

**REGULATORY FINANCIAL STATEMENTS**

**NORTHUMBRIAN WATER LIMITED**

**FOR THE YEAR ENDED 31 MARCH 2002**

Registered no: 2366703

# **CONDITION F REGULATORY FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MARCH 2002**

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## **DIRECTORS' REPORT**

### **For the year ended 31 March 2002**

The directors present their report and the audited regulatory financial statements for the year ended 31 March 2002.

#### **Results and dividends**

The group's profit after taxation for the year ended 31 March 2002 amounts to £106.9m (March 2001: £46.7m as restated). The directors proposed a final dividend of £42.1m (March 2001: £40.2m) for the year ended 31 March 2002 which, together with the interim dividend of £42.0m (March 2001: £36.8m), makes a total of £84.1m for the year (March 2001: £77.0m).

#### **Principal activities and review of business**

The principal activities of the business comprise the supply of potable water in both the Northern and Southern regions, and the collection, treatment and disposal of sewage and sewage sludge throughout the North East of England.

Operational compliance with regulatory requirements during the year remained high, and the company has also achieved a better performance against the customer services measures set by Ofwat. Ofwat has not yet published its water industry comparative performance statistics against these measures but, given that Northumbrian Water Limited achieved the best performance in the water industry in 2000/01 and has improved its performance in 2001/02, the company expects to be well placed in the 2001/02 performance rankings.

The appointed business turnover from existing operations has increased by 1.4% from £407.3m to £413.1m. This is mainly due to an increase of £8.1m reflecting RPI of 3.2% being applied to the previous years tariff income of £387.0m, partially offset by the remaining weighted average price reduction of 1.1% required by Ofwat at the last periodic review. However, reductions in consumption by large users, together with the failure of a number of these customers, have resulted in income losses of £2.6m.

There has also been a transfer of the income and costs associated with the supply of non-potable water to industrial customers from the non-appointed to the appointed business. The income from this activity of £9.2m is disclosed separately in the profit and loss account.

The appointed business operating costs show an increase on the prior year of £6.8m, reflecting the impact of new operating costs from a variety of sources, partially offset by further efficiencies achieved in the year. The most significant increase related to the costs of operating the new secondary sewage treatment facilities required to meet the Urban Waste Water Treatment Directive, which resulted in £9.4m of additional costs. The transfer of the non-potable water activities into the appointed business accounted for a further £8.1m cost increase. The increase also reflects the impact of other new costs including the climate change levy (£2.1m), cryptosporidium monitoring (£1.2m) and Section 74 claims (£1.2m), none of which were funded in the prices set by Ofwat at the last periodic review. Inflationary pressures have also caused an uplift in the cost base of approximately £1.8m.

These cost increases were offset by £11.0m of efficiencies achieved in the year and a net movement of £6.0m on atypical costs. The efficiencies reflected the impact of the ongoing internal efficiency programme augmented by the savings which were achieved in 2001/02 from the merger between the Northern and Southern Operating regions. In 2000/01 the company incurred £2.8m costs which were treated as atypical in the June return. In 2001/02, Northumbrian Water Limited released £3.2m of accruals relating to prior year rates charges for a number of properties which are no longer required following the introduction of new legislation in 2001.

The appointed business capital maintenance costs also show an increase of £9.2m, reflecting the depreciation impact of the new assets commissioned during 2000/01 and 2001/2, particularly the additional depreciation arising from the secondary sewage treatment facilities.

During 2001/02 the company successfully raised £150.0m as a "tap" on its existing 2023 Bond and later issued a £300m Bond dated 2017 from a new subsidiary specifically set up for funding purposes. The gearing of the appointed business has now risen to 59% which, together with the income losses and additional costs referred to above takes the company very close to the financial ratios assumed as a floor for PR99.

The future focus of the company continues to be improving efficiency levels and driving down operating costs while maintaining high standards of customer service and developing the skills and effectiveness of its employees. Continuous improvement will be necessary to ensure the company is successful in the competitive market.

**DIRECTORS' REPORT (continued)**

**Financial Statements Preparation and Going Concern**

The directors consider that it is appropriate to prepare the financial statements for the financial year on the going concern basis. The directors have arrived at their decision based on consideration of the company's detailed budget for 2002 and the five year business plan for the period from 2001 to 2005. Their analysis included a review of the capital expenditure and investment plans, the anticipated funding requirements and facilities available, and the reasonableness of the underlying assumptions of both the budget and business plans.

**Research and development**

The company places a high priority on research and technological innovation to serve the needs of customers. Research and development is now co-ordinated by a sister company, Northumbrian Lyonnaise Technology and Research Centre Limited, a specialist subsidiary, wholly owned by the company's immediate parent, which has links with other Suez S.A. group research organisations worldwide. The company incurred costs of research and development in the period of £5.1m (March 2001: £5.9m).

**Northumbrian Water payment policy**

The company's policy is to agree payment terms with suppliers when agreeing the terms of each transaction, also ensuring that suppliers are made aware of and abide by the terms of payment. The year end trade creditors expressed as a number of days of purchases made during the year is 28 days (March 2001: 26 days). This has been calculated by dividing the year end trade creditors balance of £3.3m by the aggregate of the average daily amounts invoiced by suppliers during the year.

**Fixed Assets**

Freehold land and buildings are carried in the accounts at historical cost with a net book value of £58.7m (March 2001: £69.7m). In the opinion of the directors, at 31 March 2002, there is no significant difference between the net book value and the market value of property capable of disposal within the foreseeable future.

## **DIRECTORS' REPORT (continued)**

### **Directors**

The directors who served during the year were as follows:

Professor Sir F G T Holliday CBE (66)  
Non-Executive Chairman

P Babin (44)  
Non-Executive Director

J A Cuthbert (49)  
Executive Managing Director  
(Appointed as Managing Director on 1 November 2001)

A Chaigneau (51)  
Non-Executive Director

R R Allan (67)  
Non-Executive Director

C M Green (47)  
Executive Director

G Neave (46)  
Executive Director – appointed 31 January 2002

Sir J D R Bradbeer OBE  
Resigned 31 March 2002

J A Haynes  
Resigned 31 March 2002

A J Harding  
Resigned 1 November 2001

M A B Nègre  
Resigned 2 May 2001

A Frew (45) and A Balls (58) were appointed as non-executive directors on 1 April 2002.

Directors' interests are disclosed in note 6 to the financial statements.

## **DIRECTORS' REPORT (continued)**

### **Employees and Employment Policies**

#### Equal Opportunities

The company operates an equal opportunity policy and promotes equality of opportunity in recruitment, employment continuity, training and career development. The policy is designed to ensure that no applicant or employee receives less favourable treatment than another. The company is a member of 'Opportunity Now', which demonstrates our commitment to equal opportunity, and has been awarded an 'Exemplars of Best Practice' certificate.

#### Disabled Employees

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned. In the event of members of staff becoming disabled, every effort is made to ensure that their employment with the company continues and that appropriate training is arranged. It is the policy of the company that the training, career development and promotion of disabled persons should, as far as possible, be identical with that of other employees.

#### Training and Development

Training and development of employees is a priority of the company. This year employees from the company have again participated in the Ondeo Global Player Programme which was created to ensure that highly skilled and experienced staff are ready and available to meet the ongoing worldwide business needs of the company and its parent company, Suez S.A.

#### Communication

Communication with staff is achieved through the company's corporate newspaper 'WaterMark' and the increased use of the company's intranet facilities. Employees are regularly informed about matters concerning their interests and the financial and economic factors affecting the company. The company has also established its own communication mechanisms such as team briefings, electronic mail and notice boards. Further, the company receives Job News and an English version of 'Terre Bleue', Suez S.A.'s corporate magazine.

#### Health and Safety

Health and safety policies are maintained and implemented through the company's safety team. Employee health services are provided by the company's Medical Adviser. Most employees are members of a company wide corporate health care plan managed by CIGNA Healthcare.

#### Employee Investment Schemes

The company has invited employees to join an employee investment scheme which is offered by the parent company, Suez S.A.

The present scheme, called SPRING, consists of two elements giving employees a choice of two different types of investment, or a combination of both. They can invest in a fund, SPRING Classic, which holds Suez S.A. shares which have been purchased at a discount, and/or, they can invest in a company, SPRING Multiple, which also holds Suez S.A. shares.

The SPRING Multiple investment guarantees the employee the return on their initial investment but gives the opportunity to increase their share in any growth in the value of the ultimate parent company's shares through the existence of a matched investment by Credit Agricole Indosuez.

The Directors believe that employee investment is a valuable method of strengthening the ties between the company employees and Suez S.A. by providing the opportunity for employees to participate more closely in the parent company's economic performance and results. To encourage participation in the plan the company made a discretionary contribution of up to £100 for all employees investing in SPRING Classic.

A total of 1,102 Northumbrian Water employees invested in SPRING 2000. The company has committed itself to future biennial employee investment opportunities and is currently launching SPRING 2002.

## **DIRECTORS' REPORT (continued)**

### **Pensions**

Information about the pension schemes operated by the company is contained in note 28 to the financial statements.

### **Charitable and Political Contributions**

During the year the company made charitable donations of £74,644 (March 2001: £55,182). The company made no donations to any political party during the year (March 2001: £nil).

### **Auditors**

The company has appointed Arthur Andersen as its auditors and has, by elective resolution pursuant to section 386 of the Companies Act 1985, dispensed with the obligation to appoint auditors annually.

### **Directors' Responsibilities**

The directors are responsible, under Condition F of the Instrument of Appointment by the Secretary of State for the Environment, for the company, as a water and sewerage undertaker under the Water Industry Act 1991, to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the company and of the group as at the end of the financial year and of the profit or loss of the group for that year.

The directors confirm that suitable accounting policies have been used and applied consistently, and reasonable, prudent judgements and estimates have been made in the preparation of the financial statements for the year ended 31 March 2002. The directors also confirm that, except for the departure in relation to infrastructure renewals accounting explained in note 1 to the financial statements, which arises from the instructions of the Director General of Water Services, applicable accounting standards have been followed and that the financial statements have been prepared on the going concern basis.

The directors are responsible for keeping proper accounting records as required by United Kingdom company law, for taking reasonable steps to safeguard the assets of the group, and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

### **Auditors' Responsibilities**

The auditors are responsible for forming an independent opinion on the financial statements presented by the directors, based on their audit, and reporting their opinion to shareholders. Company law also requires the auditors to report to shareholders if the following requirements are not met:

- that the company has maintained proper accounting records;
- that the financial statements are in agreement with the accounting records;
- that directors' emoluments and other transactions with the directors are properly disclosed in the financial statements; and
- that they have obtained all information and explanations which, to the best of their knowledge and belief, are necessary for the purposes of their audit.

The auditors' opinion does not encompass the Directors' Report. However, the Companies Act requires the auditors to report to the shareholders if the matters contained in the Directors' Report are inconsistent with the financial statements.

ON BEHALF OF THE BOARD

M Parker  
Company Secretary  
10th July 2002

**GROUP HISTORICAL COST PROFIT AND LOSS ACCOUNT****For the year ended 31 March 2002**

	Note	2002			2001 (as restated)		
		Appointe d business	Non- appointed business	Aggregate d basis	Appointe d business	Non- appointed business	Aggregate d basis
		£'m	£'m	£'m	£'m	£'m	£'m
<b>TURNOVER</b>							
Existing operations	3	413.1	25.0	438.1	407.3	23.0	430.3
Acquired/(disposed) operations	3	9.2	(9.2)	-	-	-	-
		<u>422.3</u>	<u>15.8</u>	<u>438.1</u>	<u>407.3</u>	<u>23.0</u>	<u>430.3</u>
Operating costs	4(a)	(186.0)	(5.9)	(191.9)	(179.2)	(13.5)	(192.7)
Capital maintenance costs	4(b)	(81.5)	(0.5)	(82.0)	(72.3)	(1.3)	(73.6)
Exceptional operating costs	4(c)	-	-	-	(2.0)	-	(2.0)
Total operating expenses	4(d)	<u>(267.5)</u>	<u>(6.4)</u>	<u>(273.9)</u>	<u>(253.5)</u>	<u>(14.8)</u>	<u>(268.3)</u>
<b>OPERATING PROFIT</b>							
Existing operations		154.0	10.2	164.2	153.8	8.2	162.0
Acquired/(disposed) operations		0.8	(0.8)	-	-	-	-
<b>TOTAL OPERATING PROFIT</b>	3	<u>154.8</u>	<u>9.4</u>	<u>164.2</u>	<u>153.8</u>	<u>8.2</u>	<u>162.0</u>
Net interest payable	5	<u>(67.4)</u>	<u>(0.7)</u>	<u>(68.1)</u>	<u>(64.4)</u>	<u>(1.0)</u>	<u>(65.4)</u>
<b>PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION</b>							
Taxation	9(a)	<u>12.8</u>	<u>(2.0)</u>	<u>10.8</u>	<u>(46.1)</u>	<u>(3.8)</u>	<u>(49.9)</u>
<b>PROFIT FOR THE FINANCIAL YEAR</b>		<u>100.2</u>	<u>6.7</u>	<u>106.9</u>	<u>43.3</u>	<u>3.4</u>	<u>46.7</u>
Dividends	10	<u>(72.8)</u>	<u>(11.3)</u>	<u>(84.1)</u>	<u>(65.0)</u>	<u>(12.0)</u>	<u>(77.0)</u>
<b>PROFIT/(LOSS) RETAINED FOR THE YEAR</b>	25	<u>27.4</u>	<u>(4.6)</u>	<u>22.8</u>	<u>(21.7)</u>	<u>(8.6)</u>	<u>(30.3)</u>

The accompanying notes are an integral part of this consolidated profit and loss account.

**STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES**

	Note	2002			2001 (as restated)		
		Appointe d business	Non- appointed business	Aggregate d basis	Appointe d business	Non- appointed business	Aggregate d basis
		£'m	£'m	£'m	£'m	£'m	£'m
Total recognised gains in the period		100.2	6.7	106.9	43.3	3.4	46.7
Prior year adjustment	2	<u>(142.5)</u>	<u>(3.9)</u>	<u>(146.4)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total gains and losses recognised since last annual report and financial statements		<u>(42.3)</u>	<u>2.8</u>	<u>(39.5)</u>	<u>43.3</u>	<u>3.4</u>	<u>46.7</u>



**GROUP HISTORICAL COST BALANCE SHEET****At 31 March 2002**

	Note	2002	2001
		<u>£'m</u>	<u>(as restated)</u>
			<u>£'m</u>
<b>FIXED ASSETS</b>			
Tangible assets	11	<u>2,289.9</u>	<u>2,186.6</u>
<b>CURRENT ASSETS</b>			
Stocks	13	2.7	2.3
Debtors	14	95.5	95.6
Investments	15	33.7	0.2
Cash at bank and in hand		<u>16.2</u>	<u>16.2</u>
		148.1	114.3
<b>CREDITORS</b>			
Amounts falling due within one year	16(a)	<u>(226.6)</u>	<u>(350.9)</u>
<b>NET CURRENT LIABILITIES</b>			
		<u>(78.5)</u>	<u>(236.6)</u>
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>			
		<u>2,211.4</u>	<u>1,950.0</u>
<b>CREDITORS: Amounts falling due after more than one year</b>			
	17	(1,137.8)	(884.2)
<b>PROVISIONS FOR LIABILITIES AND CHARGES</b>			
	22	(149.4)	(164.6)
<b>ACCRUALS AND DEFERRED INCOME</b>			
	23	<u>(33.5)</u>	<u>(33.3)</u>
		<u>(1,320.7)</u>	<u>(1,082.1)</u>
<b>NET ASSETS</b>			
		<u>890.7</u>	<u>867.9</u>
<b>CAPITAL AND RESERVES</b>			
Called up share capital	24	122.7	122.7
Profit and loss account	25	<u>768.0</u>	<u>745.2</u>
<b>EQUITY SHAREHOLDERS' FUNDS</b>			
	26	<u>890.7</u>	<u>867.9</u>

The accompanying notes are an integral part of this consolidated balance sheet.

Approved on behalf of the board on 10th July 2002

J A Cuthbert

C M Green

**COMPANY HISTORICAL COST BALANCE SHEET**  
**At 31 March 2002**

	Note	2002			2001 (as restated)		
		Appointe d business	Non- appointed business	Aggregate d basis	Appointe d business	Non- appointed business	Aggregate d basis
		£'m	£'m	£'m	£'m	£'m	£'m
<b>FIXED ASSETS</b>							
Tangible assets	11	2,192.6	97.3	2,289.9	2,076.2	110.4	2,186.6
Investments	12	89.4	-	89.4	89.4	-	89.4
		<u>2,282.0</u>	<u>97.3</u>	<u>2,379.3</u>	<u>2,165.6</u>	<u>110.4</u>	<u>2,276.0</u>
<b>CURRENT ASSETS</b>							
Stocks	13	2.5	0.2	2.7	2.2	0.1	2.3
Debtors	14	94.6	0.9	95.5	91.1	4.5	95.6
Investments	15	33.7	-	33.7	0.2	-	0.2
Cash at bank and in hand		<u>16.2</u>	<u>-</u>	<u>16.2</u>	<u>16.2</u>	<u>-</u>	<u>16.2</u>
		147.0	1.1	148.1	109.7	4.6	114.3
<b>CREDITORS</b>							
Amounts falling due within one year	16(b)	<u>(210.9)</u>	<u>(15.7)</u>	<u>(226.6)</u>	<u>(323.2)</u>	<u>(27.7)</u>	<u>(350.9)</u>
<b>NET CURRENT LIABILITIES</b>							
		<u>(63.9)</u>	<u>(14.6)</u>	<u>(78.5)</u>	<u>(213.5)</u>	<u>(23.1)</u>	<u>(236.6)</u>
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>							
		<u>2,218.1</u>	<u>82.7</u>	<u>2,300.8</u>	<u>1,952.1</u>	<u>87.3</u>	<u>2,039.4</u>
<b>CREDITORS: Amounts falling due after more than one year</b>							
	17	<u>(1,227.1)</u>	<u>(0.1)</u>	<u>(1,227.2)</u>	<u>(973.4)</u>	<u>(0.2)</u>	<u>(973.6)</u>
<b>PROVISIONS FOR LIABILITIES AND CHARGES</b>							
	22	<u>(144.3)</u>	<u>(5.1)</u>	<u>(149.4)</u>	<u>(159.7)</u>	<u>(4.9)</u>	<u>(164.6)</u>
<b>ACCRUALS AND DEFERRED INCOME</b>							
	23	<u>(33.0)</u>	<u>(0.5)</u>	<u>(33.5)</u>	<u>(32.7)</u>	<u>(0.6)</u>	<u>(33.3)</u>
		<u>(1,404.4)</u>	<u>(5.7)</u>	<u>(1,410.1)</u>	<u>(1,165.8)</u>	<u>(5.7)</u>	<u>(1,171.5)</u>
<b>NET ASSETS</b>							
		<u>813.7</u>	<u>77.0</u>	<u>890.7</u>	<u>786.3</u>	<u>81.6</u>	<u>867.9</u>
<b>CAPITAL AND RESERVES</b>							
Called up share capital	24	92.1	30.6	122.7	92.1	30.6	122.7
Profit and loss account	25	<u>721.6</u>	<u>46.4</u>	<u>768.0</u>	<u>694.2</u>	<u>51.0</u>	<u>745.2</u>
<b>EQUITY SHAREHOLDERS' FUNDS</b>							
	26	<u>813.7</u>	<u>77.0</u>	<u>890.7</u>	<u>786.3</u>	<u>81.6</u>	<u>867.9</u>

The accompanying notes are an integral part of this balance sheet.

Approved on behalf of the board on 10th July 2002

J A Cuthbert

C M Green

**GROUP HISTORICAL COST CASH FLOW STATEMENT**  
**For the year ended 31 March 2002**

	Note	2002			2001		
		Appointe d business	Non- appointed business	Aggregate d basis	Appointe d business	Non- appointed business	Aggregate d basis
		£'m	£'m	£'m	£'m	£'m	£'m
<b>NET CASH INFLOW FROM CONTINUING OPERATING ACTIVITIES</b>	a	189.2	13.8	203.0	192.9	11.1	204.0
<b>Returns on investments and servicing of finance</b>							
Interest received		3.9	-	3.9	5.3	-	5.3
Interest paid		(64.3)	(0.6)	(64.9)	(62.8)	(1.0)	(63.8)
Interest element of finance lease rentals		(0.4)	-	(0.4)	(2.4)	-	(2.4)
Net cash outflow from returns on investments and servicing of finance		(60.8)	(0.6)	(61.4)	(59.9)	(1.0)	(60.9)
<b>Taxation</b>							
United Kingdom corporation tax paid		(6.5)	(2.2)	(8.7)	(24.1)	(3.6)	(27.7)
Net cash outflow from taxation		(6.5)	(2.2)	(8.7)	(24.1)	(3.6)	(27.7)
<b>Capital expenditure and financial investment</b>							
Purchase of tangible fixed assets		(157.8)	(0.1)	(157.9)	(198.4)	(0.2)	(198.6)
Sale of tangible fixed assets		0.8	-	0.8	0.2	-	0.2
Grants, contributions and connection charges		8.6	-	8.6	8.9	-	8.9
Purchase of business		-	-	-	(0.7)	-	(0.7)
Net cash outflow from capital expenditure and financial investment		(148.4)	(0.1)	(148.5)	(190.0)	(0.2)	(190.2)
<b>Equity dividend paid</b>		(70.2)	(12.0)	(82.2)	(66.6)	(12.3)	(78.9)
<b>CASH OUTFLOW BEFORE MANAGEMENT OF LIQUID RESOURCES AND FINANCING</b>		(96.7)	(1.1)	(97.8)	(147.7)	(6.0)	(153.7)
<b>Management of liquid resources</b>							
Purchase of short term deposits		(1,028.9)	-	(1,028.9)	-	-	-
Sale of short term deposits		995.4	-	995.4	32.9	-	32.9
Net cash (outflow)/inflow from management of liquid resources		(33.5)	-	(33.5)	32.9	-	32.9
<b>Financing</b>							
New loans		457.7	-	457.7	134.8	-	134.8
New leases		0.8	-	0.8	1.1	-	1.1
Loan repayments		(324.3)	-	(324.3)	(10.9)	-	(10.9)
Capital element of finance lease rental payments		(4.0)	-	(4.0)	(3.5)	-	(3.5)
Net cash inflow from financing	b	130.2	-	130.2	121.5	-	121.5
<b>(DECREASE)/INCREASE IN CASH IN THE YEAR</b>		-	(1.1)	(1.1)	6.7	(6.0)	0.7

The accompanying notes are an integral part of this consolidated cash flow statement.

**NOTES TO THE CASH FLOW STATEMENT**  
**For the year ended 31 March 2002**

**a. RECONCILIATION OF OPERATING PROFIT TO CASH FLOWS**

	2002			2001		
	Appointed business	Non- appointed business	Aggregated basis	Appointed business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Operating profit	154.8	9.4	164.2	153.8	8.2	162.0
Depreciation on tangible fixed assets	49.0	0.5	49.5	39.6	1.1	40.7
Infrastructure renewals expenditure	(34.7)	-	(34.7)	(29.9)	-	(29.9)
Provision for infrastructure renewals	33.0	0.1	33.1	32.9	0.2	33.1
Amortisation of grants	(3.3)	(0.1)	(3.4)	(1.6)	-	(1.6)
Profit on sale of fixed assets	(0.6)	-	(0.6)	(0.2)	-	(0.2)
(Increase)/decrease in stock	(0.3)	(0.1)	(0.4)	0.8	-	0.8
Decrease/(increase) in debtors	(2.8)	3.6	0.8	(1.4)	0.5	(0.9)
(Decrease)/increase in creditors	(4.2)	(0.6)	(4.8)	0.1	1.1	1.2
(Decrease)/increase in provisions	(0.8)	0.1	(0.7)	(1.1)	(0.1)	(1.2)
(Decrease)/increase in inter business debtor/creditor	(0.9)	0.9	-	(0.1)	0.1	-
Net cash inflow from operating activities	<u>189.2</u>	<u>13.8</u>	<u>203.0</u>	<u>192.9</u>	<u>11.1</u>	<u>204.0</u>

The operating cash flows are all from continuing operations.

