures	8.0	—	—
Amounts owed to parent company and fellow subsidiaries	0.1	0.1	0.3
Less: Bank overdrafts	(21.5)	(21.3)	(23.2)
After one year:			
Loans	295.5	357.1	359.1
Eurobonds	914.4	1,157.1	1,157.0
Debentures	14.3	14.3	14.3
Amounts owed to parent company and fellow subsidiaries	0.5	3.8	3.5
	1,355.4	1,550.8	1,552.6

Loans to the NSL Group from third parties, any part of which falls due for repayment in five years or more and which are repayable by instalments, amount to £259.9 million (2002: £259.9 million, 2001: £181.4 million) and bear rates of interest in the range of 4.94 per cent. to 8.55 per cent. (2002: 4.94 per cent. to 8.55 per cent., 2001: 7.16 per cent. to 8.55 per cent.). None (2001: £0.6 million) of these loans bear interest rates linked to LIBOR.

Loans to the NSL Group from third parties repayable otherwise than by instalments which fall due for repayment after more than five years amount to £1,031.8 million (2002: £1,029.8 million, 2001: £996.7 million) and bear rates of interest in the range of 3.5 per cent. to 11.75 per cent. (2002: 3.5 per cent. to 11.75 per cent., 2001: 3.5 per cent. to 11.75 per cent.). Of these loans, £120.5 million (2002: £120.5 million, 2001: £75.0 million) bears interest rates linked to LIBOR.

The aggregate amount of NSL Group loans, any part of which falls due for repayment in five years or more, is £1,291.7 million (2002: £1,289.7 million, 2001: £1,178.1 million).

Loans include fixed rate indebtedness to the European Investment Bank. If these loans are terminated prior to their agreed maturity date, break costs may be incurred. As these break costs would be determined by reference to fixed rates at the time of termination, the potential costs cannot be estimated at this stage.

Included in the loans are debenture stocks as follows:

(a) £8.7 million issued by North East Water plc and secured by a floating charge on the assets of Northumbrian Water Limited;

(b) £5.6 million issued by Essex and Suffolk Water plc and secured by a floating charge on the assets of Northumbrian Water Limited.

19. Obligations under Hire Purchase Contracts and Finance Leases

	As at 31 December 2001 £m	2002 £m	As at 31 March 2003 £m
Amounts due:			
In less than one year	3.7	3.2	3.2
Between one and two years	2.9	3.2	3.3
Between two and five years	9.2	8.9	8.7
In more than five years	75.4	68.9	68.8
Gross obligations	91.2	84.2	84.0
Less: finance charges allocated to future periods	(34.3)	(25.1)	(24.6)
	56.9	59.1	59.4
Disclosed as due:			
Within one year	3.7	3.2	3.2
After more than one year	53.2	55.9	56.2
	56.9	59.1	59.4

The aggregate gross amount of obligations under hire purchase contracts and finance leases, any part of which falls due for repayment in five years or more, is £77.1 million (2002: £77.2 million, 2001: £89.6 million).

20. Derivatives and Financial Instruments

The NSL Group's policy in respect of derivative financial instruments is disclosed in note 1(o).

(a) *NSL Group strategy*

The level of capital expenditure which the NSL Group is obliged to incur is such that it cannot be wholly financed by internally generated sources. As a result, the NSL Group must rely upon raising additional finance on a regular basis, to be principally used to fund the long term assets required in its regulated business. The NSL Group's strategy is to finance such investment by raising medium to long term debt, to provide a balance sheet match with long term assets and to fix a major proportion of interest rates.

(b) *Treasury operations*

The main purpose of the NSL Group's treasury function is to assess the NSL Group's ongoing capital requirement and to raise funding on a timely basis, taking advantage of any favourable market opportunities. It also invests any surplus funds the NSL Group may have with financial institutions and the parent company have based upon its forecast requirements and in accordance with the NSL Group's treasury policy. On occasion, derivatives are used as part of this process, but the NSL Group's policies prohibit their use for speculation.

(c) *Risks arising from NSL Group's financial instruments*

The main risks arising from the NSL Group's financial instruments are liquidity risk, interest rate risk and foreign currency risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below. All treasury activities are conducted in accordance with these policies. As at 31 March 2003, and after taking into account the effects of interest rate swaps the Group had 89 per cent. of its debt at fixed rates which is within the board approved policy of not less than 60 per cent. of the Group's debt to be at fixed rate.

(d) *Liquidity risk*

As regards day to day liquidity, the NSL Group's policy is to have available standby committed bank borrowing facilities with a value of no less than £50.0 million and with a bank agreement availability period of no less than three months. At the period end the policy is in place.

(e) *Interest rate risk*

The NSL Group finances its operations through a mixture of retained profits and bank borrowings. It borrows at both fixed and floating rates of interest and accordingly uses interest rate swaps to generate the desired interest profile and to manage the NSL Group's exposure to interest rate fluctuations. The NSL Group's policy is to keep a minimum 60 per cent. of its borrowings at fixed rates of interest. At the period ends the NSL Group is in line with the stated policy.

(f) *Foreign currency risk*

The NSL Group's policy is that any foreign currency exposure in excess of £100,000 sterling equivalent of a transactional nature or £3.0 million sterling equivalent of a translation nature, should be covered immediately on identification.

(g) *Market price risk*

The NSL Group's exposure to market price risk principally comprises interest rate exposures. The NSL Group's policy is to accept a degree of interest rate risk. On the basis of the NSL Group's analysis, it is estimated that a one per cent. rise in interest rates would not have a material affect on the NSL Group's pre-tax profits.

(h) *Interest rate risk profile of financial assets and financial liabilities*

The interest rates and currency profile of the NSL Group's net borrowings at 31 December 2001 were:

			Fixed rate net borrowings		
	Total net borrowings £m	*Variable rate net borrowings £m*	*Borrowings £m*	*Weighted average interest rate %*	*Weighted average period until maturity Years*
Currency					
Sterling borrowings:					
Bank loans	318.1	90.8	227.3	7.56	9.4
Eurobonds	1,014.4	—	1,014.4	7.13	15.0
Debentures	22.3	—	22.3	10.53	4.5
Finance leases	56.9	51.0	5.9	8.64	6.0
	1,411.7	141.8	1,269.9	7.47	14.2
Euro borrowings:					
Amounts owed to parent company	0.6	0.6	—		
Cash including overdrafts	(378.0)	(378.0)	—		
Sterling loans receivable	(25.7)	(25.7)	—		
Net borrowings at 31 December 2001	1,008.6	(261.3)	1,269.9		

In addition there are provisions due after more than one year which are £22.0 million on which no interest is payable.

The interest rates and currency profile of the NSL Group's net borrowings at 31 December 2002 were:

Currency	Total net borrowings £m	Variable rate net borrowings £m	Fixed rate net borrowings: Borrowings £m	Weighted average interest rate %	Weighted average period until maturity Years
Sterling borrowings:					
Amounts owed to parent company and fellow subsidiaries	3.2	—	3.2	5.25	34.3
Bank loans	375.5	135.4	240.1	6.55	10.6
Eurobonds	1,157.1	—	1,157.1	6.64	18.7
Debentures	14.3	—	14.3	9.84	4.5
Finance leases	59.1	52.1	7.0	7.15	5.8
	1,609.2	187.5	1,421.7	6.66	17.27
Amounts owed to parent company:					
Euro borrowings	0.4	0.4	—		
SA Rand borrowings	0.3	0.3	—		
Cash including overdrafts	(62.8)	(62.8)	—		
Sterling loans receivable	(430.9)	(325.9)	(105.0)		
Net borrowings at 31 December 2002	1,116.2	(200.5)	1,316.7		

In addition there are provisions due after more than one year which are £2.9 million, on which no interest is payable.

The interest rates and currency profile of the NSL Group's net borrowings at 31 March 2003 were:

Currency	Total net borrowings £m	Variable rate net borrowings £m	Fixed rate net borrowings: Borrowings £m	Weighted average interest rate %	Weighted average period until maturity Years
Sterling borrowings:					
Amounts owed to parent company and fellow subsidiaries	3.2	—	3.2	5.25	34.0
Bank loans	375.5	135.4	240.1	6.55	10.3
Eurobonds	1,157.0	—	1,157.0	6.64	18.5
Debentures	14.3	—	14.3	9.84	4.2
Finance leases	59.4	52.7	6.7	7.09	5.5
	1,609.4	188.1	1,421.3	6.66	16.9
Amounts owed to parent company:					
Euro borrowings	0.4	0.4	—		
SA Rand borrowings	0.2	0.2	—		
Cash including overdrafts	(30.4)	(30.4)	—		
Gibraltar borrowings	2.0	2.0	—		
Sterling loans receivable	(409.4)	(304.4)	(105.0)		
Net borrowings at 31 March 2003	1,172.2	(144.1)	1,316.3		

In addition there are provisions due after more than one year which are £2.9 million, on which no interest is payable.

As permitted by FRS 13, short term debtors and creditors have been excluded from the disclosures, other than the currency disclosures.

The variable rate net borrowings comprise sterling denominated bank borrowings and deposits that bear interest at rates based upon up to 12 months' LIBOR.

Included within the external sterling borrowings of the NSL Group above are loans amounting to £21.3 million (2002: £21.3 million, 2001: £108.8 million) whose rates are fixed for a period of five to seven years from their inception and which, under the terms of the respective loan agreements, can then either be repaid or rolled over for a similar period at a new fixed rate, based upon prevailing market rates at that date. The weighted average period for which the rates on such loans are fixed has been taken as the same average period until maturity.

Included in the debentures above are £2.1 million (2002: £2.1 million, 2001: £2.1 million) of irredeemable debentures, which have been excluded from the calculation of the weighted average maturity and fixed periods.

(i) *Currency exposures*

At 31 March 2003, after taking into account the effects of forward foreign exchange contracts, the NSL Group had no currency exposures (2002: nil, 2001: nil).

(j) *Borrowing facilities*

The NSL Group has various undrawn committed borrowing facilities. The facilities available at 31 March 2003, in respect of which all conditions precedent have been met are as follows:

	As at 31 December		*As at 31 March*
	2001	*2002*	*2003*
	£m	*£m*	*£m*
Expiring in one year or less	50.0	100.0	40.0
Expiring in more than one year but not more than three years	75.0	—	—
	125.0	100.0	40.0

(k) *Fair values of financial assets and financial liabilities*

	As at 31 December				*As at 31 March*	
	2001		*2002*		*2003*	
	Book value	*Fair value*	*Book value*	*Fair value*	*Book value*	*Fair value*
	£m	*£m*	*£m*	*£m*	*£m*	*£m*
Primary financial instruments held or issued to finance the Group's operations:						
Short term financial liabilities and current portion of long term borrowings	155.9	161.7	43.0	46.6	45.0	48.9
Long term borrowings	1,277.9	1,325.7	1,588.2	1,695.3	1,590.3	1,661.0
Financial assets	(425.2)	(425.2)	(515.0)	(496.4)	(463.1)	(463.1)
Derivative financial instruments held to manage the interest rate and currency profile:						
Interest rate swaps	—	(2.2)	—	(1.0)	—	(0.7)
Provision for liabilities and charges	(22.0)	(22.0)	(2.9)	(2.9)	(2.9)	(2.9)
Total	986.6	1,038.0	1,113.3	1,241.6	1,169.3	1,243.2

The fair values of the interest rate swaps, forward foreign currency contracts and sterling denominated long term fixed rate debt with a book value of £1,171.3 million (2002: £1,174.6 million, 2001: £1,036.7 million) have been determined by reference to prices available from the markets on which the instruments involved are traded. All the other fair values shown above have been calculated by discounting cash flows at prevailing interest rates.

(l) *Gains and losses on hedges*

The NSL Group enters into forward foreign currency contracts to eliminate the currency exposures that arise on sales denominated in foreign currencies immediately those sales are transacted. It also uses interest rate swaps to manage its interest rate profile. Changes in the fair value of instruments used as hedges are not recognised in the financial statements until the hedged position matures.