**b. ANALYSIS AND RECONCILIATION OF NET DEBT**

	Appointed business			
	1 April 2001	Cash Flow	Other non-cash changes	31 March 2002
	£'m	£'m	£'m	£'m
Cash in hand and at bank	16.2	-	-	16.2
Debt due after 1 year	(830.8)	(281.7)	30.7	(1,081.8)
Debt due within 1 year	(148.3)	148.3	(30.6)	(30.6)
Finance leases	(56.5)	3.2	(4.7)	(58.0)
	<u>(1,035.6)</u>	<u>(130.2)</u>	<u>(4.6)</u>	<u>(1,170.4)</u>
Current asset investments	-	33.5	-	33.5
Net debt	<u>(1,019.4)</u>	<u>(96.7)</u>	<u>(4.6)</u>	<u>(1,120.7)</u>

**b. ANALYSIS AND RECONCILIATION OF NET DEBT (continued)**

	<b>Non-appointed business</b>			
	1 April 2001	Cash Flow	Other non-cash changes	31 March 2002
	£'m	£'m	£'m	£'m
Overdrafts	(16.9)	(1.1)	-	(18.0)
Net debt	(16.9)	(1.1)	-	(18.0)

Reconciliation of cash flow movement to net debt:

	2002	2002			2001
	Group	Appointe d business	Non- appointed business	Aggregated business	Group and Aggregated business
	£'m	£'m	£'m	£'m	£'m
(Decrease)/increase in cash in the year	(1.1)	-	(1.1)	(1.1)	0.7
Cash inflow from increase in debt and lease financing	(130.2)	(130.2)	-	(130.2)	(121.5)
Cash outflow/(inflow) from reduction in liquid resources	33.5	33.5	-	33.5	(32.9)
Change in net debt resulting from cash flows	(97.8)	(96.7)	(1.1)	(97.8)	(153.7)
Finance costs incurred during the year	0.1	0.1	-	0.1	(0.2)
Finance lease interest capitalised	(2.2)	(2.2)	-	(2.2)	(1.4)
Finance lease non cash movement	(2.5)	(2.5)	-	(2.5)	(1.1)
Debt acquired from Essex & Suffolk Water plc	-	-	-	-	(105.5)
Debt issued to purchase the assets of Essex & Suffolk Water plc	-	-	-	-	(176.0)
Movement in net debt in year	(102.4)	(101.3)	(1.1)	(102.4)	(437.9)
Net debt at 1 April 2001	(1,036.3)	(1,019.4)	(16.9)	(1,036.3)	(598.4)
Net debt at 31 March 2002	(1,138.7)	(1,120.7)	(18.0)	(1,138.7)	(1,036.3)

## NOTES TO THE HISTORICAL COST FINANCIAL STATEMENTS

For the year ended 31 March 2002

### 1. STATEMENT OF ACCOUNTING POLICIES

In accordance with Condition F of "the Instrument", these financial statements have been prepared to show separately in respect of each of:

- i. the appointed business;
- ii. the non-appointed business; and
- iii. on an aggregated basis, the appointed and non-appointed businesses;

a profit and loss account, a statement of assets and liabilities and a cash flow statement, together with notes thereto prepared under the historical cost basis.

These financial statements have been prepared in accordance with applicable Accounting Standards in the United Kingdom with the exception of:

- capital grants and contributions to infrastructure assets which is not in accordance with the Companies Act 1985 (as described in (e) below).
- infrastructure renewals accounting which, following the instructions of the Director General of Water Services set out in his letter RD15/99, dated 21 April 1999, "Regulatory Accounts for 1998/9 Reporting Requirements – RAG 3.04", has been accounted for in accordance with RAG 2, "Classification of Infrastructure Expenditure". RAG 2 is not in accordance with Financial Reporting Standard No. 12, "Provisions, Contingent Liabilities and Contingent Assets" and Financial Reporting Standard No. 15, "Tangible Fixed Assets" as described in section (d) (i) below.

A summary of the more important accounting policies, which have been applied consistently throughout the year and in the preceding year, is set out below.

#### (a) Basis of accounting

These accounts have not been prepared for the purposes of Section 226 of the Companies Act 1985, "Duty to prepare individual company accounts," and are therefore not statutory accounts.

The financial statements have been prepared under the historical cost convention on the going concern basis.

#### (b) Basis of consolidation

The consolidated financial statements include the company and its subsidiary undertakings. The results of subsidiaries acquired during the year are included from the date of their acquisition. Intra-group sales and profits are eliminated fully on consolidation.

#### (c) Turnover

Turnover, which excludes Value Added Tax, represents the income receivable in the ordinary course of business for services provided within the United Kingdom.

#### (d) Tangible fixed assets and depreciation

Tangible fixed assets comprise:

##### (i) Infrastructure assets

Infrastructure assets comprise a network of systems which include water mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls.

**1. STATEMENT OF ACCOUNTING POLICIES (continued)**

Expenditure on infrastructure assets relating to increases in capacity or enhancements of the network is treated as additions which are included at cost after deducting grants and contributions.

Expenditure on maintaining the operating capability of the network in accordance with defined standards of service is charged as an operating cost. No depreciation is charged on infrastructure assets because the network of systems is required to be maintained in perpetuity and therefore has no finite economic life.

In accordance with instructions from the Director General of the Office of Water Services set out in his letter RD15/99, dated 21 April 1999, “Regulatory Accounts for 1998/9 Reporting Requirements – RAG 3.04”, the Group and Company have not applied Financial Reporting Standard No. 12, “Provisions, Contingent Liabilities and Contingent Assets” (“FRS12”) and Financial Reporting Standard No. 15, “Tangible Fixed Assets” (“FRS15”) in respect of infrastructure renewals accounting and have continued to charge infrastructure renewal costs (calculated in accordance with their Asset Management Plan) to the profit and loss account. Expenditure during the year is charged to the provision.

Under FRS12 and FRS15, it is not permitted to recognise a provision for the costs of renewals expenditure. Adoption of FRS12 and FRS15, taken together with Financial Reporting Standard No. 15, Measurement of Tangible Assets, would require:

- restatement of the cost and accumulated depreciation of infrastructure fixed assets to reflect infrastructure renewals expenditure, depreciation and retirement of assets since renewals accounting was first adopted. Accordingly, infrastructure renewals provisions and prepayments at years ended 31 March 2001 and 31 March 2002 would have been included within infrastructure fixed assets.
- the depreciation of infrastructure assets and the inclusion of the infrastructure renewals charge as a component of the depreciation charge for the year.

**(ii) Other assets**

Other assets (including properties, overground plant and equipment) are included at cost less accumulated depreciation and provisions for diminution in value. Additions are included at cost.

Freehold land is not depreciated. Other assets are depreciated evenly to their estimated residual values over their estimated economic lives, which are principally as follows:

Freehold buildings	30 – 60 years
Operational structures, plant and machinery	4 – 80 years
Fixtures, fittings, tools and equipment	4 – 10 years

**(iii) Assets in the course of construction**

Assets in the course of construction are not depreciated until commissioned, which is when the asset is available for use.

**(e) Government grants and contributions**

Revenue grants are credited to the profit and loss account when received.

Grants and contributions relating to infrastructure assets have been deducted from the cost of those assets as permitted under Statement of Standard Accounting Practice No. 4. This is not in accordance with the Companies Act 1985 which requires fixed assets to be stated at their purchase price or production cost without deduction of grants and contributions which are accordingly accounted for as deferred income. This departure from the requirements of the Act is, in the opinion of the directors, necessary for the accounts to give a true and fair view as infrastructure assets are not depreciated, and it is therefore not appropriate to recognise related grants and contributions as deferred income. The effect of the departure on the value of tangible fixed assets is disclosed in note 11.

Capital grants and contributions relating to other assets are treated as deferred income and amortised in the profit and loss account over the expected useful economic lives of the qualifying assets.

**1. STATEMENT OF ACCOUNTING POLICIES (continued)****(f) 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 company, 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 charged 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 charged to the profit and loss account in the period in which they are incurred.

**(g) Stocks**

Raw materials and consumables are stated at purchased cost less any provision necessary to recognise damage and obsolescence. Cost of work in progress includes labour, materials, transport and an element of overheads.

**(h) 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 accruals in the balance sheet.

**(i) Taxation**

The charge for current UK corporation tax is based on the profit for the year as adjusted for taxation purposes using the rates of tax enacted by the balance sheet date.

Financial Reporting Standard No. 19, "Deferred taxation" ("FRS19"), has been adopted in the period. In previous periods deferred tax was dealt with under Statement of Standard Accounting Practice 15 and by adopting a partial provision approach no provision was made in the accounts. Under FRS19 full provision for deferred tax is required for deferred tax assets and liabilities arising from timing differences between the recognition of gains and losses in the financial statements and their recognition in a tax computation.

As permitted by the FRS the company has decided to adopt a policy of discounting deferred tax assets and liabilities to reflect the time value of money over the period between the balance sheet date and the dates on which it is estimated that the underlying timing differences will reverse. The discount rates used reflect the post-tax yields to maturity that can be obtained on government bonds with similar maturity dates to those of the deferred tax assets or liabilities.

As a consequence the balance sheet has been restated to show a deferred tax liability at 31 March 2001 of £146.4m and the profit and loss account has been restated to show a deferred tax charge for the year ended 31 March 2001 of £40.2m, as described in note 2.

**(j) Foreign currency**

All transactions denominated in foreign currencies are translated into sterling at the actual rates of exchange ruling at the dates of the transactions. Foreign currency balances are translated into sterling at the rates of exchange ruling at the balance sheet date or applicable foreign forward contract rate. Exchange gains or losses are recognised in the profit and loss account in the period incurred.

**(k) Research and development**

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

**(l) Investments**

Fixed asset investments are stated at their purchase cost, less provision for diminution in value.



**1. STATEMENT OF ACCOUNTING POLICIES (continued)****(m) Derivative Financial Instruments**

The company 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 company in line with the company'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.

**2. PRIOR YEAR ADJUSTMENT**

As set out in note 1(i) above the company has changed its accounting policy for deferred tax by adopting FRS 19. As a result the comparatives have been restated as follows :

**(a) Group profit and loss account**

	Taxation			Profit for the financial year		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Year ended 31 March 2001 as previously reported	6.1	3.6	9.7	83.3	3.6	86.9
Prior year adjustment	40.0	0.2	40.2	(40.0)	(0.2)	(40.2)
Year ended 31 March 2001 as restated	46.1	3.8	49.9	43.3	3.4	46.7

The brought forward reserves for 2001 have been restated by £106.2m (appointed business: £102.5m, non-appointed business: £3.7m).

**(b) Group balance sheet**

	Provisions for liabilities and charges			Profit and loss reserve		
	Deferred tax					
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
£'m	£'m	£'m	£'m	£'m	£'m	
Year ended 31 March 2001 as previously reported	-	-	-	836.7	54.9	891.6
Prior year adjustment	142.5	3.9	146.4	(142.5)	(3.9)	(146.4)
Year ended 31 March 2001 as restated	142.5	3.9	146.4	694.2	51.0	745.2

## SECTION B – HISTORICAL COST FINANCIAL STATEMENTS

## 3. TURNOVER AND OPERATING PROFIT

The directors consider that the company has one class of business and this is conducted wholly within the United Kingdom.

## 4. OPERATING COSTS AND CAPITAL MAINTENANCE COSTS

(a) Operating costs comprise:

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Materials and consumables	12.3	0.6	12.9	11.7	0.5	12.2
Other external charges	50.7	2.7	53.4	36.5	2.2	38.7
Manpower costs (note 8a)	59.3	1.8	61.1	56.1	2.7	58.8
Other operating charges	79.9	0.8	80.7	87.6	8.1	95.7
Own work capitalised	(16.2)	-	(16.2)	(12.7)	-	(12.7)
	<u>186.0</u>	<u>5.9</u>	<u>191.9</u>	<u>179.2</u>	<u>13.5</u>	<u>192.7</u>

The value of own work capitalised represents both employment costs (note 8a) and some other costs incurred on capital projects.

(b) Capital maintenance costs comprise:

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Depreciation:						
Owned tangible fixed assets	44.4	0.7	45.1	34.9	1.0	35.9
Tangible fixed assets held under finance leases	4.4	-	4.4	4.7	0.1	4.8
Acquired/(disposed) operations	0.3	(0.3)	-	-	-	-
Infrastructure renewals expenditure	34.7	-	34.7	29.9	-	29.9
Infrastructure renewals accrued	(1.7)	0.1	(1.6)	3.0	0.2	3.2
Profit on disposal of fixed assets	(0.6)	-	(0.6)	(0.2)	-	(0.2)
	<u>81.5</u>	<u>0.5</u>	<u>82.0</u>	<u>72.3</u>	<u>1.3</u>	<u>73.6</u>

(c) Exceptional operating costs comprise:

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Reorganisation/ restructuring costs	<u>-</u>	<u>-</u>	<u>-</u>	<u>2.0</u>	<u>-</u>	<u>2.0</u>

The reorganisation/restructuring costs represent exceptional costs resulting from a severance scheme which was introduced during 2000 following the merging of the operations of Northumbrian Water Limited and Essex and Suffolk Water plc.