An analysis of these unrecognised gains and losses at 31 December 2000 is as follows:

	Gains £m	*Losses £m*	*Total net gains/ (losses) £m*
Unrecognised gains and losses on hedges at 1 January 2000	2.2	0.1	2.1
Gains and losses arising in previous years that were recognised in 2000	1.0	0.1	0.9
Gains and losses arising before 1 January 2000 that were not recognised in 2000	1.2	—	1.2
Gains and losses arising in 2000 that were not recognised in 2001	1.6	—	1.6
Unrecognised gains and losses on hedges at 31 December 2000	2.8	—	2.8
Of which:			
Gains and losses expected to be recognised in 2001	1.0	—	1.0
Gains and losses expected to be recognised in 2002 or later	1.8	—	1.8

An analysis of these unrecognised gains and losses as at 31 December 2001 is as follows:

	Gains £m	*Losses £m*	*Total net gains/ (losses) £m*
Unrecognised gains and losses on hedges at 1 January 2001	2.8	—	2.8
Gains and losses arising in previous years that were recognised in 2001	(1.3)	—	(1.3)
Gains and losses arising before 1 January 2001 that were not recognised in 2001	1.5	—	1.5
Gains and losses arising in 2001 that were not recognised in 2001	1.1	0.4	0.7
Unrecognised gains and losses on hedges at 31 December 2001	2.6	0.4	2.2
Of which:			
Gains and losses expected to be recognised in 2002	1.4	0.3	1.1
Gains and losses expected to be recognised in 2003 or later	1.2	0.1	1.1

An analysis of these unrecognised gains and losses as at 31 December 2002 is as follows:

	Gains *£m*	*Losses* *£m*	*Total net gains/ (losses)* *£m*
Unrecognised gains and losses on hedges at 1 January 2002	2.6	0.4	2.2
Gains and losses arising in previous years that were recognised in 2002	(1.4)	(0.4)	(1.0)
Gains and losses arising before 1 January 2002 that were not recognised in 2002	1.2	—	1.2
Gains and losses arising in 2002 that were not recognised in 2002	0.3	0.4	(0.1)
Unrecognised gains and losses on hedges at 31 December 2002	1.5	0.4	1.1
Of which:			
Gains and losses expected to be recognised in 2003	0.8	0.4	0.4
Gains and losses expected to be recognised in 2004 or later	0.7	—	0.7

An analysis of these unrecognised gains and losses as at 31 March 2003 is as follows:

	Gains *£m*	*Losses* *£m*	*Total net gains/ (losses)* *£m*
Unrecognised gains and losses on hedges at 1 January 2003	1.4	0.4	1.0
Gains and losses arising in previous years that were recognised to March 2003	—	—	—
Gains and losses arising before 1 January 2003 that were not recognised in March 2003	1.4	0.4	1.0
Gains and losses arising to March 2003 that were not recognised in March 2003	—	0.3	(0.3)
Unrecognised gains and losses on hedges at 31 March 2003	1.4	0.7	0.7
Of which:			
Gains and losses expected to be recognised in the period April 2003 to March 2004	0.7	0.6	0.1
Gains and losses expected to be recognised from April 2004 or later	0.7	0.1	0.6

21. Provisions for Liabilities and Charges

	Investment in associate £m	*Reorganisation and restructuring provision £m*	*Pension provision £m*	*Deferred taxation £m*	*Other £m*	*Total £m*
At 31 December 2000	14.5	6.9	8.9	144.7	3.2	178.2
Charged/(credited) to the profit and loss account	—	0.7	(0.7)	7.2	4.4	11.6
Other movements	(13.5)	—	—	—	—	(13.5)
Share of profit in associate	(1.0)	—	—	—	—	(1.0)
Utilised during the year	—	(1.3)	—	—	(0.1)	(1.4)
At 31 December 2001	—	6.3	8.2	151.9	7.5	173.9
(Credited)/charged to the profit and loss account	—	(0.2)	(0.6)	10.2	1.2	10.6
Reclassification	—	7.6	(7.6)	—	—	—
Utilised during the year	—	(0.8)	—	—	(5.8)	(6.6)
At 31 December 2002	—	12.9	—	162.1	2.9	177.9
Charged/(credited) to the profit and loss account	—	4.4	—	1.4	—	5.8
Utilised during the period	—	(13.1)	—	—	—	(13.1)
At 31 March 2003	—	4.2	—	163.5	2.9	170.6

The reorganisation and restructuring provision represents outstanding pension contributions in respect of costs of restructuring programmes within the NSL Group. Following the recommendation of the actuary of the pension scheme in which the individuals concerned belong, the amount was paid in full in January 2003 with the approval of the trustees of the pension scheme.

The provision for deferred tax comprises:

	As at 31 December		*As at 31 March*
	2001 £m	*2002 £m*	*2003 £m*
Accelerated capital allowances	420.1	457.0	461.8
Other timing differences	(52.3)	(52.8)	(53.3)
Pension revaluation surplus	6.0	5.5	5.4
Undiscounted provision for deferred tax	373.8	409.7	413.9
Discount	(221.9)	(247.6)	(250.4)
Discounted provision for deferred tax	151.9	162.1	163.5

Other provisions comprise contract issues representing the best estimate of amounts payable, principally in the next 24 months, and provisions held in respect of dilapidations.

22. Accruals and Deferred Income

Capital grants and contributions:

	£m
At 31 December 2000	115.9
Additions	7.3
Amortisation in the year	(3.6)
At 31 December 2001	119.6
Additions	11.6
Amortisation in the year	(3.0)
At 31 December 2002	128.2
Additions	2.8
Amortisation in the period	(0.7)
At 31 March 2003	130.3

23. Called up Share Capital

The share capital of the NSL Group is shown below:

	As at 31 December		*As at 31 March*
	2001	*2002*	*2003*
	£m	*£m*	*£m*
Authorised:			
1,000 million ordinary shares of £1 each	1,000.0	1,000.0	1,000.0
Allotted, called up and fully paid:			
466.2 million ordinary shares of £1 each	466.2	466.2	466.2

24. Reserves

	Share premium account £m	*Group recon-struction relief reserve £m*	*Profit and loss account £m*
At 31 December 2000	217.9	—	182.4
Goodwill previously written off (see note 5)	—	107.6	8.8
Retained profit for the financial year	—	—	38.5
At 31 December 2001	217.9	107.6	229.7
Exchange differences	—	—	0.2
Retained profit for the financial year	—	—	29.5
At 31 December 2002	217.9	107.6	259.4
Exchange differences	—	—	—
Retained profit for the period	—	—	15.9
At 31 March 2003	217.9	107.6	275.3

25. Reconciliation of Movement in Equity Shareholders' Funds

	As at 31 December			*As at 31 March*
	2000	*2001*	*2002*	*2003*
	£m	*£m*	*£m*	*£m*
Profit for the financial period	86.3	98.1	91.8	15.9
Dividends	(57.0)	(59.6)	(62.3)	—
Retained profit for the period	29.3	38.5	29.5	15.9
Exchange differences	—	—	0.2	—
Goodwill previously written off (see note 5)	—	116.4	—	—
Increase in equity shareholders' funds	29.3	154.9	29.7	15.9
Opening equity shareholders' funds as previously stated	837.2	866.5	1,021.4	1,051.1
Closing equity shareholders' funds	866.5	1,021.4	1,051.1	1,067.0

26. Pensions

(a) *SSAP 24*

The NSL Group operates a funded defined benefit pension scheme, providing benefits based on final pensionable remuneration to 2,345 employees. The scheme, named the Northumbrian Lyonnaise Pension Scheme, comprises four unitised sub-funds – Water Pension Scheme ("WPS"), Northern, Southern and Mirror Image Scheme ("MIS").

The assets of the scheme are held separately from those of the NSL Group in independently administered funds.

The most recent actuarial valuation of the scheme was at 31 December 2001. At that date the market value of assets amounted to £441 million in aggregate (excluding MIS which was transferred into the scheme on 1 April 2002 and was valued at approximately £20 million). The 2001 valuation disclosed that the combined value of the assets represented 109 per cent. of the value of the accrued liabilities. The NSL Group contributed a further £15.0 million to the scheme on 2 January 2003.

The following table sets out the agreed contributions based on the 31 December 2001 valuations:

	Section			
	WPS	*Northern*	*Southern*	*MIS*
Members' contributions	6%	5%	5%	5%/6%
Employers' contributions	15.5%	10.5%	Nil	6%/7.2%

NSL's contribution rate was assessed using the Projected Unit Method and the following actuarial assumptions:

	As at 31 December 2001
	%
Investment return:	
Pre retirement	6.2
Post retirement	5.7
Pay increases:	
For 5 years after 1998 valuation date	3.8
Thereafter	4.3
Pension increases	2.8
Price inflation	2.8

The next valuation will be carried out at 31 December 2004. An independent qualified actuary performs the actuarial valuation.

The SSAP 24 pension surplus is shown in note 14, amounts receivable after more than one year.

The Northumbrian Water Group Personal Pension Plan provides defined contribution benefits to 775 employees.

The NSL Group made contributions of £1.8 million (2002: £6.4 million).

Additional disclosures regarding the NSL Group's defined benefit scheme are required under the transitional provisions of FRS 17 'Retirement benefits' and these are set out below. The disclosures relate to the second year of the transitional provisions.

A qualified actuary using revised assumptions that are consistent with the requirements of FRS 17 has updated the actuarial valuation described above at 31 December 2001. Investments have been valued, for this purpose, at fair value.

(b) *FRS 17*

FRS 17 actuarial assumptions:

	As at 31 December 2001 %	*2002* %	*As at 31 March 2003* %
Pay increases:			
For 5 years after 1998 valuation date	3.8	—	—
Thereafter	4.3	3.5	3.5
Pension increases	2.8	2.5	2.5
Price inflation	2.8	2.5	2.5
Discount rate	5.9	5.4	5.3

The fair value of the assets in the scheme, the present value of the liabilities in the scheme and the long-term expected rate of return at 31 December 2001, 31 December 2002 and 31 March 2003 were:

	As at 31 December				*As at 31 March*	
	2001 Long-term expected rate of return %	*2001* £m	*2002 Long-term expected rate of return* %	*2002* £m	*2003 Long-term expected rate of return* %	*2003* £m
Equities	7.5	288.0	7.0	268.9	6.8	253.2
Corporate bonds	5.8	9.9	5.4	14.4	5.3	14.3
Government bonds	4.9	72.1	4.8	46.9	4.5	41.9
Property	6.5	47.0	6.0	48.9	5.8	49.3
Cash	4.0	23.0	4.0	9.2	3.8	25.7
Total fair value of assets		440.0		388.3		384.4
Present value of scheme liabilities		(377.0)		(464.6)		(497.7)
Surplus/(deficit) in the scheme		63.0		(76.3)		(113.3)
Related deferred tax (liability)/asset		(18.9)		22.9		34.0
Net pension asset/(liability)		44.1		(53.4)		(79.3)

Analysis of the amount that would have been charged to operating profit under FRS 17:

	Year ended 31 December 2002 £m	*Three months ended 31 March 2003 £m*
Current service cost	7.9	2.1
	7.9	2.1

Analysis of the amount that would have been credited to net finance income under FRS 17:

	Year ended 31 December 2002 £m	*Three months ended 31 March 2003 £m*
Expected return on pension scheme assets	25.6	6.2
Interest on pension scheme liabilities	(21.8)	(6.3)
	3.8	(0.1)

Analysis of the actuarial loss that would have been recognised in the statement of total recognised gains and losses:

	Year ended 31 December 2002 £m	*Three months ended 31 March 2003 £m*
Actual return less expected return on pension scheme assets	(67.1)	(23.6)
Experience gains and losses arising on the scheme liabilities	(52.1)	12.1
Changes in assumptions underlying the present value of the scheme liabilities	(22.6)	(24.7)
	(141.8)	(36.2)

History of experience gains and losses

	Year ended 31 December 2002 £m	*Three months ended 31 March 2003 £m*
Difference between the expected and actual return on scheme assets:		
Amount (£m)	(67.1)	(23.6)
Percentage of scheme assets	17.3%	6.1%
Experience gains and losses on scheme liabilities:		
Amount (£m)	(52.1)	12.1
Percentage of the present value of scheme liabilities	11.2%	2.4%
Total actuarial gain recognised in the statement of total recognised gains and losses:		
Amount (£m)	(141.8)	(36.2)
Percentage of the present value of scheme liabilities	30.5%	7.8%

Reconciliation of net assets and reserves under FRS 17

Net assets

	As at 31 December 2001 £m	*As at 31 December 2002 £m*	*As at 31 March 2003 £m*
Net assets as stated in balance sheet	1,024.7	1,053.8	1,070.0
SSAP 24 balance	(19.8)	(18.1)	(17.7)
Related deferred tax	6.0	5.5	5.4
Net assets excluding defined benefit assets/(liabilities)	1,010.9	1,041.2	1,057.7
FRS 17 pension assets	440.0	388.3	384.4
FRS 17 defined benefit liabilities	(377.0)	(464.6)	(497.7)
Related deferred tax	(18.9)	22.9	34.0
Net assets including defined benefit assets/(liabilities)	1,055.0	987.8	978.4

Reserves

	As at 31 December 2001 £m	*As at 31 December 2002 £m*	*As at 31 March 2003 £m*
Profit and loss account as stated in balance sheet	229.7	259.4	275.3
SSAP 24 balance	(19.8)	(18.1)	(17.7)
Related deferred tax	6.0	5.5	5.4
Profit and loss account excluding amounts relating to defined benefit assets/(liabilities)	215.9	246.8	263.0
FRS 17 pension assets	440.0	388.3	384.4
FRS 17 defined benefit liabilities	(377.0)	(464.6)	(497.7)
Related deferred tax	(18.9)	22.9	34.0
Profit and loss account including defined benefit assets/(liabilities)	260.0	193.4	183.7

Analysis of the movement in surplus/(deficit) in the scheme

Movement in surplus during the period

	Year ended 31 December 2002 £m	*Three months ended 31 March 2003 £m*
Surplus/(deficit) in scheme at beginning of the period	63.0	(76.3)
Adjustment to surplus at the beginning of the period	1.2	—
Current service cost	(7.9)	(2.1)
Employer contributions	5.4	1.4
Net return	3.8	(0.1)
Actuarial (losses)	(141.8)	(36.2)
Deficit in scheme at end of period	(76.3)	(113.3)

27. Financial Commitments

(a) *Capital expenditure:*

	As at 31 December 2000 £m	*As at 31 December 2001 £m*	*As at 31 December 2002 £m*	*As at 31 March 2003 £m*
Expenditure contracted for	82.5	95.0	67.0	67.6

In addition to these commitments, the NSL Group has longer term expenditure plans, which include investment to meet shortfalls in performance and condition and to provide for new demand and growth within the water and sewerage business.

(b) *Lease commitments:*

The NSL Group has entered into non-cancellable operating leases in respect of land and buildings, plant, machinery and motor vehicles. The total amount payable under these leases in the next year is as follows:

	As at 31 December			*As at 31 March*
	2000	*2001*	*2002*	*2003*
	£m	*£m*	*£m*	*£m*
Land and buildings				
Leases which expire:				
Within one year	0.3	0.9	0.5	0.5
Within two to five years	0.2	0.1	0.2	0.2
After five years	0.6	0.5	0.3	0.3
	1.1	1.5	1.0	1.0
Other				
Leases which expire:				
Within one year	0.5	0.7	0.3	0.3
Within two to five years	1.7	0.6	0.7	0.7
After five years	—	—	0.1	0.1
	2.2	1.3	1.1	1.1

28. Related Party Transactions

Transactions with other members of the Suez Group outside the NSL Group, comprised:

	As at 31 December			*As at 31 March*
	2000	*2001*	*2002*	*2003*
	£m	*£m*	*£m*	*£m*
Sales	5.7	3.3	3.6	2.9
Purchases	25.9	24.5	28.8	2.3
The amounts due to and from these companies was:				
Debtors	15.1	30.7	433.2	407.9
Creditors	4.6	6.1	4.1	4.9

29. Post Balance Sheet Event

At 31 March 2003 the ultimate parent company and the controlling party of NSL was SUEZ SA, incorporated in France. By 23 May 2003, the entire share capital of NSL had been acquired by Atlantic Water Limited, a subsidiary of Suez S.A. On 23 May 2003, the entire share capital of Atlantic Water Limited was acquired by Northumbrian Water Group plc whose shares were admitted to the Alternative Investment Market of the London Stock Exchange. The intercompany balances with the parent company as at 31 March 2003 were settled as part of this transaction.

Yours faithfully

Ernst & Young LLP

PART 5

Accountants' Report on the Company

ERNST & YOUNG

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Northumbrian Water Group plc
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The Directors
Collins Stewart Limited
9th floor
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EC2V 7QR

18 September 2003

Dear Sirs

Northumbrian Water Group plc

We report on the financial information set out below. This financial information has been prepared for inclusion in the listing particulars dated 18 September 2003 of Northumbrian Water Group plc (the "Company").

The Company was incorporated with the name Aquavit plc on 12 May 2003 and changed its name to Northumbrian Water Group plc on 20 May 2003.

Basis of preparation

The financial information set out below is based on the non-statutory financial statements of the Company from incorporation to 15 May 2003 prepared on the basis described in note 1 to which no adjustments were considered necessary.

Responsibility

Such financial statements are the responsibility of the directors of the Company.

The directors of the Company are responsible for the contents of the listing particulars dated 18 September 2003 in which this report is included.

It is our responsibility to compile the financial information set out in our report from the financial statements, to form an opinion on the financial information and to report our opinion to you.

Basis of opinion

We conducted our work in accordance with the Statements of Investment Circular Reporting Standards issued by the Auditing Practices Board of the United Kingdom. Our work included an assessment of evidence relevant to the amounts and disclosures in the financial information. It also included an assessment of significant estimates and judgements made by those responsible for the preparation of the financial statements underlying the financial information and whether the accounting policies are appropriate to the entity's circumstances, consistently applied and adequately disclosed.

We planned and performed our work so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial information is free from material misstatement whether caused by fraud or other irregularity or error.

Opinion

In our opinion the financial information gives, for the purposes of the listing particulars dated 18 September 2003, a true and fair view of the state of affairs of the Company at 15 May 2003.

1. Profit and loss accounts

During the period the Company did not trade and received no income and incurred no expenditure. Consequently, during the period the Company made neither a profit nor a loss.

2. Balance sheet

	Note	£
Current assets		
Other debtors		37,500
Cash at bank and in hand		12,500
		50,000
Capital and reserves		
Called up share capital	2	50,000

3. Cash flow

Financing	£
Issue of ordinary shares	12,500
Increase in cash in the period	12,500

4. Notes to the financial information

1. The Company was incorporated on 12 May 2003. The Company has not yet commenced business, no audited financial statements have been made up and no dividends have been declared or paid since the date of incorporation.

   Basis of preparation

   The financial information has been prepared in accordance with applicable UK law and accounting standards.

2. Called up Share Capital

Authorised	
750,000,000 ordinary shares of £0.10 each	£75,000,000
Allotted, called up	£
125,000 ordinary shares of £0.10 each – paid	12,500
375,000 ordinary shares of £0.10 each – unpaid	37,500
	50,000

3. On 23 May 2003 the Company acquired the entire issued share capital of Atlantic Water Limited, the immediate holding company of Northumbrian Services Limited, and the shares of the Company were admitted to the Alternative Investment Market of the London Stock Exchange.

Yours faithfully

Ernst & Young LLP

PART 6

Unaudited Pro Forma Financial Information

Admission will not affect the net assets or profit and loss account of the Group. However, the most recent financial information in this document pertaining to the operations of the Group (included in the accountants' reports in Parts 4 and 5 of this document) is drawn up to a date prior to the Atlantic Acquisition. Accordingly, set out below are pro forma statements to show the impact of the Atlantic Acquisition, Placing and new debt facilities on the net assets and profit and loss account.

Pro Forma Profit Statement

The unaudited pro forma profit statement of the Group is provided for illustration purposes only to show the effect on the profit and loss account had the Placing, Atlantic Acquisition and related financing occurred on 1 January 2002 (being the beginning of the most recent period of 12 months for which financial information has been published). It has been compiled on the basis described below from the profit and loss account of the Company and NSL as set out in Parts 4 and 5 of this document. The unaudited pro forma combined financial information has been prepared for illustrative purposes only and, because of its nature, may not give a true picture of:

- the financial results of the Group had the Placing and Atlantic Acquisition and related financing in fact occurred on 1 January 2002; or
- the results of operations of the Group for any future period or its financial condition at any future date.

			Adjustments		
	Northumbrian Water Group plc 3 days to 15 May 2003 £m (Note 1)	*NSL 12 months to 31 December 2002 £m (Note 2)*	*Additional interest on new debt £m (Note 3)*	*Amortisation of goodwill arising £m (Note 4)*	*Pro forma Enlarged Group £m (Note 5-8)*
Group turnover	—	504	—	—	504
Operating costs	—	(339)	—	2	(337)
Operating profit	—	165	—	2	167
Share of associated undertakings' operating profit	—	1	—	—	1
Share of joint ventures' operating profit	—	1	—	—	1
Net interest payable	—	(75)	(21)	—	(96)
Profit on ordinary activities before taxation	—	92	(21)	2	73
Tax on profit on ordinary activities	—	—	6	—	6
Profit on ordinary activities after taxation	—	92	(15)	2	79
Minority interests	—	—	—	—	—
Profit for the financial year	—	92	(15)	2	79
Earnings per Share (pence)					15.2

Notes:

1. Extracted without material adjustment from the accountants' report on the Company as set out in Part 5 of this document.
2. Extracted without material adjustment from the accountants' report on NSL for the 12 months to 31 December 2002 as set out in Part 4 of this document.
3. An increase in net debt of £536 million is assumed to result in additional interest of £21 million, based on an interest rate of 4.00 per cent. (being the maximum rate payable on the new debt raised and associated hedge contracts). The tax effect of this is £6 million.
4. Negative goodwill of £42 million arises on the acquisition (based on the cost of investment of £1,028 million less net assets acquired of £1,070 million) and is amortised over a period of 20 years.
5. No account has been taken of the trading results since 15 May 2003 for the Company and since 31 December 2002 for NSL.
6. No account has been taken of fair value and accounting basis adjustments arising on acquisition.
7. All of the adjustments are considered to have a continuing effect.
8. Earnings per share is based on pro forma profit for the financial year of £79 million and the number of shares in issue of 518,632,845.

Pro Forma Statement of Net Assets

The following unaudited pro forma statement of net assets of the Group is provided for illustrative purposes only to show the effect on the net assets of the Group had the Placing, Atlantic Acquisition and related financing occurred on 15 May 2003. It has been compiled on the basis described below from the balance sheet of the Company at 15 May 2003 as set out in Part 5 of this document. The unaudited pro forma combined financial information has been prepared for illustrative purposes only and, because of its nature, may not give a true picture of:

- the financial position of the Group had the Placing and Atlantic Acquisition and related financing in fact occurred on 15 May 2003; or
- the results of operations of the Group for any future period or its financial condition at any future date.

	NWG 15 May 2003 (Note 1) £m	*NSL 31 March 2003 (Note 2) £m*	*Proceeds from Placing (Note 3) £m*	*New debt (Note 4) £m*	*Repayment of Suez loans (Note 5) £m*	*Cost of Atlantic Acquisition (Note 6) £m*	*Pro forma enlarged Group (Note 7-8) £m*
Fixed Assets							
Intangible assets	—	—	—	—	—	(42)	(42)
Tangible assets	—	2,591	—	—	—	—	2,591
Investments	—	3	—	—	—	—	3
Investments in joint ventures	—	3	—	—	—	—	3
	—	2,597	—	—	—	(42)	2,555
Current Assets							
Stock	—	5	—	—	—	—	5
Debtors less than 1 year	—	528	—	—	(349)	—	179
Debtors greater than 1 year	—	18	—	—	—	—	18
Cash	—	54	373	195	349	(898)	73
	—	605	373	195	—	(898)	275
Creditors due within 1 year	—	(227)	—	—	—	—	(227)
Net current assets/(liabilities)	—	378	373	195	—	(898)	48
Total assets less current liabilities	—	2,975	373	195	—	(940)	2,603
Creditors due after 1 year	—	(1,604)	—	(195)	—	—	(1,799)
Provisions	—	(171)	—	—	—	—	(171)
Accruals and deferred income	—	(130)	—	—	—	—	(130)
Net assets	—	1,070	373	—	—	(940)	503
Net debt (note 9)	—	(1,172)	373	—	—	(898)	(1,697)

Notes:

1. Extracted without material adjustment from the accountants' report on the Company at 15 May 2003 as set out in Part 5 of this document. The Company has share capital of £50,000, cash of £12,500 and unpaid share capital of £37,500.
2. Extracted without material adjustment from the accountants' report on NSL at 31 March 2003 as set out in Part 4 of this document.
3. The net proceeds from the Placing were £373 million (£389 million net of expenses of £16 million) which was used to fund the Atlantic Acquisition.
4. The new debt raised was £526 million (net of £10 million of expenses) which was used to fund the consideration for the Atlantic Acquisition. £331 million was subsequently repaid from existing cash balances, resulting in new net debt of £195 million.
5. £349 million of loans receivable from Suez (which were included in debtors receivable within one year) were repaid at the time of the Atlantic Acquisition.
6. The cost of the Atlantic Acquisition reflects the following:
   – the cost of the Atlantic Acquisition was £1,010 million, of which £880 million was in the form of cash and £130 million was in the form of fully paid consideration shares;
   – expenses of the Atlantic Acquisition were £18 million;
   – negative goodwill is based on the cost of investment of £1,028 million less net assets acquired of £1,070 million.
7. No account has been taken of the trading results since 15 May 2003 for the Company and since 31 March 2003 for NSL.
8. No account has been taken of fair value and accounting based adjustments arising on the Atlantic Acquisition.
9. Net debt is an aggregation of relevant amounts included within various categories in the above net asset statement (as set out in note 20 of the accountants report on NSL).

Reporting Accountants Letter

ERNST & YOUNG

The Directors
Northumbrian Water Group PLC
Northumbria House
Abbey Road
Pity Me
Durham
DH1 5FJ

Citygate
St James' Boulevard
Newcastle upon Tyne
NE1 4JD

The Directors
Collins Stewart Limited
9th Floor
88 Wood Street
London
EC2V 7QR

18 September 2003

Dear Sirs

Pro Forma Financial Information

We report on the pro forma financial information set out in Part 6 of the listing particulars dated 18 September 2003, which has been prepared, for illustrative purposes only, to provide information about how the Placing, Atlantic Acquisition and new debt facilities, might have affected the financial information of the Company had these been undertaken at the beginning of the period concerned or at the date stated for the accountants' reports as set out in Parts 4 and 5 of the Listing Particulars.

Responsibility

It is the responsibility solely of the directors of the Company to prepare the pro forma financial information in accordance with paragraph 12.29 of the Listing Rules.

It is our responsibility to form an opinion, as required by the Listing Rules on the pro forma financial information and to report our opinion to you.

Basis of opinion

We conducted our work in accordance with the Bulletin 1998/8 "Reporting on Pro Forma Financial Information Pursuant to the Listing Rules" issued by the Auditing Practices Board. Our work, which involved no independent examination of any of the underlying financial information, consisted primarily of comparing the unadjusted financial information with the source documents, considering the evidence supporting the adjustments and discussing the pro forma financial information with the directors of the Company.

Opinion

In our opinion:

(a) the pro forma financial information has been properly compiled on the basis stated;

(b) such basis is consistent with the accounting policies of the Company; and

(c) the adjustments are appropriate for the purposes of the pro forma financial information as disclosed pursuant to paragraph 12.29 of the Listing Rules.

Yours faithfully

Ernst & Young LLP

PART 7

Additional Information

1. Responsibility

The Directors, whose names appear on page 3, accept responsibility for the information contained in this document. To the best of the knowledge and belief of the Directors (who have taken all reasonable care to ensure that such is the case), the information contained in this document is in accordance with the facts and does not omit anything likely to affect the import of such information.

2. The Company

2.1 The Company was incorporated in England and Wales under the Act with the name Aquavit plc as a public company limited by shares on 12 May 2003, with number 4760441.

2.2 On 20 May 2003 pursuant to a written resolution of the Company, the Company's name was changed from Aquavit plc to Northumbrian Water Group plc.

2.3 The Company was issued with a certificate under Section 117 of the Act, enabling it to do business on 15 May 2003.

2.4 The Company's registered office is Northumbria House, Abbey Road, Pity Me, Durham DH1 5FJ.

3. Share Capital of the Company

3.1 The authorised share capital of the Company on incorporation was £75,000,000 divided into 750,000,000 Ordinary Shares of £0.10 each of which two were subscribed at par, nil paid, by Instant Companies Limited and Swift Incorporations Limited both having their registered address at 1 Mitchell Lane, Bristol, BS1 6BU.