## 4. OPERATING COSTS AND CAPITAL MAINTENANCE COSTS (continued)

(d) Total operating expenses comprise:

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Existing operations	259.1	14.8	273.9	253.5	14.8	268.3
Acquired/(disposed) operations	8.4	(8.4)	-	-	-	-
	<u>267.5</u>	<u>6.4</u>	<u>273.9</u>	<u>253.5</u>	<u>14.8</u>	<u>268.3</u>

(e) Profit on ordinary activities before taxation

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Profit on ordinary activities before taxation is stated after crediting:						
Receipt and amortisation of capital grants and contributions	<u>4.0</u>	<u>-</u>	<u>4.0</u>	<u>1.6</u>	<u>-</u>	<u>1.6</u>
And after charging:						
Operating leases: Plant and machinery	0.8	-	0.8	2.4	-	2.4
Costs of research and development	5.1	-	5.1	5.9	-	5.9
Directors' emoluments (note 6)	<u>0.8</u>	<u>-</u>	<u>0.8</u>	<u>0.8</u>	<u>-</u>	<u>0.8</u>

Auditors' remuneration for the regulatory audit amounted to £31,000 (March 2001: regulatory audit £44,200). There were no fees for non audit services (March 2001: nil)

**5. NET INTEREST**

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Net interest payable comprises:						
Interest payable:						
Bank loans and overdrafts	67.0	0.7	67.7	62.4	1.0	63.4
Debenture stock interest	2.3	-	2.3	2.3	-	2.3
Financing charges payable under finance leases	2.7	-	2.7	3.7	-	3.7
Total interest payable	72.0	0.7	72.7	68.4	1.0	69.4
Interest receivable	(4.6)	-	(4.6)	(4.0)	-	(4.0)
Net interest payable	67.4	0.7	68.1	64.4	1.0	65.4

**6. DIRECTORS' EMOLUMENTS AND INTERESTS**Directors' remuneration

The remuneration of the directors of the company was as follows:

	2002	2001
	£'000	£'000
Emoluments (including benefits in kind)	806.7	802.9

Highest paid director

The above amounts for remuneration include the following in respect of the highest paid director:

	2002	2001
	£'000	£'000
Emoluments (including benefits in kind)	204.2	210.5

The accrued pension entitlement under the company's defined benefit scheme of the highest paid director at 31 March 2002 was £34,746 (March 2001: £56,501). In addition to the pension, there is a tax free lump sum at normal pension date of which the accrued entitlement at 31 March 2002 is £104,238 (March 2001: £148,939).

Three of the directors at 31 March 2002 were members of a defined benefit pension scheme where the company makes contributions towards the cost (March 2001: 3)

The directors who held office at 31 March 2002 had no interest in the shares of the company.

The directors who held office on 31 March 2002 had the following beneficial interests in the ordinary shares, other than share options, and debentures of the company's ultimate parent company, Suez S.A.:

Name of Director	Description of shares or debentures	31 March 2002	Start of period or subsequent date of appointment
P Babin	Ordinary Shares of €	2,633	3,067
J A Cuthbert	Ordinary Shares of €	3,561	3,561
Professor Sir F G T Holliday	Ordinary Shares of €	-	2,000
C M Green	Ordinary Shares of €	2,446	2,446
A Chaigneau	Ordinary Shares of €	7,742	9,042

**6. DIRECTORS' EMOLUMENTS AND INTERESTS (continued)**

The directors who held office on 31 March 2002 held the following options over ordinary shares of €2 each in Suez S.A.:

Name of Director	Start of period or subsequent date of appointment	Granted/(Exercised) During the year	31 March 2002	Exercise Price
P Babin	17,500	-	17,500	€17.47
	20,000	-	20,000	€29.82
	22,500	-	22,500	€30.22
	32,500	-	32,500	€36.41
	-	40,000	40,000	€34.51
	92,500	40,000	132,500	
J A Cuthbert	6,000	(6,000)	-	€13.90
	11,000	-	11,000	€17.47
	11,500	-	11,500	€29.82
	12,500	-	12,500	€30.22
	13,000	-	13,000	€36.41
	-	14,000	14,000	€34.51
	54,000	8,000	62,000	
Professor Sir F G T Holliday	15,000	-	15,000	€17.47
	15,000	-	15,000	€29.82
	15,000	-	15,000	€30.22
	15,000	-	15,000	€36.41
	-	15,000	15,000	€34.51
	60,000	15,000	75,000	
C M Green	3,500	-	3,500	€17.47
	5,000	-	5,000	€29.82
	3,500	-	3,500	€30.22
	4,500	-	4,500	€36.41
	-	5,000	5,000	€34.51
	16,500	5,000	21,500	
A Chaigneau	5,000	(5,000)	-	€13.90
	17,500	-	17,500	€17.47
	20,000	-	20,000	€29.82
	25,000	-	25,000	€30.22
	30,000	-	30,000	€36.41
	-	35,000	35,000	€34.51
	97,500	30,000	127,500	

No options have lapsed during the year.

On 4 May 2001 Suez S.A. shareholders resolved to restructure that company's ordinary share capital by splitting each Suez S.A. ordinary share with a nominal value of €10 into five new shares with a nominal value of €2 each. The restructure took effect on 15 May 2001 and the Company's Register of Directors Interests in shares has been adjusted to reflect the change.

All options with an exercise price of €13.90 were granted on 24 July 1996 and are exercisable between 24 July 1998 and 24 July 2004.

All options with an exercise price of €17.47 were granted on 17 November 1997 and are exercisable between 17 November 2002 and 17 November 2005.

All options with an exercise price of €29.82 were granted on 16 November 1998 and are exercisable between 16 November 2003 and 16 November 2006.

All options with an exercise price of €30.22 were granted on 15 November 1999 and are exercisable between 15 November 2004 and 15 November 2007.

All options with an exercise price of €36.41 were granted on 28 November 2000 and are exercisable between 28 November 2004 and 28 November 2010.

**6. DIRECTORS' EMOLUMENTS AND INTERESTS (continued)**

All options with an exercise price of €34.51 were granted on 28 November 2001 and are exercisable between 28 November 2005 and 28 November 2011.

The highest and lowest prices of the Suez S.A. shares during the year were €8.75 and €30.88 respectively.

No director holds any other interest required to be disclosed in accordance with Schedule 7 of the Companies Act 1985.

**7. TRANSACTIONS WITH DIRECTORS AND OFFICERS**

No transactions or arrangements which are disclosable under the provisions of the Companies Act 1985 have occurred during the year.

**8. EMPLOYEE INFORMATION**

(a) The total employment costs of all employees (including directors) were charged as follows:

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Costs charged to the profit and loss account:						
Wages and salaries	38.7	1.5	40.2	38.3	2.3	40.6
Social security costs	3.1	0.1	3.2	3.2	0.2	3.4
Other pension costs	2.9	0.2	3.1	3.1	0.2	3.3
	<u>44.7</u>	<u>1.8</u>	<u>46.5</u>	<u>44.6</u>	<u>2.7</u>	<u>47.3</u>
Costs charged to capital schemes and infrastructure renewals:						
Wages and salaries	12.6	-	12.6	9.8	-	9.8
Social security costs	1.0	-	1.0	0.8	-	0.8
Other pension costs	1.0	-	1.0	0.9	-	0.9
	<u>14.6</u>	<u>-</u>	<u>14.6</u>	<u>11.5</u>	<u>-</u>	<u>11.5</u>

(b) The average monthly number of employees on the payroll during the financial year was as follows:

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	No.	No.	No.	No.	No.	No.
Average during the year	<u>2,148</u>	<u>55</u>	<u>2,203</u>	<u>2,066</u>	<u>74</u>	<u>2,140</u>
Total at 31 March	<u>2,185</u>	<u>50</u>	<u>2,235</u>	<u>2,053</u>	<u>64</u>	<u>2,117</u>

**9. TAXATION****(a) Analysis of charge in the period:**

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Current tax:						
UK corporation tax on profits of the period at 30%	1.4	0.3	1.7	1.9	0.7	2.6
Adjustments in respect of prior periods	(4.6)	-	(4.6)	(3.3)	(0.9)	(4.2)
Payable in respect of group relief for the current period at 30%	2.9	1.7	4.6	4.1	3.0	7.1
Adjustments in respect of prior periods	0.4	-	0.4	3.4	0.8	4.2
Total current tax	0.1	2.0	2.1	6.1	3.6	9.7
Deferred tax:						
Origination and reversal of timing differences	27.8	0.1	27.9	27.6	0.1	27.7
(Decrease)/increase due to discount	(40.7)	(0.1)	(40.8)	12.4	0.1	12.5
Total deferred tax	(12.9)	-	(12.9)	40.0	0.2	40.2
Tax on profit on ordinary activities	(12.8)	2.0	(10.8)	46.1	3.8	49.9

The appointed business has provisionally claimed tax losses from fellow subsidiaries in the current year of £9.7m (March 2001: £13.7m) for which payment will be made at the rate of 30%.

The non-appointed business has provisionally claimed tax losses from fellow subsidiaries in the current year of £5.6m (March 2001: £10.0m) for which payment will be made at the rate of 30%.

The high level of deferred tax charge in the year to 31 March 2001 was due to the impact of significant falls in interest rates.

**9. TAXATION (continued)****(b) Factors affecting the tax charge for the period:**

The tax assessed for the period is lower than the standard rate of corporation tax in the UK (30%). The differences are explained below:

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Profit on ordinary activities before tax	87.4	8.7	96.1	89.4	7.2	96.6
Profit on ordinary activities multiplied by standard rate of UK corporation tax (30%)	26.2	2.6	28.8	26.8	2.2	29.0
Effects of:						
Expenses not deductible for tax purposes	1.8	0.1	1.9	2.0	0.1	2.1
Capital allowances in excess of depreciation	(21.0)	(0.6)	(21.6)	(24.4)	(0.6)	(25.0)
Other timing differences	(2.5)	-	(2.5)	(0.9)	-	(0.9)
Other items	(0.2)	(0.1)	(0.3)	2.5	2.0	4.5
Adjustment to tax charge in respect of previous periods	(4.2)	-	(4.2)	0.1	(0.1)	-
Current tax charge	0.1	2.0	2.1	6.1	3.6	9.7

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

The company expects to continue 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 is therefore influenced by future fluctuations in gilt rates.



**10. DIVIDENDS**

	2002			2001		
	Appointed business	Non- appointed business	Aggregated basis	Appointed business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Equity:						
Interim paid of 34.23p (March 2001: 29.99p) per share on an aggregated basis	36.0	6.0	42.0	30.8	6.0	36.8
Final paid of 34.31p (March 2001: 32.76p) per share on an aggregated basis	36.8	5.3	42.1	34.2	6.0	40.2
	<u>72.8</u>	<u>11.3</u>	<u>84.1</u>	<u>65.0</u>	<u>12.0</u>	<u>77.0</u>

The directors have a policy which, unless circumstances dictate otherwise, aims to grow dividends on a slow but regular basis and which takes into account the principle of incentive based price cap regulation, including operating and investment performance.

Included within the dividend payable of £77.0m in 2001 is an amount of £10.0m, relating to dividends payable from the profits generated by the operations acquired from Essex and Suffolk Water plc since April 2000.

By agreement with Ofwat, the company has transferred the activities of the raw water business from the non-appointed business to the appointed business with effect from 1 April 2001. The appointed business dividend has been increased accordingly and the non-appointed business dividend reduced. Other than this one off stepped change, the company has maintained its policy of a steady 2% real growth per annum for the appointed business dividend. Dividends from the non-appointed business are determined by the directors and are based upon performance.

In accordance with the principle of incentive based price cap regulation, rewards to shareholders will reflect company performance against Ofwat targets, in particular operating and investment targets.

Accordingly, the level of dividend has been declared by reference to:-

- the company's ability to finance its functions;
- the company's cumulative financial performance; and
- Directors' judgement as to a fair reward for shareholders in the context of market conditions.

**10. TANGIBLE FIXED ASSETS – GROUP AND COMPANY**

The net book value of infrastructure assets, including infrastructure assets in the course of construction, is stated after the deduction of grants and contributions amounting to £96.7m (March 2001: £91.7m) in order to give a true and fair view (note 1e).