3.2 The following changes have taken place in the issued share capital of the Company since incorporation:

(A) On 14 May 2003, the two subscriber shares of £0.10 each were transferred to Ecofin Limited and Bernard Lambilliotte respectively at £1.00 per share, each £0.10 paid.

(B) On 14 May 2003, 499,998 Ordinary Shares of £0.10 each were allotted to Ecofin Limited at £1.00 per share, of which 124,998 were £0.10 paid and 375,000 were nil paid.

(C) On 16 May 2003, the authorised share capital of the Company was reduced to £70,000,000 by the cancellation of 50,000,000 Ordinary Shares of 10p each which at such date had not been taken or agreed to be taken by any person.

(D) On 23 May 2003, effective on the AIM Admission, and pursuant to the authority given by the resolution referred to in paragraph 3.3 below:

(1) 388,967,884 Ordinary Shares of £0.10 each were allotted at £1.00 per share, each fully paid to various placees pursuant to the Placing in connection with the Atlantic Acquisition; and

(2) 129,655,961 Ordinary Shares of £0.10 each were allotted at £1.00 per share, fully paid to Suez as non-cash consideration for the Atlantic Acquisition.

3.3 On 16 May 2003, resolutions were passed to the following effect:

(A) the Directors were unconditionally authorised in accordance with Section 80 of the Act to allot relevant securities (as defined in Section 80(2) of the Act) up to an aggregate nominal amount of £70,000,000 such authority to expire on the conclusion of the next Annual General Meeting of the Company; and

(B) the Directors were empowered to allot equity securities (as defined in Section 94(2) of the Act) as if Section 89(1) of the Act did not apply during the period of the authority referred to in (A) above provided that such power be limited to (i) the allotment of equity securities pursuant to the Placing, (ii) the allotment of equity securities pursuant to a rights issue, and (iii) in addition to (i) and (ii) above up to an aggregate nominal value of £2,500,000.

3.4 Immediately following the AIM Admission the authorised share capital of the Company was £70,000,000 divided into 700,000,000 Ordinary Shares of which 518,623,845 Ordinary Shares (representing approximately 74.1 per cent. of the authorised share capital) were issued fully paid or credited as fully paid.

3.5 No shares in the capital of the Company are under option or have been agreed, conditionally or unconditionally, to be put under option.

3.6 Save as set out below in paragraph 9 of this Part 7 the Directors have no present intention to issue any of the unissued Ordinary Shares following Admission.

4. Subsidiary Undertakings

4.1 The Company is the holding company of the Group which has a leading UK water and sewerage business.

4.2 The following table shows the principal subsidiary and associated undertakings of the Company. Except where otherwise stated each of these companies is wholly owned by a member of the Group and the issued share capital is fully paid (and is based on the number of shares in issue as at 16 September 2003, being the last practicable date prior to publication of this document).

Name	*Registered office*	*Principal activity*	*Approximate proportion of capital held (%)*
Northumbrian Services Limited (formerly Ondeo Services UK plc)	Northumbria House Abbey Road Pity Me Durham DH1 5FJ	Holding company	100
Northumbrian Water Limited	Northumbria House Abbey Road Pity Me Durham DH1 5FJ	Water and sewerage undertaker, regulated by the Water Industry Act 1991	100
Lyonnaise Des Eaux (Gibraltar) Limited	31 Cannon Lane Gibraltar	Water and sewerage undertaker	66.67
Caledonian Environmental Services plc	c/o CELTS Ltd Elm Park Methilhaven Road Methil Levin Fife KY8 3WA	Water and sewerage treatment	75
Entec UK Limited	Northumbria House Regent Centre Gosforth Newcastle Upon Tyne NE3 3PX	Provision of environmental and engineering consultancy	100

Name	*Registered office*	*Principal activity*	*Approximate proportion of capital held (%)*
Analytical & Environmental Services Limited	Northumbria House Abbey Road Pity Me Durham DH1 5FJ	Provision of analytical, laboratory and scientific services	100
Ayr Environmental Services Limited	Meadowhead Wastewater Treatment, Works & Sewage Treatment Centre, Meadowhead Road, Irvine, Ayrshire KA11 5AY	Water and sewerage treatment	50
Northumbrian Water Technical Centre Limited (formerly "Northumbrian Lyonnaise Technology and Research Centre Limited")	Northumbria House Abbey Road Pity Me Durham DH1 5FJ	Technical assistance, research and development	100
Fastflow Pipeline Services Limited	Northumbria House Abbey Road Pity Me Durham DH1 5FJ	Provision of infrastructure replacement and rehabilitation	100
Northumbrian Water Finance plc	Northumbria House Abbey Road Pity Me Durham DH1 5FJ	Holding of finance instruments	99.99

4.3 Save as set out below there have been no material changes in the issued share capital of any of the subsidiary undertakings of the Company in the three years preceding the date of this document.

The ordinary issued share capital of Essex and Suffolk Water Limited was increased on 28 April 2003 from a total of 10,459,185 £1 ordinary A and B shares to a total of 52,295,925 £1 ordinary A and B shares, by the issue of 41,836,740 £1 ordinary B shares as free bonus shares *pro rata* to all shareholders at a rate of four bonus shares for every A and B share held, by the capitalisation of historical reserves which were no longer necessary. The issued share capital was then reduced on 30 June 2003 to a total of 13,750,000 issued £1 ordinary A and B shares by a re-purchase of shares from capital.

5. Memorandum and Articles of Association

5.1 The memorandum of association of the Company provides that its principal object is to carry on business as a holding company. The objects of the Company are fully set out in clause 4 of its memorandum of association which is available for inspection at the address specified in paragraph 19 below.

5.2 The Articles were adopted by the Company pursuant to a written resolution of the Company on 16 May 2003. The effect of certain of their provisions, certain related contractual provisions and relevant English law is summarised below:

(A) *Voting*

Subject to any special terms as to voting upon which shares may be issued or may for the time being be held, and any restrictions on voting referred to under the heading

"Restrictions on Voting" in paragraph 5.2(B) below, on a show of hands every Shareholder who is present in person at a general meeting of the Company (which includes a person present as the duly authorised representative of a corporate member acting in that capacity) shall have one vote and on a poll every Shareholder who is present in person or by proxy has one vote for every Ordinary Share held by him.

(B) *Restrictions on Voting*

The Board may preclude a Shareholder from attending or voting at any general meeting of the Company or at any separate meeting of the holders of any class of shares of the Company or from exercising any other right in relation to any meeting of the Company or any class of Shareholders, if such Shareholder or other person appearing to be interested or to have been interested in the shares held by such member fails to comply with a notice served under the Act requiring the disclosure of information concerning the interests in the shares concerned within 14 days following the date of service or deemed service of such notice.

(C) *Dividends*

No dividends shall be payable otherwise than out of profits available for that purpose under the provisions of the Act.

The Company may by ordinary resolution declare dividends not exceeding an amount recommended by the Board.

The Board may, in so far as, in its opinion, the profits of the Company justify such payments, pay interim dividends from time to time of such amounts and on such dates and in respect of such periods as it thinks fit.

The Board may, in respect of any dividend declared or paid on or before the date of the fifth annual general meeting of the Company after the date of the adoption of the Articles, and thereafter with the sanction of an ordinary resolution of the Company, offer Shareholders the right to receive shares, credited as fully paid in whole or in part by way of scrip dividend instead of cash. The Board has a wide discretion to decide the terms on which such offer shall be made.

The Board may withhold dividends payable on shares representing not less than 0.25 per cent. by number of the issued shares of any class after there has been a failure to comply with any notice requiring the disclosure of information relating to interests in the shares concerned as referred to in paragraph 5.2(B) above.

Any dividend unclaimed after a period of 12 years after such dividend became payable shall be forfeited and revert to the Company.

(D) *Return of Capital*

On a liquidation of the Company, the Shareholders are entitled pari passu amongst themselves, in proportion to the number of Ordinary Shares held by them and to the amounts paid up or credited as paid up thereon, to share in the whole of any surplus assets of the Company remaining after the discharge of its liabilities.

A liquidator of the Company may, with the authority of an extraordinary resolution and subject to any provision sanctioned in accordance with the Act, divide amongst the Shareholders in specie or in kind the whole or any part of the assets of the Company (whether they shall consist of property of the same kind or not) and may, for such purpose, set such values as he deems fair upon any assets to be divided and may determine how such division shall be carried out for the Shareholders or for different classes of Shareholders.

(E) *Variation of Rights*

Whether or not the Company is being wound up, the rights attaching to any class of shares for the time being in issue may, subject to the provisions of the Act, be varied or abrogated with the consent in writing of the holders of not less than three-quarters in nominal value of the issued shares of that class or with the sanction of an extraordinary resolution passed at a separate general meeting of the holders of the shares of the class.

(F) *Transfer of Shares*

The Shares are registered and may be held in certificated or uncertificated form. The Articles provide for shares to be held in CREST accounts, or through another system for holding shares in uncertificated form, such shares being referred to in the Articles as "Uncertificated Shares". Subject to such of the restrictions in the Articles as may be applicable, any Shareholder may transfer all or any of his shares. In the case of shares represented by a certificate ("Certificated Shares") the transfer must be made by an instrument of transfer in the usual common form or in any other form which the Board may approve. A transfer of an Uncertificated Share need not be in writing, but shall comply with such rules as the Board shall make in relation to the transfer of such shares, a CREST transfer being acceptable under the current rules.

The instrument of transfer of a Certificated Share must be signed by or on behalf of the transferor and (in the case of a partly paid share) the transferee, and the transferor is deemed to remain the holder of the share until the name of the transferee is entered in the register.

The Board may, in its absolute discretion and without giving any reason, decline to register any transfer of a share which is not fully paid up or on which the Company has a lien, but such discretion may not be exercised to prevent dealings in listed shares from taking place on an open and proper basis.

The Board may also refuse to register a transfer unless:

(1) in the case of a Certificated Share, the duly stamped instrument of transfer is lodged with the registrars for the time being of the Company accompanied by the relevant share certificate and such other evidence of the right to transfer as the Board may reasonably require;

(2) in the case of a Certificated Share, the instrument of transfer is in respect of only one class of share; and

(3) in the case of a transfer to joint holders of a Certificated or an Uncertificated Share, the transfer is in favour of not more than four such transferees.

In the case of Uncertificated Shares, the Board may refuse to register a transfer if the Uncertificated Securities Regulations 1995 allow it to do so, and must do so where such regulations so require.

The Board may also decline to register a transfer of shares if they represent at least 0.25 per cent. in number of their class and there has been a failure to comply with a notice requiring disclosure of interests in the shares (as referred to in paragraph 5.2(B) above under the heading "Restrictions on Voting"). Such refusal may continue until the failure has been remedied, but the Board may not decline to register:

(a) a transfer of shares to any bona fide unconnected third party; and

(b) a transfer made pursuant to the provisions of the Act concerning powers of compulsory purchase in respect of a takeover offer as defined in the Articles.

No transfer of any share shall be made to a bankrupt or a person who is mentally disordered or a patient for the purpose of any statute relating to mental health.

(G) *Alterations of Capital*

The Company may by ordinary resolution increase its share capital, consolidate and sub-divide its shares or cancel any shares which have not been taken or agreed to be taken by any person.

The Company may by ordinary resolution, subject to the provisions of the Act, direct that any new shares shall be offered in the first instance to all the holders for the time being of shares of any class or classes in proportion to the number of such shares held by them respectively or may make any other provision as to the issue of the new shares.

The Company may by special resolution, subject to any consent or confirmation required by law, reduce its authorised and issued share capital, any capital redemption reserve, any share premium account or other undistributable reserve in any manner.

(H) *Non-UK Shareholders*

Unless the Directors expressly resolve otherwise, Shareholders with addresses outside the United Kingdom are not entitled to receive notices from the Company unless they have given the Company an address within the United Kingdom at which such notices may be served.

(I) *Purchase of Own Shares*

Subject to the provisions of the Act, the Articles and to any confirmation or consent required by law, the Company may purchase its own shares (including any redeemable shares) provided that if there are in issue any convertible shares of the Company then no purchase by the Company of any of its own shares shall take place unless it has been sanctioned by an extraordinary resolution passed at a separate general meeting of the holders of each class of convertible shares or the terms of issue of such convertible shares include provisions permitting the Company to purchase such shares.

(J) *Untraced Shareholders*

Subject to various notice requirements, the Company may sell any Ordinary Shares of a Shareholder if, during a period of 12 years, at least three cash dividends on such shares have become payable and all cheques or warrants for amounts payable to such Shareholder in respect of his shares have remained uncashed and the Company has received no communication from such Shareholder.

(K) *Borrowing Powers*

The Board may exercise all the powers of the Company to borrow money and to mortgage or charge all or any of its undertaking, property and assets (present and future) and uncalled capital and to issue debentures and other securities, whether outright or as collateral security for any debt, liability or obligation of the Company or any third party. Such borrowing powers may only be varied by an amendment to the Articles approved by a special resolution of the Shareholders as required by the Act.

(L) *Directors*

(1) *Number and Appointment of Directors*

Unless otherwise determined by ordinary resolution of the Company, the Directors shall not be less than two and not more than 15 in number.

Lyonnaise Europe shall be entitled to appoint two persons as non-executive Directors and to remove from office any person so appointed and appoint another person in that person's place.

(2) *Rotation and Age of Directors*

At every annual general meeting, all Directors who then have held office for three years or more since their appointment or re-appointment must retire from office, but shall be eligible for re-appointment. However, if these Directors, together with any other Directors voluntarily retiring at the meeting, represent less than a third of the Directors, additional Directors must then retire to bring the number retiring up to one third of the Directors, those retiring being the Directors who have been longest in office.