	Freehold land and buildings	Infra- structure assets	Operational structures, plant and machinery	Fixtures, fittings, tools and equipment	Assets in the course of construction	Aggregated Basis
	£'m	£'m	£'m	£'m	£'m	£'m
<b>Cost:</b>						
At 1 April 2001	87.1	961.6	1,172.9	75.8	182.4	2,479.8
Additions	-	-	-	-	158.0	158.0
<b>Schemes</b>						
commissioned/reallocated	(8.2)	8.5	253.7	14.4	(268.4)	-
Disposals	(0.3)	-	-	-	-	(0.3)
Grants and contributions	-	(2.0)	-	-	(3.0)	(5.0)
At 31 March 2002	78.6	968.1	1,426.6	90.2	69.0	2,632.5
<b>Depreciation:</b>						
At 1 April 2001	17.4	-	223.2	52.6	-	293.2
Provision for year	2.6	-	40.1	6.8	-	49.5
Disposals	(0.1)	-	-	-	-	(0.1)
At 31 March 2002	19.9	-	263.3	59.4	-	342.6
<b>Net book value:</b>						
At 31 March 2002	58.7	968.1	1,163.3	30.8	69.0	2,289.9
At 31 March 2001	69.7	961.6	949.7	23.2	182.4	2,186.6
<b>Leased assets included above:</b>						
<b>Net book value</b>						
At 31 March 2002	-	2.2	27.6	1.9	-	31.7
At 31 March 2001	-	2.2	27.2	2.5	1.0	32.9
			Appointed business Water Supply	Sewerage services	Non- Appointed business	Aggregated basis
			£'m	£'m	£'m	£'m
<b>Cost:</b>						
At 1 April 2001			949.5	1,393.0	137.3	2,479.8
Additions			97.1	60.8	0.1	158.0
Raw Water assets			18.5	-	(18.5)	-
Disposals			(0.3)	-	-	(0.3)
Grants and contributions			(2.4)	(2.6)	-	(5.0)
At 31 March 2002			1,062.4	1,451.2	118.9	2,632.5
<b>Depreciation:</b>						
At 1 April 2001			96.5	169.8	26.9	293.2
Provision for the year			14.7	34.3	0.5	49.5
Raw Water assets			5.8	-	(5.8)	-
Disposals			(0.1)	-	-	(0.1)
At 31 March 2002			116.9	204.1	21.6	342.6
<b>Net Book Value:</b>						
At 31 March 2002			945.5	1,247.1	97.3	2,289.9
At 31 March 2001			853.0	1,223.2	110.4	2,186.6

**12. FIXED ASSET INVESTMENTS – COMPANY**

	March 2002	March 2001
	£'m	£'m
Investment in Newcastle and Gateshead Water plc	47.2	47.2
Investment in Suffolk Water plc	42.2	42.2
	<u>89.4</u>	<u>89.4</u>

The company has a wholly owned subsidiary undertaking, Newcastle and Gateshead Water plc, whose principal activity is the holding of a loan note due from the company. This investment equates to a 100% holding in Newcastle and Gateshead Water plc of £40.7m, and a long term loan investment of £6.5m. Included in the net assets of Newcastle and Gateshead Water plc is a loan note receivable from Northumbrian Water Limited of £47.2m. Both companies have agreed that no interest will be levied on the loan note. The results of this subsidiary have been consolidated in these financial statements.

The company has a wholly owned subsidiary undertaking in Suffolk Water plc, whose principal activity is the holding of a loan note due from the company. This investment is valued at £42.2m which equates to the net assets of that company. Both companies have agreed that no interest will be levied on the loan note. The results of this subsidiary have been consolidated in these financial statements.

**13. STOCKS – GROUP AND COMPANY**

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Raw materials and consumables	<u>2.5</u>	<u>0.2</u>	<u>2.7</u>	<u>2.2</u>	<u>0.1</u>	<u>2.3</u>

There is no material difference between the balance sheet value of stocks and their replacement costs.

**14. DEBTORS – GROUP AND COMPANY**

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Trade debtors	57.4	0.6	58.0	65.5	3.1	68.6
Amounts owed by other group companies	2.1	0.2	2.3	5.8	0.2	6.0
Other debtors	5.4	-	5.4	5.1	-	5.1
Prepayments and accrued income	<u>29.7</u>	<u>0.1</u>	<u>29.8</u>	<u>14.7</u>	<u>1.2</u>	<u>15.9</u>
	<u>94.6</u>	<u>0.9</u>	<u>95.5</u>	<u>91.1</u>	<u>4.5</u>	<u>95.6</u>

**15. INVESTMENTS – GROUP AND COMPANY**

	2002			2001		
	Appointed business	Non- appointed business	Aggregated basis	Appointed business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Short term deposits	33.5	-	33.5	-	-	-

## SECTION B – HISTORICAL COST FINANCIAL STATEMENTS

Assets held for resale	0.2	-	0.2	0.2	-	0.2
	<u>33.7</u>	<u>-</u>	<u>33.7</u>	<u>0.2</u>	<u>-</u>	<u>0.2</u>

**16. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR****(a) Group:**

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Obligations under finance leases (note 20)	3.6	-	3.6	4.5	-	4.5
Bank overdraft	-	18.0	18.0	-	16.9	16.9
Loans (note 18)	22.6	-	22.6	13.5	-	13.5
Debenture stock (note 19)	8.0	-	8.0	-	-	-
Trade creditors	3.1	0.2	3.3	4.2	0.1	4.3
Amounts owed to other group companies	13.6	0.8	14.4	152.6	1.7	154.3
Taxation and social security	1.2	0.1	1.3	1.7	0.1	1.8
Corporation tax	12.8	0.4	13.2	16.7	0.5	17.2
Receipts in advance	15.1	-	15.1	14.7	-	14.7
Other creditors	14.9	0.1	15.0	19.6	0.3	19.9
Dividend payable	36.8	5.3	42.1	34.2	6.0	40.2
Accruals and deferred income	69.6	0.4	70.0	62.8	0.8	63.6
Inter business balance	9.6	(9.6)	-	(1.3)	1.3	-
	<u>210.9</u>	<u>15.7</u>	<u>226.6</u>	<u>323.2</u>	<u>27.7</u>	<u>350.9</u>

**(b) Company:**

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Obligations under finance leases (note 20)	3.6	-	3.6	4.5	-	4.5
Bank overdraft	-	18.0	18.0	-	16.9	16.9
Loans (note 18)	22.6	-	22.6	13.5	-	13.5
Debenture stock (note 19)	8.0	-	8.0	-	-	-
Trade creditors	3.1	0.2	3.3	4.2	0.1	4.3
Amounts owed to other group companies	19.1	0.8	19.9	152.6	1.7	154.3
Taxation and social security	1.2	0.1	1.3	1.7	0.1	1.8
Corporation tax	12.8	0.4	13.2	16.7	0.5	17.2
Receipts in advance	15.1	-	15.1	14.7	-	14.7
Other creditors	14.9	0.1	15.0	19.6	0.3	19.9
Dividend payable	36.8	5.3	42.1	34.2	6.0	40.2
Accruals and deferred income	64.1	0.4	64.5	62.8	0.8	63.6
Inter business balance	9.6	(9.6)	-	(1.3)	1.3	-

## SECTION B – HISTORICAL COST FINANCIAL STATEMENTS

210.9	15.7	226.6	323.2	27.7	350.9
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**16. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR (continued)**

Accruals and deferred income includes accruals related to capital projects of £29.0m (March 2001: £31.6m). Amounts owed to other group companies includes amounts related to capital projects of £2.9m (March 2001: £2.7m)

Included in amounts owed to other group companies is £4.6m (appointed business £3.7m (March 2001: £5.1m), non-appointed business £0.9m (March 2001: £1.7m)) payable in respect of tax losses surrendered by fellow subsidiaries.

**17. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR**

	2002		2001	
	Group	Company	Group	Company
	£'m	£'m	£'m	£'m
Obligations under hire purchase contracts and finance leases (note 20)	54.4	54.4	52.0	52.0
Loans (note 18)	596.4	295.5	318.2	318.2
Debenture stocks (note 19)	14.2	14.2	22.2	22.2
Amounts owed to other group companies	471.7	862.0	490.4	579.8
Other creditors	1.1	1.1	1.4	1.4
	<u>1,137.8</u>	<u>1,227.2</u>	<u>884.2</u>	<u>973.6</u>

At 31 March 2002 the group and company had entered into the following interest swap arrangements: £15.0m (March 2001: £15.0m) over a ten year period commencing on 10 May 1994 under which the group and company is required to pay interest at a rate linked to LIBOR and will receive interest at 9.00%, and £29.0m (March 2001: £4.7m) over a seven year period commencing on 16 December 1996 under which the group and company is required to pay interest at a rate linked to LIBOR and will receive interest at 7.45%, and £25.0m over a three year period commencing on 7 December 2000 under which the group and company is required to pay interest at 5.61% and will receive interest at a rate linked to LIBOR, and £25.0m over a five year period commencing 23 May 1997 under which the group and company is required to pay interest at a rate linked to LIBOR and will receive interest at 7.45%.

Included in amounts owed to other group companies is £0.5m (appointed business £0.4m (March 2001: £nil), non-appointed business £0.1m (March 2001: £nil)) payable in respect of tax losses surrendered by fellow subsidiaries.

Included in other creditors is £0.1m (appointed business £0.1m (March 2001: £0.2m), non-appointed business £nil (March 2001: £0.2m)) in respect of corporation tax payable.

**18. LOANS**

	2002		2001	
	Group	Company	Group	Company
	£'m	£'m	£'m	£'m
External loans are repayable as follows:				
Within one year	22.6	22.6	13.5	13.5
Between one and two years	23.0	23.0	22.6	22.6
Between two and five years	94.8	94.8	84.0	84.0
After five years	478.6	177.7	211.6	211.6
	<u>619.0</u>	<u>318.1</u>	<u>331.7</u>	<u>331.7</u>

**18. LOANS (continued)**

Loans repayable by instalments wholly repayable within 5 years amount to £32.4m (March 2001: £29.8m).

Loans repayable by instalments not wholly repayable within 5 years amount to £180.8m (March 2001: £196.9m) and bear interest rates in the range of 6.02% to 8.55% of which £78.0m (March 2001: £75.3m) falls due in less than 5 years and £102.8m (March 2001: £121.6m) falls due after more than 5 years.

Loans repayable otherwise than by instalments which fall due in less than 5 years amount to £30.0m (March 2001: £15.0m) and bear interest rates in the range of 4.05% to 7.95%.

Loans repayable otherwise than by instalments which fall due after more than 5 years amount to £375.8m (March 2001: £90.0m) and bear interest at rates in the range of 3.5% to 6.0%.

The level of capital expenditure which the company is obliged to incur is such that it cannot be wholly financed by internally generated sources. As a result, the company must rely upon raising additional finance on a regular basis to fund the long term assets required in its business. The company'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.

**Treasury operations**

The company's board is responsible for the financing strategy of the company which is determined within treasury policies set by the company's immediate parent company, Ondeo Services UK plc. The aim of this strategy is to assess the ongoing capital requirement of the company and to raise funding on a timely basis, taking advantage of any favourable market opportunities.

The treasury department carries out treasury operations on behalf of the company. Surplus funds are invested based upon forecast requirements, in accordance with the treasury policy. On occasion, derivatives are used as part of this process, but the treasury policies prohibit their use for speculation.

**Risks arising from company's financial instruments**

The main risks arising from the company's financial instruments are liquidity risk, interest rate risk and foreign currency risk. As noted above, the company's financing strategy is developed in accordance with the treasury policies of Ondeo Services UK plc, whose board reviews and agrees policies for managing each of these risks. These are summarised below. All Northumbrian Water Limited treasury activities are conducted in accordance with these policies.

**Liquidity risk**

As regards day to day liquidity, the company is responsible for cash management but is reliant upon the committed borrowing facilities available to Ondeo Services UK plc. Ondeo Services UK plc's policy is to have available standby committed bank borrowing facilities with a value of no less than £50m and with a bank agreement availability period of no less than 3 months.

**Interest rate risk**

The company finances its operations through a mixture of retained profits and borrowings. It borrows at both fixed and floating rates of interest and, as noted above, on occasion uses derivatives to generate the desired interest profile and to manage its exposure to interest rate fluctuations. Ondeo Services UK plc's policy is to keep a minimum 50 per cent of its borrowings at fixed rates of interest.

**Foreign currency risk**

Ondeo Services UK plc's policy is that any foreign currency exposure in excess of £100,000 sterling equivalent of a transactional nature, or £3m sterling equivalent of a translation nature, should be covered immediately on recognition.

**18. LOANS (continued)****Interest rate risk profile of financial assets and financial liabilities**

The interest rates and currency profile of the net borrowings of the group at 31 March 2002 were:

	Total net borrowings	Variable rate net borrowings	Fixed Rate Net Borrowings			Financial liabilities on which no interest is paid	
			Fixed Rate Borrowings	Weighted average interest rate	Weighted average period until maturity		
	£'m	£'m	£'m	%	Years	Years	£'m
Sterling borrowings:							
External loans	(318.1)	(90.8)	(227.3)	7.56	9.1	9.1	-
Eurobonds	(300.9)	-	(300.9)	6.00	15.5	15.5	-
Debentures	(22.2)	-	(22.2)	10.53	4.3	4.3	-
Internal loans	(471.2)	(119.5)	(351.7)	6.75	20.9	20.9	-
Finance leases	(58.0)	(51.6)	(6.4)	8.24	5.6	5.6	-
Bank overdraft	(18.0)	(18.0)	-	-	-	-	-
Total borrowings	(1,188.4)	(279.9)	(908.5)	6.81	15.6	15.6	-
Cash	16.2	16.2	-	-	-	-	-
Short term investments	33.5	33.5	-	-	-	-	-
Net borrowings	(1,138.7)	(230.2)	(908.5)				-

The interest rates and currency profile of the net borrowings of the group at 31 March 2001 were:

	Total net borrowings	Variable rate net borrowings	Fixed Rate Net Borrowings			Financial liabilities on which no interest is paid	
			Fixed Rate Borrowings	Weighted average interest rate	Weighted average period until maturity		
	£'m	£'m	£'m	%	Years	Years	£'m
Sterling borrowings:							
External loans	(331.7)	(92.5)	(239.2)	7.58	9.9	9.9	-
Debentures	(22.2)	-	(22.2)	10.53	5.3	5.3	-
Internal loans	(625.2)	(430.4)	(194.8)	6.99	21.9	21.9	-
Finance leases	(56.5)	(49.4)	(7.1)	9.12	1.6	1.6	-
Bank overdraft	(16.9)	(16.9)	-	-	-	-	-
Total borrowings	(1,052.5)	(589.2)	(463.3)	7.49	14.6	14.6	-
Cash	16.2	16.2	-	-	-	-	-
Net borrowings	(1,036.3)	(573.0)	(463.3)				-

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

Included within the external sterling loans of the group above are loans amounting to £98.8m whose rates are fixed for a period of 5 to 7 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.