There is no age limit for the appointment or retirement of a Director, and it is not necessary to give special notice of any resolution appointing or approving the appointment of a Director by reason only of his age.

(3) *Remuneration of Directors*

The basic level of remuneration of Directors for their services as such (being those fees received in relation to their role as Directors of the Company and excluding remuneration received as a holder of any employment or executive office in the Group) is determined by the Board, but must not exceed in aggregate the sum of £500,000 per annum or such greater sum as the Company may approve by ordinary resolution.

Any Director who is the holder of any employment or executive office is entitled to such remuneration (whether by way of salary, commission, participation in profits or otherwise) as the Board may determine and either in addition to or in lieu of his remuneration as a Director.

Any Director who, by request, goes or resides abroad for any purposes of the Company or who performs services which, in the opinion of the Board, go beyond the ordinary duties of a Director, may be paid such extra remuneration (whether by way of salary, commission, participation in profits or otherwise) or may receive such other benefits as the Board may determine.

Each Director is entitled to be paid his reasonable travelling, hotel and incidental expenses of attending and returning from meetings of the Board or meetings of Shareholders and to be paid all expenses properly and reasonably incurred by him in the conduct of the Company's business or on the discharge of his duties as a Director.

(4) *Pensions and Allowances*

The Board may on behalf of the Company exercise all the powers of the Company to grant pensions, annuities, gratuities, superannuation or other allowances and benefits in favour of any person, including any Director or former Director, or the relations or dependants of any Director or former Director.

Unless the Articles otherwise permit, no benefits may be granted to or in respect of a Director or former Director who has not been employed by, or held an executive or other office or place of profit under the Company or any of its present or former subsidiary undertakings or any predecessor in business of the Company or any such subsidiary undertaking, without the approval of an ordinary resolution of the Company.

(5) *Restrictions on Voting*

Save as set out below, a Director may not vote (or be counted in the quorum) on any resolution of the Board in respect of any transaction in which he has an interest which to his knowledge is a material interest, and if he does so his vote shall not be counted. Subject to the provisions of the Act, and in the absence of some other material interest, this prohibition does not apply to a Director in relation to:

(a) the giving to him of any guarantee, security or indemnity in respect of money lent by him or obligations undertaken by him for the benefit of the Company or any of its subsidiary undertakings;

(b) the giving by the Company or any of its subsidiary undertakings of any guarantee, security or indemnity to a third party in respect of a debt or obligation of the Company or any of its subsidiary undertakings in respect of which he himself has given an indemnity or which he has guaranteed or secured in whole or in part;

(c) any transaction involving the subscription by him of debentures or other securities of the Company or any of its subsidiaries issued or to be issued pursuant to any offer or invitation to the Shareholders or debenture holders of the Company or any class thereof or his underwriting or sub-underwriting of the same;

(d) any transaction in which he is interested by virtue of his interest in shares, debentures or other securities of the Company or by reason of any interest in or through the Company;

(e) any transaction concerning any other company (not being a company in which he owns one per cent. or more of the equity shares or voting rights) in which he is interested, directly or indirectly, whether as an officer, shareholder, creditor or otherwise howsoever;

(f) any transaction concerning the adoption, modification or operation of a superannuation fund or retirement, death or disability benefits scheme that relates both to directors and employees of the Company or of any of its subsidiaries and that does not accord to him any privilege or advantage not generally accorded to employees;

(g) any transaction concerning any insurance which the Company is empowered to purchase and/or maintain for the benefit of the Directors, being insurance against any liability incurred by them in the course of their duties;

(h) any arrangement for the benefit of employees of the Company or any of its subsidiaries under which he benefits in a similar manner to the employees and which does not accord to him any privilege or advantage not generally accorded to the employees to whom such arrangement relates (including, without limitation, any savings related share option scheme or profit sharing scheme approved by the Inland Revenue); and

(i) (save in relation to any matter concerning or directly affecting his own participation therein) the adoption or modification of any executive share option scheme and approved by the Inland Revenue.

(M) *Entitlement to Profits*

The Shareholders are entitled to such profits as are paid as dividends.

6. Directors and Company Secretary

6.1 The full names, business addresses and functions of the Directors and Company Secretary, including the Chairman, are as follows:

Name	*Business Address*	*Function*
Sir Frederick George Thomas Holliday	Northumbria House Abbey Road, Pity Me, Durham DH1 5FJ	Chairman
John Arthur Cuthbert	Northumbria House Abbey Road, Pity Me, Durham DH1 5FJ	Managing Director
Christopher Michael Green	Northumbria House Abbey Road, Pity Me, Durham DH1 5FJ	Finance Director
Sir Austen Patrick Brown	Northumbria House Abbey Road, Pity Me, Durham DH1 5FJ	Non-Executive

Name	*Business Address*	*Function*
Martin André Bernard Nègre	Northumbria House Abbey Road, Pity Me, Durham DH1 5FJ	Non-Executive
Alain Chaigneau	Northumbria House Abbey Road, Pity Me, Durham DH1 5FJ	Non-Executive
Jacques Francis Pétry	Northumbria House Abbey Road, Pity Me, Durham DH1 5FJ	Non-Executive
Martin Parker	Northumbria House Abbey Road, Pity Me, Durham DH1 5FJ	Company Secretary

6.2 The current directorships and partnerships of the Directors and the Company Secretary and the directorships and partnerships held by them over the previous five years are as follows:

Directors and Company Secretary

Name	*Directorship and Partnership*
Sir Fred Holliday	*Current* Northumbrian Water Group plc Northern Venture Trust plc Northern 2 VCT plc Brewin Dolphin Holdings plc – Chairman Northumbrian Holdings Limited – Chairman Northumbrian Water Limited – Chairman Northumbrian Services Limited – Chairman *Previous* Suez S.A. Shell UK Limited Wise Speke Group plc The British Trust for Ornithology The Go-Ahead Group plc The Freshwater Biological Association Lyonnaise Europe plc
John Cuthbert	*Current* Northumbrian Water Group plc Northern Business Forum Limited Water UK Econoliner Limited EL Water Management Services Limited Essex and Suffolk Water Limited Fastflow Pipeline Services Limited North East Water Limited (in members' voluntary liquidation, for further details see paragraph 6.6(A) of Part 7 of this document) Northumbrian Holdings Limited Northumbrian Water Pension Trustees Limited Northumbrian Water Limited Northumbrian Water Finance plc Northumbrian Overseas Investments Limited Northumbrian Services Limited Atlantic Water Limited The Water Companie's Association (dissolved, for further details see paragraph 6.6(B) of Part 7 of this document) The Water Services Association of England and Wales (dissolved, for further details see paragraph 6.6(C) of Part 7 of this document)

John Cuthbert	*Previous* Eurowater Limited IMASS Limited Northumbrian Water Technical Centre Limited Lyonnaise Europe plc Lyonnaise UK Water Services Limited Water Services Limited United Water UK Limited WTI Water and Sanitation Services South Africa (Pty) Limited Johannesburg Water Management (Pty) Limited
Chris Green	*Current* Analytical & Environmental Services Limited Coquetdale Property Investment Limited El Water Management Services Limited Entec Gould Group Limited Essex and Suffolk Water Limited Fastflow Pipeline Services Limited Fisheries Development Limited International Training Consortium Limited Jayhold Limited Northumbrian Water Group plc Northumbrian Water Technical Centre Limited North East Water Limited (in members' voluntary liquidation, for further details see paragraph 6.6(A) of Part 7 of this document) Northumbrian Water Pension Trustees Limited Northumbrian Water Limited Northumbrian Water Finance plc Northumbrian International Holdings Limited Northumbrian Water Projects Limited Northumbrian Overseas Investments Limited Northumbrian Water Mexico Limited Northumbrian Water Services Limited Northumbrian Services Limited St Mary's Court Leasing Limited Suffolk Water Limited ULG Northumbrian Limited Atlantic Water Limited *Previous* United Water UK Limited Vehicle Lease and Service Limited Accessace Limited Binn Landfill (Glenfarg) Limited Cleveland Waste Management Limited Cotsmead Limited CPCR Limited Enviricare Limited Epic Products Limited IMASS Limited Montec International Limited Northumbrian Environmental Management Limited Northumberland Waste Management Limited Northumbrian Water Services Limited Northumbrian Water Share Scheme Trustees (Guernsey Limited) Tyne Waste Limited United Water UK Limited Sita Holdings UK Limited

Sir Patrick Brown	*Current* Arlington Pension Scheme Trustees Limited Arlington Securities Limited CAF Nominees Limited Mobility Choice (a charity) Mobility Roadshow Limited Northumbrian Water Group plc The Go-Ahead Group plc *Previous* Articlift Limited Dartford River Crossing Limited HC Airlines Limited Heavylift Aircraft Engineering Limited Heavylift Aviation Holdings Limited (in administrative receivership) Hunting plc MacQuarrie Infrastructure (UK) Limited Marinet Systems Limited Midland Expressway Limited Trans-World Leasing Limited
Martin Nègre	*Current* Ecofin Water & Power Opportunities plc Bolux SICAV Luxembourg Dynaction S.A. Northumbrian Water Group plc *Previous* Northumbrian Water Limited Australian Water Services Water Services of South Africa New Zealand Water Services Lyonnaise des Eaux (Gibraltar) Limited SITA Holdings UK Limited SITA S.A. Electricite de Tahiti Electricite et Eaux de Caledonie Maynilad Water Services, Philippines Lyonnaise South East Asia, Malaysia Palyja, Indonesia Compania Electricitade de Macau SAAM, Macau Sino French Holdings Ltd, Hong Kong Northumbrian Services Limited Northumbrian Water Pension Trustees Limited Northumbrian Water Technical Centre Limited Northumbrian Water Projects Limited Lyonnaise Europe plc Northumbrian Holdings Limited Chambre de Commerce Francaise de Grande – Bretagne Limited
Alain Chaigneau	*Current* Lyonnaise Europe plc Lyonnaise des Eaux France S.A.

Alain Chaigneau	*Current (continued)* Northumbrian Water Group plc Ondeo Degremont S.A. Aguas Argentinas S.A. Inversiones Aguas Metropolitanas S.A. Ondeo North America Inc. Ondeo Services Chile S.A. United Water Resources Inc. Aguas Andinas S.A. *Previous* Northumbrian Water Limited Northumbrian Services Limited OIS Corporate S.A. Generale de Banque S.A. Tractebel S.A. Union Miniere S.A. Recticel S.A. Genfina S.A. Frabepar S.A.
Jacques Pétry	*Current* Northumbrian Water Group plc Lyonnaise Europe plc Northumbrian Water Limited Ondeo S.A. Suez Environnement S.A. Ondeo Degremont S.A. Societe des Eaux de Marseille S.A. OIS Corporate S.A. Aguas de Barcelona Ondeo Nalco Inc. United Water Resources Inc. Ondeo de Puerto Rico Inc. Sita Netherlands B.V. *Previous* Sita S.A. Watco S.A. Teris LLC Sita France S.A. Scori S.A. Sita FD S.A. Novergie S.A. Cespa Sita Deutschland GmbH Eloyo S.A. Entrepose S.A. El Water Management Services Limited Essex and Suffolk Water Limited Northumbrian Environmental Management Limited Northumbrian Services Limited Sita Holdings UK Limited Sita UK Limited

Martin Parker	*Current* Conserva Limited Cremer & Warner Limited C&W Limited Essex and Suffolk Water Limited Gould Rural Environment Limited Hydrotechnical Limited Hydrotechnical Services (International) Limited Neil Bunting & Associates Limited Newcastle and Gateshead Water Limited Northumbrian Water Pension Trustees Limited Northumbrian Water Environmental Trust Limited Northumbrian International Holdings Limited Northumbrian Water Estates Limited Northumbrian Water Mexico Limited Northumbrian Water Share Scheme Trustees Limited Amtec Bunting Limited Renovexx Technology Limited Rural Building Consultants Aquus Water Services Limited Suffolk Water Limited Wallace Whittle & Partners Limited Water Industry Solutions Limited Waterco Four Limited Waterco Nine Limited Waterco One Limited Waterco Six Limited *Previous* Eurowater Limited Lyonnaise UK Water Services Limited Sunderland & South Shields Water (Trustee) Company Limited Water Services Limited Waterco Two Limited

6.3 Save as set out in paragraph 6.2 above none of the Directors nor the Company Secretary has any business interests nor performs any activities outside the Group which are significant with respect to the Group.

6.4 None of the Directors nor the Company Secretary has: (a) any unspent convictions in relation to indictable offences; or (b) has been the subject of any public criticisms by statutory or regulatory authorities (including designated professional bodies) or has been disqualified by a court from acting as a director of, or from acting in the management or conduct of the affairs of, any company.

6.5 Save as set out below in paragraph 6.6 none of the Directors nor the Company Secretary has been: (a) a director of a company with an executive function at the time of or within the 12 months preceding the commencement of a receivership, compulsory liquidation, creditors' voluntary liquidation, administration, company voluntary arrangement or a composition or arrangement with creditors of that company generally or any class of its creditors of any company or (b) a partner of a partnership at the time of, or within the 12 months preceding any compulsory liquidation, administration or partnership voluntary arrangement of that partnership.

6.6 (A) John Cuthbert and Chris Green are directors of NEW. A statutory declaration of solvency was passed by all directors of NEW on 25 July 2003. The extraordinary general meeting to resolve to wind up NEW and appoint the liquidator was held on 30 July 2003. Both resolutions were passed unanimously by the shareholders present, who represented more than 99 per cent. of the share capital. As NEW had not traded since 1996 an early distribution of shareholder funds was possible, and took place on 11 August 2003.

(B) John Cuthbert was a director of The Water Companie's Association Limited (the "WCA"), a private company limited by guarantee with no share capital, from 7 July 1993 to 13 May 1999; executive duties never formed part of his role as a director. WCA was dissolved on 16 November 1999 and had no outstanding charges.

(C) John Cuthbert was appointed to The Water Services Association of England and Wales (the "WSA"), a private company limited by guarantee with no share capital, as a director on 19 December 2000; executive duties never formed part of his role as a director. WSA was dissolved on 2 October 2001 and had no outstanding charges.

6.7 None of the Directors nor the Company Secretary is or has been bankrupt or has made an individual voluntary arrangement with his creditors, or suffered the appointment of a receiver over any of his assets.

7. Directors and Other Interests

7.1 Save as set out below, none of the Directors nor any of their immediate families (as at 16 September 2003, being the latest practicable date prior to publication of this document) have interests in the shares or debentures of the Company or any member of the Group: (a) which are required to be notified by each Director pursuant to section 324 or 328 of the Act; (b) which are required, pursuant to section 325 of the Act, to be entered in the Register of Directors' interests maintained under section 325 of the Act, or which are interests of a connected person of a Director which would, if the connected person were a Director, be required to be disclosed under (a) or (b) above, and the existence of which is known to or could, with reasonable diligence, be ascertained by that Director:

(A) Martin Nègre is the chairman of and a shareholder in Ecofin Water & Power Opportunities plc and a director of and a shareholder in Bolux SICAV Luxembourg both of which are Shareholders and also owns 30,000 Ordinary Shares;

(B) Sir Fred Holliday holds 8,700 Ordinary Shares;

(C) John Cuthbert holds 80,000 Ordinary Shares;

(D) Geraldine Green (Chris Green's wife) holds 25,000 Ordinary Shares;

(E) Sir Patrick Brown holds 43,000 Ordinary Shares;

(F) Geraldine Green (Chris Green's wife) holds £25,000 in aggregate principal amount of the NSL 2006 Bonds; and

(G) John Cuthbert holds £40,000 in aggregate principal amount of the NSL 2006 Bonds.

For details of the proposed share incentive schemes please see paragraph 9 of Part 7 of this document.

7.2 The Directors do not hold any options to subscribe for or to purchase Ordinary Shares.

7.3 As far as is known to the Company, the Directors are not aware of any persons who directly or indirectly, jointly or severally, exercise or could exercise control over the Company at the date of this document.

7.4 As far as is known to the Company as at 16 September 2003 (being the latest practicable date prior to the publication of this document) the following persons are interested, directly or indirectly, in three per cent. or more of the ordinary share capital of the Company:

Name	No. of Ordinary Shares held at the date of this document	Percentage of Ordinary Shares held at the date of this document
HSBC Global Custody Nominee (UK) Limited 739311 ACCT	129,655,961	25.00
Vidacos Nominees Limited	91,234,432	17.59
Deutsche Bank Aktiengesellschaft London PROP001 ACCT	34,674,255	6.68
BNY (OCS) Nominees Limited	29,181,531	5.62
Morstan Nominees Limited	24,550,000	4.73

7.5 No Director has or has had any interest in any transaction which is or was unusual in its nature or conditions or significant to the Business and which was effected by the Company (i) during the current or immediately preceding financial year or, (ii) during an earlier financial year and remains in any respect outstanding and unperformed.

7.6 There are no loans or guarantees granted or provided by any member of the Group to or for the benefit of any of the Directors which are now outstanding.

8. Directors' Service Agreements and Remuneration

8.1 The following Directors entered into service agreements, the main terms of which are described below, with the Company, dated 22 May 2003, and their employment with the Company began on 23 May 2003. However, it should be noted that each of John Cuthbert and Chris Green have been employed by a company within the Group since a date prior to 23 May 2003. John Cuthbert commenced employment at NEW on 2 January 1991 and Chris Green commenced employment at Northumbrian Holdings Limited (at the time called Northumbrian Water Group plc) on 22 January 1990.

Director	*Details*
John Cuthbert	John is entitled to receive an annual salary of £221,500 and a performance bonus of up to £88,600 per annum. Company benefits include executive pension arrangement (see paragraph 10.2 below for further details), private health care, medical screening, accident insurance, permanent health insurance and long term incentive plans and/or share option arrangements for executives. In addition, John participates in the employee car ownership scheme which is partly funded by the Company (to the net amount of £5,244 per annum). This continuing contract is subject to termination by either 12 months' written notice given by the Company or by John, or the contract being terminated due to dishonest behaviour, serious or persistent misconduct, by a failure to carry out duties or gross negligence, a breach of the employment contract, becoming bankrupt or being found guilty of a criminal offence or being disqualified from holding the office of director. As an alternative to serving notice of termination the Company may at its absolute discretion, terminate the service agreement without prior notice and make a payment in lieu of the basic salary (but not the other benefits) to which John would have been entitled during his notice period. Normal retirement is at 65 years of age. John will not without the prior written consent of the Company directly or indirectly be engaged or interested in any capacity (whether executive, non-executive, as a consultant or on any other basis) in any other business, trade, occupation or activity whatsoever, although John, his

spouse and his children under 18 years of age may hold or acquire (by way of a bona fide investment only) up to one per cent. of any class of securities in a company whose shares are dealt in on a recognised stock exchange or the unlisted securities market or in any other company whose business does not compete with any business carried on by any member of the Group.

If the Company consents to John becoming involved in any other business, trade, occupation or activity he will pay to the Company all salary and other remuneration together with the cash value of any benefits in kind which he receives.

John will not (and will ensure, so far as he is able, that his wife and children under 18 years of age will not) deal or become or cease to be interested in any securities of the Company or of any Group company except in accordance with the Company's code of practice for the time being in relation to such transactions.

Chris Green

Chris is entitled to receive an annual salary of £146,500 and a performance bonus of up to £58,600 per annum. Company benefits include executive pension arrangement (see paragraph 10.2 below for further details), private health care, medical screening, accident insurance, permanent health insurance and long term incentive plans and/or share option arrangements for executives. In addition, Chris participates in the employee car ownership scheme which is partly funded by the Company (to the net amount of £3,756 per annum).

This continuing contract is subject to termination by either 12 months' written notice given by the Company or by Chris, or the contract being terminated due to dishonest behaviour, serious or persistent misconduct, by a failure to carry out duties or gross negligence, a breach of the employment contract, becoming bankrupt or being found guilty of a criminal offence or being disqualified from holding the office of director. As an alternative to serving notice of termination the Company may at its absolute discretion terminate the service agreement without prior notice and make a payment in lieu of the basic salary (but not the other benefits) to which Chris would have been entitled during his notice period.

Normal retirement is at 65 years of age.

Chris will not without the prior written consent of the Company directly or indirectly be engaged or interested in any capacity (whether executive, non-executive, as a consultant or on any other basis) in any other business, trade, occupation or activity whatsoever, although Chris, his spouse and his children under 18 years of age may hold or acquire (by way of a bona fide investment only) up to one per cent. of any class of securities in a company whose shares are dealt in on a recognised stock exchange or the unlisted securities market or in any other company whose business does not compete with any business carried on by any member of the Group.

If the Company consents to Chris becoming involved in any other business, trade, occupation or activity he will pay to the Company all salary and other remuneration together with the cash value of any benefits in kind which he receives.

Chris will not (and will ensure, so far as he is able, that his wife and children under 18 years of age will not) deal or become or cease to be interested in any securities of the Company or of any member of the Group except in accordance with the Company's code of practice for the time being in relation to such transactions.

8.2 There are no commission or profit sharing arrangements with Directors other than as referred to in paragraph 8.1 above, and the share incentive schemes, particulars of which appear in paragraph 9 below, in which the Directors are entitled to participate.

8.3 Other than Sir Fred Holliday, the non-executive Chairman, who is entitled to receive an annual fee of £125,000, each of the other non-executive Directors are entitled to receive an annual fee of £30,000.

8.4 Save as disclosed above in paragraphs 8.1 and 8.3, there are no service contracts between any of the Directors and the Company or any member of the Group.

8.5 There is no arrangement under which any Director has agreed to waive future emoluments, and there were no waivers of Directors' emoluments during the year ended 31 December 2002.

8.6 The total aggregate remuneration paid and benefits in kind granted to the Directors by any member of the Group in respect of the financial year ended 31 December 2002 was £506,465, made up as follows:

	£
Executive Directors' salaries	285,000
Fees paid to Non-Executive Directors	85,000
Bonus payments accrued	85,500
Other emoluments, including benefits in kind	50,965

8.7 The aggregate remuneration of the Directors (including proposed directors) that has or will be payable by the Company or any member of the Group in respect of the current financial year (being the 15 month period from 1 January 2003 to 31 March 2004) under the arrangements currently in force is estimated to be £893,645, made up as follows:

	£
Executive Directors' salaries	441,223
Fees paid to Non-Executive Directors	243,274
Bonus payments	134,400
Other emoluments, including benefits in kind	74,748

9. Share Incentive Schemes

9.1 Employees (including executive directors) of the Group were, prior to the Atlantic Acquisition, eligible to participate in share incentive schemes operated by Suez. Although on such acquisition employees were entitled to retain their awards under the various share incentive schemes, they are no longer eligible for the grant of future awards under those schemes.

9.2 The Company is proposing to establish two new share incentive schemes: the Northumbrian Water SIP – a share incentive plan, under which all employees would be eligible to benefit, and the Northumbrian Water LTIP – a long term incentive plan under which it is intended that senior management only would benefit. Shareholder approval for the establishment of the plans will first be sought at an Extraordinary General Meeting of the Company. However, the Company has not fully finalised the terms of the plans and, therefore, details of the features of the plans will be given to Shareholders in the notice of the Extraordinary General Meeting at which their approval is sought.

10. Pension Schemes

10.1 The Final Salary Scheme provides defined (final salary) benefits. In addition to the Company, the following members of the Group are eligible to participate in the Final Salary Scheme: NSL, NWL, Entec UK Limited, Analytical & Environmental Services Limited, Vehicle Lease and Service Limited, Fastflow Pipeline Services Limited, Northumbrian Water Technical Centre Limited, Coquetdale Property Investment Limited, and ULG Northumbrian Limited. In addition to these companies, two former members of the Group

(SITA Holdings UK Limited and Imass Limited) continue to participate in the Final Salary Scheme pursuant to interim participation terms agreed on the sale of those companies. The Final Salary Scheme is an Inland Revenue approved arrangement and is contracted-out of the State Second Pension (prior to April 2002, the State Earnings Related Pension Scheme or SERPS).

10.2 The Final Salary Scheme is divided into the following sections: the Lyonnaise UK Scheme Section (which is further sub-divided into the "Northern" and the "Southern" sub-sections), the Water Pension Scheme (or WPS) Section and the Mirror Image Scheme (or MIS) Section. Employees contribute between three and six per cent. of pensionable salaries, depending on which section they are members of. Different sections have different accrual rates for benefits (between 1/90th and 1/60th), depending on the rate of employee contributions. The Final Salary Scheme also provides lump sum death in service benefits of four times pensionable salary and dependants' pensions. Certain Directors and senior employees are eligible to receive enhanced benefits under the Final Salary Scheme (this is known as the "Executive Pension Arrangement" or "EPA"). There is an unfunded unapproved retirement benefit arrangement in place for John Cuthbert which, broadly, provides benefits that would have been payable under the Final Salary Scheme if John Cuthbert had not been subject to the earnings cap.

10.3 The most recent actuarial valuation of the Final Salary Scheme was carried out as at 31 December 2001. On an ongoing basis, the value of the Final Salary Scheme's assets at this valuation was a little over £440 million, with the liabilities of the scheme amounting to just under £404 million. The Southern sub-section of the Final Salary Scheme was in surplus by approximately £41 million, with the Northern sub-section in surplus by approximately £6 million and WPS Section showing a deficit of just under £10 million.

The MIS Section was not included in this actuarial valuation, as it was created following a bulk transfer of benefits from the Water Mirror Image Pension Scheme after 31 December 2001. The transfer payment into the MIS Section was approximately £20 million.

The trustees of the Final Salary Scheme have received actuarial advice that, if the results of this actuarial valuation were projected forward to 30 June 2003, using the 31 December 2001 assumptions, the Final Salary Scheme had an overall deficit on an ongoing basis as at that date of approximately £36 million. However, the trustees of the scheme have received further actuarial advice that, were the valuation to be carried out using the assumptions appropriate to the market conditions as at 30 June 2003, the fund would have had an overall deficit as at that date of approximately £81 million.

NWL submitted its Draft Business Plan to Ofwat in August 2003 which included proposals to increase contribution rates with effect from January 2006, following the acutarial valuation which will be carried out as at 31 December 2004. These proposals will seek to address the deficits over the remaining life of the relevant employees. NWL will reassess its proposals before submitting its Final Business Plan in April 2004.

10.4 Participating employers currently pay contributions to the Northern sub-section at 10.5 per cent. of pensionable salaries and nil for the Southern sub-section, to the WPS Section at 15.5 per cent. of pensionable salaries and to the MIS Section at 21 per cent. and 20.7 per cent. of pensionable salaries (depending on the level of employee contributions).

These contribution rates take account of the surplus in the Final Salary Scheme at 31 December 2001 and the long term cost in the Water Mirror Image Pension Scheme at 31 March 2001 (the last valuation prior to the bulk transfer, at which employer contribution rates to that scheme were set). In addition to these regular contributions, a one-off employer contribution of £15 million was made to the WPS Section in January 2003 in respect of past severance schemes.

10.5 NSL also operates two group personal pension plans, each called the Northumbrian Water Group Personal Pension Plan, one is with Scottish Equitable and the other is with Royal & Sun Alliance (the "NWG PPPs"). Both of the NWG PPPs have been approved by the Inland Revenue. Employees can choose whether or not to contract-out of the State Second Pension through an appropriate personal pension arrangement.