**18. LOANS (continued)****Currency exposures**

At 31 March 2002, the group and the company had no currency exposures (March 2001: nil).

**Borrowing facilities**

The group had no undrawn committed borrowing facilities as at 31 March 2002 but had access to undrawn committed borrowing facilities available to Ondeo Services UK plc which, at 31 March 2002, amounted to £150.0m.

The facilities available to Ondeo Services UK plc at 31 March 2002, in respect of which all conditions precedent have been met, were as follows:

	£'m
Expiring in one year or less	110.0
Expiring in more than one year but not more than three years	40.0
	<u>150.0</u>

**Fair values of financial assets and financial liabilities**

Set out below is a comparison by category of book values and fair values of the financial assets and liabilities of the group as at 31 March 2002:

	<u>Book value</u>	<u>Fair value</u>
	£'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	(52.2)	(57.6)
Long-term borrowings	(1,136.2)	(1,159.8)
Financial assets	49.7	49.7
Derivative financial instruments held to manage the interest rate and currency profile:		
Interest rate swaps	-	1.9
As at 31 March 2002	<u>(1,138.7)</u>	<u>(1,165.8)</u>

Set out below is a comparison by category of book values and fair values of the financial assets and liabilities of the group as at 31 March 2001:

	<u>Book value</u>	<u>Fair value</u>
	£'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	(169.7)	(172.3)
Long-term borrowings	(882.8)	(902.1)
Financial Assets	16.2	16.2
Derivative financial instruments held to manage the interest rate and currency profile:		
Interest rate swaps	-	2.3
As at 31 March 2001	<u>(1,036.3)</u>	<u>(1,055.9)</u>



**18. LOANS (continued)**

The fair values of the interest rate swaps, and sterling denominated long-term fixed rate debt with a book value of £674.8m (March 2001: £217.0m), 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.

**Gains and losses on hedges**

The company's board uses the Northumbrian Water Limited treasury function to enter into any necessary forward foreign currency contracts on the company's behalf to eliminate the currency exposures that arise on sales denominated in foreign currencies immediately those sales are transacted. The company 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 for the group is as follows:

	<u>Gains</u>	<u>Losses</u>	<u>Total net Gains/Losses</u>
	£'m	£'m	£'m
Unrecognised gains and losses on hedges at 1 April 2001	2.7	0.4	2.3
Gains and losses arising in previous years that were recognised in 2001/2002	1.1	0.2	0.9
Gains and losses arising before 1 April 2001 that were not recognised in 2001/2002	1.6	0.2	1.4
Gains and losses arising in 2001/2002 that were not recognised in 2001/2002	0.6	0.1	0.5
Unrecognised gains and losses on hedges at 31 March 2002	<u>2.2</u>	<u>0.3</u>	<u>1.9</u>
Of which:			
Gains and losses expected to be recognised in 2002/2003	2.2	0.2	2.0
Gains and losses expected to be recognised in 2003/2004 or later	-	0.1	0.1
	<u>2.2</u>	<u>0.3</u>	<u>1.9</u>

**Market price risk**

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

**19. DEBENTURE STOCKS – GROUP AND COMPANY**

	<u>2002</u>	<u>2001</u>
	Appointed and aggregated basis	Appointed and aggregated basis
	£'m	£'m
Debenture stocks are repayable as follows:		
In less than one year:		
£1, 11.75% Redeemable 2002/04	8.0	-
Between two and five years:		
£1, 11.75% Redeemable 2002/04	-	8.0
£1, 12.0% Redeemable 2004	5.0	5.0
£1, 12.0% Redeemable 2005	2.0	2.0
£1, 11.2% Redeemable 2005/09	3.5	3.5
In five years or more:		
£1, 3.75% Redeemable 2012	0.3	0.3
£1, 4.25% Redeemable 2012	0.7	0.7
£1, 5.25% Redeemable 2012	0.7	0.7
£1, 3.5% Irredeemable	0.2	0.2
£1, 4.0% Irredeemable	0.8	0.8
£1, 5.0% Irredeemable	1.0	1.0
	<u>22.2</u>	<u>22.2</u>

The debenture stocks are secured by a floating charge on the company's business undertaking and on its assets.

**20. OBLIGATIONS UNDER FINANCE LEASES – GROUP AND COMPANY**

Obligations under hire purchase contracts and finance leases are as follows:

	<u>2002</u>	<u>2001</u>
	Appointed and aggregated basis	Appointed and aggregated basis
	£'m	£'m
Amounts due:		
Within one year	3.6	4.5
Between one and two years	2.5	3.9
Between two and five years	9.7	8.7
After five years	<u>75.5</u>	<u>75.4</u>
	91.3	92.5
Less:		
Finance charge allocated to future periods	<u>(33.3)</u>	<u>(36.0)</u>
	<u>58.0</u>	<u>56.5</u>
Disclosed as due:		
Within one year (note 16)	3.6	4.5
After more than one year (note 17)	<u>54.4</u>	<u>52.0</u>
	<u>58.0</u>	<u>56.5</u>

**21. AMOUNTS DUE TO OTHER GROUP COMPANIES**

Amounts due to other group companies relate to loans repayable as follows:

	2002		2001	
	Group	Company Appointed and aggregated basis	Group	Company Appointed and aggregated basis
	£'m	£'m	£'m	£'m
Within one year	-	-	134.8	134.8
Between one and two years	-	-	-	-
Between two and five years	-	-	-	-
After five years	471.2	861.5	490.4	579.8
	<u>471.2</u>	<u>861.5</u>	<u>625.2</u>	<u>714.6</u>

£47.2m is owed to a subsidiary undertaking of the group, Newcastle & Gateshead Water plc, in the form of an unsecured loan note repayable, at par, otherwise than by instalments and is subject to interest at an agreed rate of 0%. The company may exercise an option to repay the loan note at any time, also at par, subject to three months notice in writing. At present there is no intention to repay, therefore it has been classified as being due in five years or more.

£42.2m is owed to a subsidiary undertaking of the group, Suffolk Water plc, in the form of an unsecured loan note repayable, at par, otherwise than by instalments and is subject to interest at an agreed rate of 0%. The company may exercise an option to repay the loan note at anytime, also at par, subject to three months notice in writing. At present there is no intention to repay, therefore it has been classified as being due in five years or more.

£119.5m is owed to a fellow subsidiary, North East Water plc, in the form of an unsecured loan note repayable, at par, otherwise than by instalments after more than 5 years and is subject to an interest rate linked to LIBOR. The company may exercise an option to repay the loan note at any time, also at par, subject to three months notice in writing. At present there is no intention to repay, therefore it has been classified as being due in five years or more.

£351.7m is owed to the immediate parent company, Ondeo Services UK plc. Ondeo Services UK plc issued £200.0m Guaranteed Eurobonds in February 1998 and issued a further £150.0m Guaranteed Eurobonds in September 2001, maturing 6 February 2023, with an annual coupon of 6.875%. The issues were guaranteed by the company who received the issue proceeds by way of inter-company loans of £194.2m and £156.2m respectively. Finance costs allocated during the year amounted to £0.2m (December 2000: £0.2m).

£300.9m is owed to Northumbrian Water Finance plc, a subsidiary undertaking of the group. Northumbrian Water Finance plc issued £300.0m Guaranteed Eurobonds during the year, maturing October 2017, with an annual coupon of 6.0%. The issue was guaranteed by Northumbrian Water Limited who received the issue proceeds by way of an inter company loan.

At 31 March 2001 £176.0m was owed to a fellow subsidiary, Essex and Suffolk Water plc, in the form of an unsecured loan note repayable, at par. At that time there was no intention to repay and the loan was therefore classified as being due in five years or more. In March 2002, the company exercised its option to repay the loan note at any time, also at par.

**22. PROVISIONS FOR LIABILITIES AND CHARGES – GROUP AND COMPANY**

	2002			2001		
	Appointed business	Non- appointed business	Aggregated basis	Appointed business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Infrastructure renewals:						
At 1 April	2.6	1.1	3.7	-	0.9	0.9
Transferred from Essex & Suffolk Water plc	-	-	-	(0.4)	-	(0.4)
Transferred from profit and loss account	33.0	0.1	33.1	32.9	0.2	33.1
Utilised during the year (note 4b)	(34.7)	-	(34.7)	(29.9)	-	(29.9)
At 31 March	0.9	1.2	2.1	2.6	1.1	3.7
Reorganisation/ restructuring provision:						
At 1 April	5.9	(0.1)	5.8	7.0	-	7.0
Transferred from Essex & Suffolk Water plc	-	-	-	0.1	-	0.1
Utilised during the year	(0.6)	0.1	(0.5)	(3.2)	(0.1)	(3.3)
Provided in the year	0.4	-	0.4	2.0	-	2.0
At 31 March	5.7	-	5.7	5.9	(0.1)	5.8
Pension provision:						
As at 1 April	8.7	-	8.7	8.7	-	8.7
Utilised during the year	(0.6)	-	(0.6)	-	-	-
At 31 March	8.1	-	8.1	8.7	-	8.7
Deferred tax:						
As at 1 April	142.5	3.9	146.4	102.5	3.7	106.2
Movement in the period (note 9a)	(12.9)	-	(12.9)	40.0	0.2	40.2
At 31 March	129.6	3.9	133.5	142.5	3.9	146.4
Closing balance	144.3	5.1	149.4	159.7	4.9	164.6

The reorganisation provision remaining at the end of the year incorporates outstanding pension contributions for staff who left the business on early retirement terms as part of voluntary severance schemes in 1998 and 1999 and outstanding severance and pension payments relating to the additional provision made in the current year. The redundancy component of the provision will be paid within twelve months of the balance sheet date, and the pension augmentation component will be paid or amortised following the recommendations of the actuaries of the pension schemes in which the individuals concerned belong.

The pension provision represents amounts provided in respect of pension contributions for staff leaving the business as part of voluntary severance schemes prior to 1998. The company's actuary has assessed that the company is not required to make cash payments to fund these contributions. Accordingly the provision is being released over the average remaining service life of current employees.

**22. PROVISIONS FOR LIABILITIES AND CHARGES – GROUP AND COMPANY (continued)**

The provision for deferred tax comprises:

	2002			2001 (as restated)		
	Appointed business	Non- appointed business	Aggregated basis	Appointed business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Accelerated capital allowances	384.0	15.8	399.8	358.4	15.7	374.1
Other timing differences	(17.4)	(0.5)	(17.9)	(19.6)	(0.5)	(20.1)
Undiscounted provision for deferred tax	366.6	15.3	381.9	338.8	15.2	354.0
Discount	(237.0)	(11.4)	(248.4)	(196.3)	(11.3)	(207.6)
Discounted provision for deferred tax	129.6	3.9	133.5	142.5	3.9	146.4

**23. ACCRUALS AND DEFERRED INCOME – GROUP AND COMPANY**

	2002			2001		
	Appointed business	Non- appointed business	Aggregated basis	Appointed business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Non infrastructure capital grants and contributions:						
At 1 April	32.7	0.6	33.3	31.0	0.6	31.6
Additions	3.6	-	3.6	3.3	-	3.3
Amortised during the year	(3.3)	(0.1)	(3.4)	(1.6)	-	(1.6)
At 31 March	33.0	0.5	33.5	32.7	0.6	33.3

**24. CALLED UP SHARE CAPITAL – GROUP AND COMPANY**

	2002			2001		
	Appointed business	Non- appointed business	Aggregated basis	Appointed business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Authorised:						
122,650,000 Ordinary Shares at £1 each (March 2001: 122,650,000)	92.1	30.6	122.7	92.1	30.6	122.7
Allotted, called up and fully paid:						
122,650,000 Ordinary Shares of £1 each (March 2001: 122,650,000)	92.1	30.6	122.7	92.1	30.6	122.7

**25. PROFIT AND LOSS ACCOUNT – GROUP AND COMPANY**

	2002			2001 (as restated)		
	Appointed business	Non- appointed business	Aggregated basis	Appointed business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
At 1 April	694.2	51.0	745.2	818.4	63.3	881.7
Prior year adjustment (note 2)	-	-	-	(102.5)	(3.7)	(106.2)
At 1 April restated	694.2	51.0	745.2	715.9	59.6	775.5
Profit/(loss) retained for the year	27.4	(4.6)	22.8	(21.7)	(8.6)	(30.3)
At 31 March	721.6	46.4	768.0	694.2	51.0	745.2

As permitted by Section 230 of the Companies Act 1985, the company's profit and loss account has not been included in these financial statements. The profit for the financial year of £106.9m (March 2001: £46.7m – as restated) relates to the operations of the company.

**26. RECONCILIATION OF MOVEMENTS IN EQUITY SHAREHOLDERS' FUNDS – GROUP AND COMPANY**

	2002			2001 (as restated)		
	Appointed business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Profit for the financial year	100.2	6.7	106.9	43.3	3.4	46.7
Dividends	(72.8)	(11.3)	(84.1)	(65.0)	(12.0)	(77.0)
Net additions to /(deductions from) equity shareholders' funds	27.4	(4.6)	22.8	(21.7)	(8.6)	(30.3)
Opening equity shareholders' funds	786.3	81.6	867.9	910.5	93.9	1,004.4
Prior year adjustment (note 2)	-	-	-	(102.5)	(3.7)	(106.2)
Closing equity shareholders' funds	813.7	77.0	890.7	786.3	81.6	867.9

**27. COMMITMENTS AND CONTINGENT LIABILITIES – GROUP AND COMPANY**

(a) Capital expenditure:

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Expenditure contracted for	<u>67.2</u>	<u>-</u>	<u>67.2</u>	<u>33.0</u>	<u>0.4</u>	<u>33.4</u>

(b) Lease commitments:

The company and 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:-

	2002			2001		
	Appointe d business	Non- appointed business	Aggregated basis	Appointe d business	Non- appointed business	Aggregated basis
	£'m	£'m	£'m	£'m	£'m	£'m
Land and buildings:						
Leases which expire:						
Within one year	0.4	-	0.4	0.3	-	0.3
In five years or more	0.2	-	0.2	0.4	-	0.4
	<u>0.6</u>	<u>-</u>	<u>0.6</u>	<u>0.7</u>	<u>-</u>	<u>0.7</u>
Other:						
Leases which expire:						
Within one year	0.5	-	0.5	0.2	-	0.2
Between two and five years	-	-	-	0.8	-	0.8
	<u>0.5</u>	<u>-</u>	<u>0.5</u>	<u>1.0</u>	<u>-</u>	<u>1.0</u>

## 28. PENSIONS

Ondeo Services UK plc operates a funded defined benefit pension scheme, providing benefits based on final pensionable remuneration to 2,304 employees. The Scheme, named the Northumbrian Lyonnaise Pension Scheme, comprises three unitised sections – the WPS section, LUKPS (North) section and LUKPS (South) section.

The assets of the Scheme are held separately from those of the Ondeo Services UK plc in independently administered funds.

The most recent actuarial valuation of the Scheme was at 31 December 1998. At that date the market value of the assets amounted to £416.2m in aggregate. The 1998 valuation disclosed that the combined value of the assets represented 114% of the value of the accrued liabilities.

The following table sets out the contributions agreed based on the 31 December 1998 valuations:

<b>Section</b>	<b>South</b>	<b>North</b>	<b>WPS</b>
Members' contributions	5%	5%	6%
Employer's contributions	Nil	6.3%	17.2%

The company contribution rate was assessed using the Projected Unit Method and the following actuarial assumptions:

-

<b>Investment Return</b>	
Pre Retirement	6.2%
Post Retirement	5.7%
<b>Pay Increases</b>	
for 5 years after valuation date	3.8%
thereafter	4.3%
<b>Pension Increases</b>	2.8%
<b>Price Inflation</b>	2.8%

The actuaries are currently undertaking the next valuation, which was due at 31 December 2001.

Under the transitional provisions of FRS 17 "Retirement benefits" additional disclosures regarding the group defined benefit pension scheme are required. In accordance with FRS 17, the company will account for its contributions to the Scheme as if it were a defined contribution scheme because it is not possible to identify the company's share of the net assets and liabilities in the Scheme on a consistent and reasonable basis.

The latest actuarial valuation of the Scheme, prepared for the purposes of making the transitional disclosures in accordance with FRS 17 in the consolidated financial statements of the parent company, shows a surplus of £63.0m. Further details of this valuation can be found in the consolidated financial statements of the parent company as at 31 December 2001.

Ondeo Services UK plc also participates in the Water Mirror Image Pension Scheme and the Employer's contribution has been assessed and paid in accordance with the advice of an independent actuary. This Scheme provides a defined benefit pension arrangement for 56 employees. The last actuarial valuation was carried out as at 31 March 2001. At that date the Scheme assets amounted to £21.8m and the assets represented 103% of the value of the accrued liabilities.

The Northumbrian Water Group Personal Pension Plan provides defined contribution benefits to 651 employees.



**29. INFORMATION IN RELATION TO ALLOCATIONS AND APPORTIONMENTS**

The appointed and non-appointed businesses operate separate accounting ledgers including sales and purchase ledgers. Turnover, operating costs, assets and liabilities are taken directly from these ledgers.

Overhead costs incurred in the appointed business which relate to the non-appointed business have been allocated using an activity based approach to comply with Regulatory Accounting Guideline No 5.

Interest has been allocated between the appointed and non-appointed businesses on the basis of actual cash balances held by these businesses during the year at market rates. Capital costs and the related depreciation charges are specifically identifiable to the appropriate business and service.

Turnover is separately recorded between water services and sewerage services and therefore no apportionment has been necessary. Operating costs have been allocated between water and sewerage services in accordance with the guidance set out in Regulatory Accounting Guideline No 4.

**30. RELATED PARTY DISCLOSURES**

The company is a wholly owned subsidiary of Ondeo Services UK plc which produces publicly available financial statements which include the results of the company. Consequently the company is exempt under the terms of Financial Reporting Standard No 8 “Related Party Disclosures” from disclosing transactions with other members of the group headed by Ondeo Services UK plc.

Transactions with other members of the group headed by Suez S.A. outside of the Ondeo Services UK, comprised purchases of £17.0m (31 March 2001: £27.7m) and sales of £1.6m (31 March 2001: £1.1m). As at 31 March 2002, the amount due to these companies was £8.2m (31 March 2001: £0.2m) and due from these companies was £1.4m (31 March 2001: £0.3m).

The companies with which Northumbrian Water Limited has had transactions during the year, included in the above balances, were as follows:

Macao Water Supply Company  
 Ondeo Degrémont  
 Ondeo Nalco  
 Ondeo Services S.A.  
 Safege  
 SITA Holdings UK Limited  
 Suez S.A.

**31. BILLING ON BEHALF OF WATER AND SEWERAGE COMPANIES**

The group bills and collects charges in respect of sewerage services in some of its area of supply on behalf of Anglian Water Services Limited and Thames Water Utilities Limited who are responsible for those services.

The group receives commission income for those services, which is included in other operating income. Payments on account from customers due to Anglian Water Services and Thames Water Utilities Limited are included in creditors falling due within one year.

**32. ULTIMATE PARENT COMPANY**

The ultimate parent company and controlling party of the company is Suez S.A., incorporated in France. The largest group which consolidates the results of the company is Suez S.A. and copies of the consolidated accounts are available to the public from Suez S.A., 16 rue de la Ville l’Eveque, 75383, Paris, France.

The smallest group which consolidates the results of the company is that of which Ondeo Services UK plc (formerly Northumbrian Water Group plc) is the parent. Copies of the consolidated accounts may be obtained from Ondeo Services UK plc, Northumbria House, Abbey Road, Pity Me, Durham DH1 5FJ. Ondeo Services UK plc is registered in England and Wales.

**CURRENT COST PROFIT AND LOSS ACCOUNT**  
**For the year ended 31 March 2002**

		2002	2001 (as restated)
	Note	£'m	£'m
Turnover	2	422.3	407.3
Operating costs	3	(186.0)	(179.2)
Capital maintenance costs	3	(109.1)	(106.3)
Profit on sale of fixed assets	2	0.6	0.2
<b>OPERATING PROFIT BEFORE EXCEPTIONAL ITEMS</b>		<b>127.8</b>	<b>122.0</b>
Exceptional items:			
Operating costs	3	-	(2.0)
<b>OPERATING PROFIT AFTER EXCEPTIONAL ITEMS</b>		<b>127.8</b>	<b>120.0</b>
Working capital adjustment	6	0.5	0.5
<b>OPERATING PROFIT</b>		<b>128.3</b>	<b>120.5</b>
Net interest payable		(67.4)	(64.4)
Financing adjustment	6	15.1	24.0
<b>PROFIT BEFORE TAXATION</b>		<b>76.0</b>	<b>80.1</b>
Taxation:			
Current tax		(0.1)	(6.1)
Deferred tax		12.9	(40.0)
<b>PROFIT ATTRIBUTABLE TO SHAREHOLDERS</b>		<b>88.8</b>	<b>34.0</b>
Dividends		(72.8)	(65.0)
<b>RETAINED PROFIT</b>		<b>16.0</b>	<b>(31.0)</b>

The accompanying notes are an integral part of this profit and loss account.

**CURRENT COST BALANCE SHEET**  
**At 31 March 2002**

	Note	2002	2001 (as restated)
		£'m	£'m
<b>FIXED ASSETS</b>			
Tangible fixed assets	4	11,340.1	10,943.4
Grants and contributions		(58.7)	(57.6)
		<u>11,281.4</u>	<u>10,885.8</u>
Working capital	5	(16.2)	(39.4)
<b>NET OPERATING ASSETS</b>			
		11,265.2	10,846.4
Investment		89.4	89.4
Non trade debtors		7.5	12.2
Non trade creditors due within one year		(33.1)	(169.3)
Creditors due after more than one year		(1,227.1)	(973.4)
Provisions for liabilities and charges – deferred tax		(129.6)	(142.5)
Dividends payable		(36.8)	(34.2)
<b>NET ASSETS EMPLOYED</b>			
		<u>9,935.5</u>	<u>9,628.6</u>
<b>CAPITAL AND RESERVES</b>			
Called up share capital		92.1	92.1
Profit and loss account		424.1	408.1
Current cost reserve	6	9,419.3	9,128.4
<b>TOTAL CAPITAL AND RESERVES</b>			
		<u>9,935.5</u>	<u>9,628.6</u>

The accompanying notes are an integral part of this balance sheet.

**CURRENT COST CASH FLOW STATEMENT**  
**For the year ended 31 March 2002**

	Note	2002	2001
		£'m	£'m
NET CASH INFLOW FROM CONTINUING OPERATING ACTIVITIES	7	223.9	222.8
<b>Returns on investments and servicing of finance</b>			
Interest received		3.9	5.3
Interest paid		(64.3)	(62.8)
Interest element of finance lease rentals		(0.4)	(2.4)
Net cash outflow from returns on investments and servicing of finance		(60.8)	(59.9)
<b>Taxation</b>			
United Kingdom corporation tax paid		(6.5)	(24.1)
Net cash outflow from taxation		(6.5)	(24.1)
<b>Capital expenditure and financial investment</b>			
Purchase of tangible fixed assets		(157.8)	(198.4)
Infrastructure renewals expenditure		(34.7)	(29.9)
Grants, contributions and connection charges		8.6	8.9
Sale of tangible fixed assets		0.8	0.2
Purchase of business		-	(0.7)
Net cash outflow from capital expenditure and financial investment		(183.1)	(219.9)
<b>Equity dividends paid</b>		(70.2)	(66.6)
CASH OUTFLOW BEFORE MANAGEMENT OF LIQUID RESOURCES AND FINANCING		(96.7)	(147.7)
<b>Management of liquid resources</b>			
Purchase of short term deposits		(1,028.9)	-
Sale of short term deposits		995.4	32.9
Net cash (outflow)/inflow from management of liquid resources		(33.5)	32.9
<b>Financing</b>			
New loans		457.7	134.8
New leases		0.8	1.1
Loan repayment		(324.3)	(10.9)
Capital element of finance lease rental payments		(4.0)	(3.5)
Net cash inflow from financing		130.2	121.5
INCREASE IN CASH IN THE YEAR		-	6.7

The accompanying notes are an integral part of this cash flow statement.

## NOTES TO THE CURRENT COST FINANCIAL INFORMATION

### For the year ended 31 March 2002

#### 1. CURRENT COST ACCOUNTING POLICIES

The accounting policies used are the same as those adopted in the historical cost accounts except as set out below. This financial information has been prepared for the appointed business of Northumbrian Water Limited in accordance with guidance issued by the Director General of Water Services for modified real time financial statements suitable for regulation in the water industry. They measure profitability on the basis of real financial capital maintenance in the context of assets which are valued at their current cost value to the business.