10.6 The NWG PPPs provide defined contribution (money purchase) benefits. In addition to NSL, employees of the following companies are eligible to participate in the NWG PPP with Scottish Equitable: NWL, Entec UK Limited, Analytical & Environmental Services Limited, ULG Northumbrian Limited, Caledonian Environmental Levenmouth Treatment Services Limited and Northumbrian Water Technical Centre Limited.

10.7 Employees are required to contribute a minimum of three per cent. of salary (one per cent. for employees of Entec UK Limited) and employer contributions are payable at a rate of six per cent. of salary. In the event of death in service, the value of an employee's fund is available to provide a lump sum and/or dependants' pensions.

10.8 NSL also operates a stakeholder pension plan, the Northumbrian Water Stakeholder Plan with Clerical Medical. This arrangement is available to employees of the Company and its subsidiaries who are not eligible to join any of the other arrangements and for payment of voluntary contributions for members of the Final Salary Scheme earning less than £30,000 per annum.

10.9 In addition, a lump sum death in service benefit of four times pensionable salary is payable from the Northumbrian Water Group Life Assurance Scheme (insured with Canada Life) in the event of the death of any employee who is not a Final Salary Scheme member.

10.10 Group companies participating in the various pension arrangements incurred pension costs (excluding national insurance contributions for employees who are not contracted out of the State Second Pension) totalling approximately £8.1 million in the year ended 31 December 2002.

10.11 New employees of NWL are eligible to join the Final Salary Scheme. New employees of all other subsidiaries of the Company are entitled to join the NWG PPP provided by Scottish Equitable (although there may be exceptional circumstances where senior employees are, at the discretion of the employing company, offered membership of the Final Salary Scheme).

11. Material Contracts

Other than the contracts, a summary of the principal contents of which are set out below, there are:

(a) no material contracts (which are not in the ordinary course of business) that have been entered into by any member of the Group within the two years immediately preceding the date of publication of this document; and

(b) no other contracts (not being in the ordinary course of business) that have been entered into by any member of the Group which contain any provision under which any member of the Group has an obligation or entitlement which is material to the Group as at the date of this document.

11.1 *Documents relating to the Atlantic Acquisition and AIM Admission*

(A) Share Purchase Agreement

The Company entered into a share purchase agreement on 16 May 2003 (the "SPA") with Lyonnaise Europe and United Water UK Limited (acting as partners of the Northumbrian Partnership), Lyonnaise Europe and Suez Environnement (as "Vendors"), and Suez and Suez Environnement (as "Guarantors") whereby it agreed to acquire the entire issued share capital of Atlantic conditional upon, *inter alia*: (i) the AIM Admission taking place not later than 3 June 2003; and (ii) no material adverse change (and no event occurring which could reasonably be expected to result in an adverse change) in the condition (financial or otherwise), business, assets, operations, properties, performance or prospects of the Atlantic Group from 16 May 2003, having occurred. The consideration for the Atlantic Acquisition was the cash sum of £880 million and the issue of 129,655,961 Ordinary Shares to affiliates of Suez.

Under the SPA:

(1) the Vendors provided standard warranties on a joint and several basis in relation to the shares to be transferred under the SPA and in relation to the business and operations of the Atlantic Group. Certain of these warranties were repeated upon Completion and the time limits for the Company to bring a claim for breach of the warranties (other than the property, environmental and taxation warranties) is 24 months following Completion. In relation to environmental warranties and property warranties, the Company can make a claim within three years and five years respectively from Completion. Claims for breaches of the tax warranties are covered in the Tax Deed (defined in paragraph (C) below). Certain financial limits were placed in relation to warranty claims; the maximum aggregate claim which can be made in respect of claims by the Company for any warranty breaches under the SPA and claims under the Tax Deed (as defined below) is £379 million;

(2) the Vendors undertook not to compete with the non-regulated business of the members of the Group as at the date of the SPA in the United Kingdom, for a period of 24 months following Completion;

(3) the Guarantors agreed to guarantee the obligations of the Vendors arising under the SPA; and

(4) the Company provided limited warranties in relation to its capacity and authority to enter into the SPA, disclosure of information under the Placing Agreement (as defined in paragraph (D) below) and the original Facilities Agreement (as defined in paragraph (E) below) and in relation to certain anti-trust and competition issues.

(B) *Disclosure Letter*

By a disclosure letter dated 16 May 2003 from the Vendors to the Company, the Vendors made general and specific disclosures qualifying the warranties that were given in the SPA and the Placing Agreement. In addition the Vendors and the Company agreed that all documents listed in the indices to the data room set up for the Atlantic Acquisition at 16 May 2003 were fairly disclosed.

(C) *Tax Deed*

The Company entered into a tax deed with the Vendors (the "Tax Deed") on 25 May 2003 which provided a mechanism for the Vendors to indemnify the Company in respect of all pre-Completion tax liabilities of Atlantic and the NSL Group. The Vendors' obligation to indemnify the Company is subject to certain exclusions and limitations, for example if proper provision for the tax liability in question is contained in the audited accounts of NSL for the financial year ended on 31 December 2002.

(D) *Placing Agreement*

The Company entered into the Placing Agreement on 16 May 2003 with, amongst others, Collins Stewart (the "Broker"), Ecofin Limited, Bernard Lambilliotte and Deutsche Bank, whereby the Broker agreed to act as broker to the Company and as its agent to procure placees to subscribe for or purchase the placing shares, failing which the Broker and Deutsche Bank would each subscribe for or purchase one half of such shares themselves.

Under the Placing Agreement:

(1) the Company agreed to pay the Broker a commission of four per cent. of the aggregate value of the placing shares (plus any applicable Value Added Tax);

(2) the Company agreed to pay all other costs and expenses of the Placing and the related arrangements together with value added tax on such costs;

(3) the costs of the Atlantic Acquisition were met from the proceeds of the Placing; and

(4) the Company gave certain representations and warranties to the Broker as to the accuracy of the information in the admission document produced for the AIM Admission and as to other matters relating to the Atlantic Group and its business and an indemnity to the Broker for itself and as trustee for associated companies, directors and employees in respect of certain liabilities arising out of or in connection with the carrying out by the Broker of its obligations in connection with or by reason of the issue and certain indemnities in favour of the Company given to the Company and the Broker in respect of taxation liabilities.

(E) *The Amended and Restated Facilities Agreement*

The Company entered into a facilities agreement on 16 May 2003 (the "Original Facilities Agreement") with Deutsche Bank as the facility agent and the initial lender and Deutsche Trustee Company Limited as the security trustee. The Original Facilities Agreement provided funding for the Atlantic Acquisition. Following the Atlantic Acquisition additional guarantors and borrowers in the Group acceded to the Original Facilities Agreement and provided guarantees and security over their assets in favour of the lenders. In so far as the relevant guarantees and security caused financial assistance in connection with the Atlantic Acquisition, the relevant provisions of the Act or, in relation to Atlantic, the equivalent provisions under Guernsey law were complied with.

On 29 July 2003 the facilities were further syndicated on behalf of the initial lender to a group of new lenders. This syndication was effected by the new lenders and the existing parties to the Original Facilities Agreement entering into an amendment and restatement agreement amending and restating the Original Facilities Agreement (the "Amended and Restated Facilities Agreement"). The Amended and Restated Facilities Agreement reflects the developments which followed on from the accession of the additional obligors, completion of the financial assistance procedure and the restructuring of certain of the facilities.

The Amended and Restated Facilities Agreement consists of secured sterling term and revolving facilities in the following facility tranches:

(1) Facility A is a term loan of £159,000,000 available for a 90 day period from the date of Completion and has been applied by the Company for the payment of the purchase price of the Atlantic shares and related acquisition costs. Facility A is repayable two years after the date of Completion;

(2) Facility B is a term loan of £46,000,000 available for a 90 day period from the date of Completion and has been applied by NWL for payment of a non-regulated dividend. Facility B is repayable two years after the date of Completion;

(3) Facility C is a revolving credit facility of £90,000,000 available for a 23 month period from the date of Completion. It is available to NWL for use towards the general corporate and working capital purposes. Loans under Facility C are repayable on the earlier of the last day of their respective interest periods or otherwise two years after the date of Completion;

(4) Facility D is a revolving loan and bank guarantee facility of £376,000,000. It is available to NWL for a 364 day period from the date of Completion. At the end of this period NWL may apply for an extension of one year, or alternatively may elect to convert the facility into a one year term loan. The facility is intended for the repayment of any EIB loan and the procurement of one or more bank guarantees in respect of all or part of the monetary obligations of NWL under any EIB loan. Subject to the extension and term out options described above, Facility D loans are repayable on the earlier of the last day of their respective interest periods or otherwise on the date falling 364 days after the date of Completion. If the one year extension option is granted the Facility D loans thereunder are repayable on the earlier of the last day of their respective interest periods or otherwise 364 days after the date on which the extension option was exercised. If the term out option is elected the term loan under that option is repayable on the date falling 364 days after the date on which the term out option was exercised. An issued Facility D bank guarantee is immediately repayable by the borrower; and

(5) Facility E is a term bank guarantee facility of £15,000,000. It is available to NSL from the date of Completion until 31 December 2003 for the procurement of bank guarantees on its behalf in favour of approved beneficiaries in respect of the Ayrshire Project and the CES Project. An issued Facility E bank guarantee is immediately repayable by the borrower.

Interest on the facilities are payable at a rate equal to the aggregate of the London Interbank Offered Rate ("LIBOR"), the margin and mandatory costs incurred by the lenders in complying with the regulations of the Bank of England, the European Central Bank and the Financial Services Authority.

All the facilities terminate two years after Completion if not already terminated.

(F) *Relationship Agreement*

In connection with the Atlantic Acquisition, the Company entered into a relationship agreement on 16 May 2003 with Lyonnaise Europe (the "Relationship Agreement") whereby the parties agreed to certain specific matters in relation to the governance of their relationship. These matters included corporate governance of the Company, composition of the Board (including Lyonnaise Europe's right to appoint two non-executive directors) the number of Board meetings to be held annually, matters that are to be reserved to the Shareholders or the Board, Lyonnaise Europe's rights of access to information, co-operation on technical services and equipment matters, and rights in intellectual property developed separately and jointly.

On 17 September 2003, the Company and Lyonnaise Europe entered into a deed of variation in respect of the Relationship Agreement (the "Deed of Variation"), whereby the parties agreed to variation of certain provisions of the Relationship Agreement regarding: (i) the obligation on the Company to appoint independent non-executive directors to the Board, following Admission; (ii) compliance by the Company with its obligations under Chapter 9 of the Listing Rules in particular with reference to disclosure of information required to be notified to the Regulatory Information Service (as defined under the Listing Rules), subject to and with effect from Admission (iii) Lyonnaise Europe's obligations in relation to ensuring that its officers, employers, agents, professional and other advisers ("Connected Persons") who acquire confidential information on the Group are made aware of the existence and application of relevant rules and regulations regarding, *inter alia*, the dissemination of price sensitive information and that other persons to whom Lyonnaise Europe provides confidential information are also made aware of the existence of such rules; and (iv) Lyonnaise Europe's obligations to ensure that where it is required to disclose confidential information on the Group publicly or to any governmental or regulatory body or tax authority, it uses its reasonable endeavours to ensure confidentiality is maintained and/or where public disclosure of the same is envisaged it notifies the Company in advance and uses its reasonable endeavours to ensure that the timing and content of such public disclosure is co-ordinated with any announcement or disclosure of the Company under the Listing Rules, having due regard to the requirements of the UK Listing Authority in connection with Admission.

(G) *Nominated Adviser and Broker Agreement*

The Company entered into a nominated adviser and broker agreement on 20 May 2003 with Collins Stewart (the "Nominated Adviser and Broker Agreement"), whereby the Company appointed Collins Stewart to act as nominated adviser and nominated broker to the Company for the purposes of AIM. The appointment commenced on the date of the Nominated Adviser and Broker Agreement for an initial period of 12 months and continues thereafter subject to three months' notice of termination. The Company agreed to pay Collins Stewart an annual fee of £50,000 for its services under the Nominated Adviser and Broker Agreement. The Nominated Adviser and Broker Agreement contains certain undertakings and indemnities given by the Company in respect of, *inter alia*, compliance with applicable laws and regulations and agreement to provide Collins Stewart with certain information whilst it remains its Nominated Adviser and Broker. This agreement will terminate on Admission.

11.2 *Others*

(A) The Company entered into the Sponsorship Agreement on 18 September 2003 with Collins Stewart under which the Company has agreed to appoint Collins Stewart as sponsor to the Company in connection with Admission. The Sponsorship Agreement provides for the payment of a fee of £200,000 by the Company to Collins Stewart plus its expenses and all other expenses incidental to Admission (in each case plus VAT where applicable). The Sponsorship Agreement also includes certain warranties and indemnities given by the Company to Collins Stewart.

12. Premises

The Group does not have any principal establishments which account for more than ten per cent. of the net turnover or production of the Group. However, the Group has the following main establishments:

Name & address of property	*Freehold or leasehold (and lease expiry date if relevant)*	*Registered at H M Land Registry or unregistered*
Reservoirs		
Abberton Reservoir	Freehold	Registered
Hanningfield Reservoir	Freehold	Registered
Catcleugh Reservoir, Northumberland	Freehold	Unregistered
Kielder Water Reservoir, Northumberland	Freehold	Unregistered
Whittle Dene Reservoir, Northumberland	Part Freehold Various Leasehold parts expiring as to one in 9,700 years and as to another in 2053.	Unregistered
Derwent Reservoir, Northumberland	Part Freehold Various Leasehold parts expiring 2880 or later	Unregistered

Name & address of property	*Freehold or leasehold (and lease expiry date if relevant)*	*Registered at H M Land Registry or unregistered*
Reservoirs		
Fontburn Reservoir and Water Treatment Works	Freehold	Unregistered
Burnhope Reservoir	Freehold	Unregistered
Cowgreen Reservoir, Upper Teesdale Valley	Freehold	Unregistered
Little Swinburn Reservoir	Freehold	Unregistered
Colt Crag	Freehold	Unregistered
Hallington	Freehold	Unregistered
Tosson Springs	Freehold	Unregistered
Water Treatment Works North		
Broken Scar	Freehold	Part Registered
Horsley, Northumberland	Freehold	Unregistered
Lartington	Freehold	Unregistered
Lumley	Freehold	Unregistered
Mosswood	Freehold	Unregistered
Warkworth	Freehold	Unregistered
Gunnerton	Freehold	Registered
Sewage Treatment Works		
Aycliffe	Freehold	Unregistered
Bran Sands	Leasehold Expires January 2021 with option to renew for 25 years, and an option to renew again for 23 years.	Registered
Howdon	Freehold	Registered
Marske	Freehold	Registered
Seaton Carew	Freehold	Registered
Cramlington	Freehold	Unregistered
Washington	Freehold	Part Registered
Cambois Farm	Freehold	Registered
Billingham	Freehold	Unregistered
Newbiggin by the Sea	Freehold	Registered
Seaham	Freehold	Registered
Amble	Leasehold Expires September 2197	Registered
Blyth	Freehold	Unregistered
Hendon	Leasehold Expires December 2096	Registered

Name & address of property	*Freehold or leasehold (and lease expiry date if relevant)*	*Registered at H M Land Registry or unregistered*
Water Treatment Works South		
Ormesby A	Leasehold (Lease may no longer exist, having on the face of it expired in 1989. However, the land involved appears to be insignificant).	Unregistered
Ormesby B	Freehold	Part Registered
Lound	Freehold	Unregistered
Barsham	Freehold	Unregistered
Langham	Freehold	Unregistered
Langford	Freehold	Registered
Hanningfield	Freehold	Registered
Chigwell	Freehold	Unregistered
Offices		
Hall Street Offices, Chelmsford	Freehold	Unregistered
St Mary's Convent Site	Freehold	Registered
Durham House Offices, Pity Me, Durham	Leasehold Expires June 2009	Unregistered
Pity Me Head Office Complex	Freehold	Registered
Northumbria House, the Regent Centre, Gosforth	Leasehold Expires July 2013	
Thornaby	Freehold	Registered
Vange	Freehold	Registered
Sea Pipelines		
Long Sea Outfalls	Leasehold Expires April 2096	Unregistered

13. Litigation and Arbitration

There are no, nor have there been any, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which the Company is aware) which may have or have had, during the 12 months prior to the publication of this document, a significant effect on the financial position of the Group.

14. Working Capital

The Company is of the opinion that, after taking into account the Group's existing bank facilities, the Group has sufficient working capital for its present requirements, that is for at least the next 12 months from the date of publication of this document.

15. Taxation

The following statements are intended only as a general guide to the current tax position under UK taxation law and practice. They may not apply to certain classes of Shareholders, such as dealers in securities, or to Shareholders who are not absolute beneficial owners of their shares. A Shareholder who is in any doubt as to his or her tax position or is subject to tax in any jurisdiction other than the UK should consult his or her professional adviser without delay.

15.1 *Dividends*

Under current UK legislation, the Company will not be required to withhold tax at source when paying a dividend in respect of the Ordinary Shares.

A UK resident individual Shareholder will be entitled to a tax credit in respect of any dividend received equal to one ninth of the amount of the dividend. The tax credit therefore equals ten per cent. of the aggregate amount of the dividend and tax credit. Liability to UK income tax is calculated on the sum of the dividend and the tax credit. The tax credit will be available to offset such a Shareholder's liability to income tax on the dividend.

Individual Shareholders whose income is within the starting rate or basic rate tax bands are subject to income tax at the rate of ten per cent. on their dividend income, so that such Shareholders will have no further liability to income tax on their dividends. The higher rate of income tax is 32.5 per cent. in respect of dividend income (rather than the main rate of 40 per cent.), so that a shareholder whose income is subject to higher rate income tax will, after allowing for the ten per cent. tax credit, be liable to pay further income tax equal to 22.5 per cent. of the amount of the dividend and the tax credit or 25 per cent. of the dividend actually received, before the addition of the tax credit. A Shareholder who is not liable to income tax on the dividend (or any part of it) is not able to claim payment of the tax credit (or part of it) in cash from the Inland Revenue, save where the dividend is paid on or before 5 April 2004 in respect of shares held in a personal equity plan or an individual savings account.

UK resident corporate Shareholders (including authorised unit trusts and open-ended investment companies) and pension funds will not normally be liable to UK taxation on any dividend received and are not entitled to payment in cash of the tax credit.

Registered charities may reclaim tax credits on a reducing basis until 5 April 2004.

Whether Shareholders who are resident for tax purposes in countries other than the UK are entitled to the whole or a proportion of the tax credit in respect of dividends on their shares depends in general upon the provisions of any double taxation convention or agreement which exists between such countries and the UK. In addition, individual Shareholders who are resident in countries other than the UK but who are Commonwealth citizens, nationals of member states of the European Economic Area or fall within certain other categories of person are entitled to the entire tax credit which they may set against their total UK income tax liability. Such Shareholders should consult their own tax advisers on the possible application of such provisions and any relief or credit which may be claimed in respect of such tax credit in their own jurisdictions. However, in general, no cash payment is recoverable from the Inland Revenue in respect of the tax credit.

15.2 *Capital Gains Tax*

Shareholders who are resident or ordinarily resident for tax purposes in the UK may, depending upon their individual circumstances, be liable to UK taxation on chargeable gains on a disposal of shares.

A Shareholder who is not resident or ordinarily resident for tax purposes in the UK will not be liable to UK taxation on chargeable gains unless the Shareholder carries on a trade, profession or vocation in the UK through a branch or agency or in the case of a non-resident company permanent establishment in the UK and the shares are, or have been, used, held or acquired for the purposes of such trade, profession or vocation or for the purposes of such branch or agency or in the case of a non-resident company permanent establishment.

15.3 *Inheritance Tax*

Shares are assets situated in the UK for the purposes of UK inheritance tax. A gift of shares by, or the death of, an individual Shareholder may (subject to certain exemptions and reliefs) give rise to a liability to UK inheritance tax even if the Shareholder is neither domiciled nor deemed to be domiciled in the UK.

15.4 *Stamp Duty and Stamp Duty Reserve Tax*

No stamp duty or stamp duty reserve tax ("SDRT") will be payable on the issue of shares, save to a person who issues depositary receipts or provides clearance services in respect of such shares or to a nominee or agent for such person, in which case SDRT will payable at the rate of 1.5 per cent. of the issue price. The Company will not meet such SDRT.

Where shares are held in certificated form, no stamp duty or SDRT will arise on a transfer of such shares into CREST unless such transfer is made for a consideration in money or money's worth, in which case a liability to SDRT (usually at a rate of 0.5 per cent.) will arise. Transfers of shares within CREST will be liable to SDRT rather than stamp duty.

Any agreement to transfer shares outside CREST made for a consideration in money or money's worth will give rise to a liability on the purchaser to stamp duty or SDRT usually at the rate of 0.5 per cent. of the consideration paid.

Special rules apply to market makers, broker-dealers and certain other persons. Agreements to transfer shares to charities will not give rise to stamp duty reserve tax or stamp duty.

15.5 *Effect of admission to the Official List*

The listing of the Ordinary Shares on the Official List will mean that the Ordinary Shares will no longer be classed as shares in an unlisted company for the purposes of various tax reliefs, including inheritance tax business property relief, capital gains tax taper relief and the enterprise investment scheme, among others.

16. Employees

The average number of employees of the Group in the three financial years ended 31 December 2002 was:

2000	3,480
2001	3,439
2002	3,563

17. Significant Changes

Save for the effects of the Atlantic Acquisition, Placing, related financing and Credit Rating Downgrade there has been no significant change in the financial or trading position of the Group since 31 March 2003 being the latest date reported on in the accountants' report in Parts 4 and 5 of this document.

For further details see paragraph 1 of Part 1, Part 6 and paragraph 11.1 of Part 7 in respect of the Atlantic Acquisition and the Placing; paragraphs 1 and 5 of Part 1, Part 6 and paragraph 11.1 of Part 7 in respect of the related financing; and paragraph 5 of Part 1 in respect of the Credit Rating Downgrade.

18. General

18.1 Ernst & Young LLP has given and not withdrawn its written consent to the inclusion in this document of its name and reports and the references thereto in the form and context in which they appear and has authorised those parts of this document which comprise reports and the said references for the purpose of Regulation 6(1)(e) of the Financial Services and Markets Act 2000 (Official Listing of Securities) Regulations 2001.

18.2 Collins Stewart, which is regulated by the Financial Services Authority Limited, has given and not withdrawn its written consent to the issue of this document with the inclusion herein of the references to its name in the form and context in which they appear.

18.3 Except in relation to the Atlantic Acquisition, details of which are set out in paragraph 1 of Part 1 of this document, there have been no interruptions in the business of the Group which may have or have had a significant effect on the financial position of the Group in the 12 months preceding the date of this document.

18.4 The expenses of and incidental to Admission including registration and listing fees, printing, advertising and distribution costs, legal and accounting fees and expenses and commissions which are payable by the Company are estimated to amount to approximately £0.9 million (excluding Value Added Tax).

18.5 Except for Collins Stewart, Deutsche Bank and Ecofin Limited, insofar as they may be termed promoters of the Company, and who together received approximately £38.5 million in commissions for their services to the Company in the Atlantic Acquisition, Placing and AIM Admission, there has been no promoter of the Company within the two years immediately preceding the date of this document and no cash, securities or benefits have been paid or issued or given to any of the present Shareholders within such two year period in his capacity as a promoter and none is proposed to be paid, issued or given.

18.6 Save for the Atlantic Acquisition, there have been no investments made in other undertakings by members of the Group in the last three financial years and during the period 1 January 2003 to 16 September 2003 (being the latest practicable date prior to the publication of this document).

18.7 Other than the arrangement set out below there are no patents or other intellectual property rights, licences or particular contracts or new manufacturing processes, where any of these are of fundamental importance to the Group's business or profitability:

(A) NWL currently uses ICIS software for billing and customer care purposes, pursuant to a perpetual, non-exclusive and non-transferable licence with Suez. The Directors believe such software is of fundamental importance to NWL's business and profits.

18.8 The financial information set out in this document relating to the Company does not constitute statutory accounts within the meaning of Section 240(5) of the Act. The Company was incorporated on 12 May 2003 and has not been required to prepare statutory accounts since its incorporation. Ernst & Young LLP have reported on the statutory consolidated accounts of NSL for the year ended 31 December 2002 within the meaning of Section 235 of the Act. Arthur Andersen (which has ceased trading) reported on the statutory consolidated accounts of NSL for the two years ended 31 December 2000 and 2001. Each such report was unqualified within the meaning of Section 262 of the Act and did not contain a statement under Section 237(2) or (3) of the Act.

18.9 (A) All statements and other information (other than statements of historical facts included in any information provided to Ofwat by the Group and which Ofwat may publish (on its website or in any other way), including without limitation, statements relating to NWL and/or the Group financial position, business strategy, plans and management objectives for future operations) are forward looking statements. Such publications include the Draft Business Plan.

(B) Such statements and information involve risks (known and unknown), uncertainties and other factors which may render industry results, or the actual results, performance or achievements of NWL and/or the Group, materially different from any future results, performance or achievements expressed or implied by such forward looking statements. Numerous assumptions in respect of NWL's present and future business strategies and the environment in which NWL will operate in the future govern such forward looking statements, and the statements may contain financial modelling based on provisional estimates and assumptions which may vary significantly. Except as required by the rules of the London Stock Exchange and the UK Listing Authority, the Company and the Group expressly disclaim any obligation or undertaking to publicly release any updates or revision to any such forward looking statements contained therein to reflect any change in the Company's or the Group's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based. Neither the Company nor the Group make any representation, warranty or undertaking, express or implied or accept any responsibility as to the accuracy, completeness or adequacy of any such information. Nothing contained in such statements or information is or shall be relied upon as a promise or representation by any of the Company, NWL or any of their affiliates or subsidiaries and they accept no responsibility or liability howsoever arising from the contents of such information or the status or any omissions in such information.

19. Documents on Display

Copies of the following documents will be available for inspection at the offices of Simmons & Simmons during normal business hours on any weekday (Saturday, Sundays and public holidays excepted) from the date of this document until a date one month following Admission:

(A) the Company's memorandum of association and Articles;

(B) the audited accounts of NSL for the financial years ended 31 December 2000, 2001 and 2002 and the audited non-statutory financial statements for the 13 weeks ended 31 March 2003;

(C) the reports produced by Ernst & Young LLP set out in Parts 4, 5 and 6 of this document;

(D) the statement of adjustments prepared by Ernst & Young LLP for the NSL Group;

(E) the material contracts referred to in paragraph 11 of Part 7 of this document;

(F) the executive directors' service agreements and non-executive directors' agreements referred to in paragraphs 8.1 and 8.3 of Part 7 of this document;

(G) the consent letters referred to in paragraph 18 of Part 7 of this document;

(H) the Ofwat Position Paper;

(I) the Ofwat Consultation Paper;

(J) the Ofwat Levels of Service Reports for 2002-2003, 2001-2002 and 2001-2000; and

(K) this document.

Dated: 18 September 2003

Millnet Financial (6693-01)