##### (a) Tangible fixed assets

Assets in operational use are valued at the replacement cost of their operating capability. To the extent that the regulatory regime does not allow such assets to earn a return high enough to justify that value, no adjustment is made in arriving at the replacement cost. No provision is made for the possible funding of future replacements of assets by contributions from third parties and, to the extent that some of those assets would on replacement be so funded, replacement cost again differs from value to the business. Redundant assets are valued at their recoverable amounts.

A process of continuing refinement of the Asset Management Plan (AMP), based on serviceability, will result in adjustments to the existing valuation of assets at the end of the regulatory review period. In intervening years, values are restated to take account of changes in the general level of inflation as measured by changes in the Retail Price Index (RPI) over the year.

##### (i) Land and Buildings

Non-specialised operational properties are valued on the basis of open market value for existing use. Specialised operational properties are valued at the lower of depreciated replacement cost and recoverable amount.

##### (ii) Infrastructure assets

Mains, sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls are valued at replacement cost determined principally on the basis of data provided by the AMP.

##### (iii) Other fixed assets

All other fixed assets are valued periodically at depreciated replacement cost.

##### (iv) Surplus land

Surplus land is valued at recoverable amount taking into account that part of any proceeds to be passed on to customers under Condition B of the License.

##### (v) Government grants and contributions

Government grants and contributions are revalued to take account of changes in the general level of inflation as measured by changes in the RPI over the year.

##### (b) Real financial capital maintenance adjustments

The real financial capital maintenance adjustments are calculated by applying depreciation to the current cost value of fixed assets.

##### (c) Working capital adjustment

The working capital adjustment is calculated by applying the change in the RPI over the year to the opening balance of working capital.

##### (d) Financing adjustment

The financing adjustment is calculated by applying the RPI change over the year to the opening balance of net finance which comprises all monetary assets and liabilities in the balance sheet except those included in working capital.

##### (e) Infrastructure renewals accrual/prepayment adjustment

The infrastructure renewals accrual/prepayment adjustment is calculated by applying the RPI change over the year to the opening balance of the renewals accrual/prepayment.

**2. TURNOVER**

	2002			2001		
	Water services £'m	Sewerage services £'m	Appointed business £'m	Water services £'m	Sewerage services £'m	Appointed business £'m
Measured	59.4	36.9	96.3	55.6	40.7	96.3
Unmeasured	145.0	117.3	262.3	146.5	115.3	261.8
Trade effluent	-	4.2	4.2	-	6.1	6.1
Large user revenues	22.2	7.5	29.7	22.8	-	22.8
Other sources	4.9	14.4	19.3	7.3	10.8	18.1
Third party services	10.4	0.1	10.5	-	-	-
<b>Total turnover</b>	<b>241.9</b>	<b>180.4</b>	<b>422.3</b>	<b>232.2</b>	<b>172.9</b>	<b>405.1</b>
Operating income:						
Current cost profit on disposal of fixed assets	0.4	0.2	0.6	0.1	0.1	0.2
Other operating income	-	-	-	2.2	-	2.2
	<b>0.4</b>	<b>0.2</b>	<b>0.6</b>	<b>2.3</b>	<b>0.1</b>	<b>2.4</b>
<b>Working capital adjustment</b>	<b>0.3</b>	<b>0.2</b>	<b>0.5</b>	<b>0.3</b>	<b>0.2</b>	<b>0.5</b>

## 3. OPERATING COSTS

2002

## Activity cost table

	Service analysis							Business analysis			
	Water supply			Sewerage services				Customer Services	Scientific Services	Cost of Regulation	
	Resources & Treatment	Distribution	Water Supply Subtotal	Sewerage	Sewage Treatment	Sludge Treatment & Disposal	Sewage T & D Subtotal				Sewerage Service Subtotal
£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m		
<b>Direct Costs</b>											
Employment costs	6.3	9.2	<b>15.5</b>	3.2	3.0	4.4	7.4	<b>10.6</b>			
Power	3.8	4.1	<b>7.9</b>	1.8	4.3	3.2	7.5	<b>9.3</b>			
Hired & contracted services	1.5	3.2	<b>4.7</b>	0.7	1.4	8.4	9.8	<b>10.5</b>			
Associated companies	0.4	-	<b>0.4</b>	0.1	0.4	0.3	0.7	<b>0.8</b>			
Materials and consumables	4.7	1.1	<b>5.8</b>	0.3	1.1	2.4	3.5	<b>3.8</b>			
Service charges (EA)	14.9	-	<b>14.9</b>	1.1	1.2	-	1.2	<b>2.3</b>			
Bulk supply imports	1.1	-	<b>1.1</b>	-	-	-	-	<b>-</b>			
Other direct costs	0.4	3.3	<b>3.7</b>	0.7	0.1	0.1	0.2	<b>0.9</b>			
<b>Total direct costs</b>	<b>33.1</b>	<b>20.9</b>	<b>54.0</b>	<b>7.9</b>	<b>11.5</b>	<b>18.8</b>	<b>30.3</b>	<b>38.2</b>	<b>9.2</b>	<b>8.1</b>	<b>1.5</b>
General and support expenditure	10.2	10.1	<b>20.3</b>	2.8	5.2	4.2	9.4	<b>12.2</b>	4.0	1.3	0.2
<b>Functional expenditure</b>	<b>43.3</b>	<b>31.0</b>	<b>74.3</b>	<b>10.7</b>	<b>16.7</b>	<b>23.0</b>	<b>39.7</b>	<b>50.4</b>	<b>13.2</b>	<b>9.4</b>	<b>1.7</b>
Business analysis			<b>15.9</b>					<b>8.4</b>			
<b>Total business activities c/fwd</b>			<b>90.2</b>					<b>58.8</b>			

**3. OPERATING COSTS (continued)**

2002

**Activity cost table**

	Service Analysis							
	Water supply			Sewerage services				
	Resources & Treatment	Distribution	Water Supply Subtotal	Sewerage	Sewage Treatment	Sludge Treatment & Disposal	Sewage T & D Subtotal	Sewerage Service Subtotal
£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	
<b>Total business activities b/fwd</b>			<b>90.2</b>					<b>58.8</b>
Rates			14.0					2.8
Doubtful debts			5.5					5.2
<b>Total opex less third party services</b>			<b>109.7</b>					<b>66.8</b>
Third party services – opex			9.5					-
<b>Total operating expenditure</b>			<b>119.2</b>					<b>66.8</b>
<b>Capital costs</b>								
Infrastructure renewal expenditure	1.3	24.0	25.3	9.4	-	-	-	9.4
Movement in infrastructure renewals accrual/prepayment	-	(2.0)	(2.0)	0.3	-	-	-	0.3
Current cost depreciation (allocated)	18.4	7.1	25.5	5.9	29.3	4.9	34.2	40.1
Business activities current cost depreciation (non allocated)			8.0					2.5
<b>Total capital maintenance</b>			<b>56.8</b>					<b>52.3</b>
<b>Total operating costs</b>			<b>176.0</b>					<b>119.1</b>
<b>CCA (MEA) values</b>								
Service activities			44.0					22.7
Business activities			5,367.4					5,906.0
Service totals			<b>5,411.4</b>					<b>5,928.7</b>



## SECTION C – CURRENT COST FINANCIAL INFORMATION FOR THE APPOINTED BUSINESS ONLY

**3. OPERATING COSTS (continued)**

2001

**Activity cost table**

	<b>Service analysis</b>							<b>Business analysis</b>			
	<b>Water supply</b>			<b>Sewerage services</b>				<b>Customer Services</b>	<b>Scientific Services</b>	<b>Cost of Regulation</b>	
	<b>Resources &amp; Treatment</b>	<b>Distribution</b>	<b>Water Supply Subtotal</b>	<b>Sewerage</b>	<b>Sewage Treatment</b>	<b>Sludge Treatment &amp; Disposal</b>	<b>Sewage T &amp; D Subtotal</b>				<b>Sewerage Service Subtotal</b>
£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m		
<b>Direct Costs</b>											
Employment costs	6.6	8.9	<b>15.5</b>	3.0	2.7	2.6	5.3	<b>8.3</b>			
Power	3.3	3.8	<b>7.1</b>	1.5	2.5	1.5	4.0	<b>5.5</b>			
Hired & contracted services	1.8	2.7	<b>4.5</b>	0.6	0.4	4.1	4.5	<b>5.1</b>			
Associated companies	0.1	0.1	<b>0.2</b>	0.1	0.4	0.2	0.6	<b>0.7</b>			
Materials and consumables	4.8	1.3	<b>6.1</b>	0.1	0.7	1.0	1.7	<b>1.8</b>			
Service charges (EA)	14.9	-	<b>14.9</b>	1.1	1.0	-	1.0	<b>2.1</b>			
Bulk supply imports	1.2	-	<b>1.2</b>	-	-	-	-	<b>-</b>			
Other direct costs	0.2	2.2	<b>2.4</b>	0.6	0.1	-	0.1	<b>0.7</b>			
<b>Total direct costs</b>	<b>32.9</b>	<b>19.0</b>	<b>51.9</b>	<b>7.0</b>	<b>7.8</b>	<b>9.4</b>	<b>17.2</b>	<b>24.2</b>	<b>14.2</b>	<b>7.0</b>	<b>1.6</b>
General and support expenditure	12.7	9.1	<b>21.8</b>	2.8	7.6	2.7	10.3	<b>13.1</b>	4.5	1.2	0.5
<b>Functional expenditure</b>	<b>45.6</b>	<b>28.1</b>	<b>73.7</b>	<b>9.8</b>	<b>15.4</b>	<b>12.1</b>	<b>27.5</b>	<b>37.3</b>	<b>18.7</b>	<b>8.2</b>	<b>2.1</b>
Business analysis			<b>19.2</b>					<b>9.8</b>			
<b>Total business activities c/fwd</b>			<b>92.9</b>					<b>47.1</b>			

**3. OPERATING COSTS (continued)**

2001

**Activity cost table**

	<b>Service Analysis</b>								
	<b>Water supply</b>			<b>Sewerage services</b>					
	<b>Resources &amp; Treatment</b>	<b>Distribution</b>	<b>Water Supply Subtotal</b>	<b>Sewerage</b>	<b>Sewage Treatment</b>	<b>Sludge Treatment &amp; Disposal</b>	<b>Sewage T &amp; D Subtotal</b>	<b>Sewerage Service Subtotal</b>	
£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	
<b>Total business activities b/fwd</b>			<b>92.9</b>						<b>47.1</b>
Rates			<b>15.7</b>						<b>6.1</b>
Doubtful debts			<b>4.9</b>						<b>2.3</b>
Exceptional items			<b>1.5</b>						<b>0.5</b>
<b>Total opex less third party services</b>			<b>115.0</b>						<b>56.0</b>
Third party services – opex			<b>6.4</b>						<b>3.8</b>
<b>Total operating expenditure</b>			<b>121.4</b>						<b>59.8</b>
<b>Capital costs</b>									
Infrastructure renewal expenditure	1.1	18.2	<b>19.3</b>	9.8	0.8	-	0.8		<b>10.6</b>
Movement in infrastructure renewals accrual/prepayment	-	4.0	<b>4.0</b>	(1.0)	-	-	-		<b>(1.0)</b>
Current cost depreciation (allocated)	18.3	9.5	<b>27.8</b>	5.5	27.3	3.5	30.8		<b>36.3</b>
Business activities current cost depreciation (non allocated)			<b>6.6</b>						<b>2.7</b>
<b>Total capital maintenance</b>			<b>57.7</b>						<b>48.6</b>
<b>Total operating costs</b>			<b>179.1</b>						<b>108.4</b>
<b>CCA (MEA) values</b>									
Service activities			<b>5,069.1</b>						<b>5,813.2</b>
Business activities			<b>39.2</b>						<b>21.9</b>
<b>Service totals</b>			<b>5,108.3</b>						<b>5,835.1</b>

**4. TANGIBLE FIXED ASSETS**

Analysis by asset type

<b>Water Service</b>	Specialised	Non	Infrastructure	Other	Total
	operational assets	specialised properties	assets	tangible assets	
	£'m	£'m	£'m	£'m	£'m
Gross Replacement Cost:					
At 1 April 2001	1,446.5	60.2	4,310.3	95.7	5,912.7
RPI Adjustment	19.3	0.8	57.6	1.3	79.0
Disposals	(0.3)	-	-	-	(0.3)
Additions	59.5	0.2	27.8	7.2	94.7
Raw Water assets acquired	34.7	-	158.8	-	193.5
At 31 March 2002	1,559.7	61.2	4,554.5	104.2	6,279.6
Depreciation:					
At 1 April 2001	740.6	7.3	-	56.5	804.4
RPI Adjustment	9.9	0.1	-	0.8	10.8
Disposals	(0.1)	-	-	-	(0.1)
Charge for year	25.6	5.0	-	2.9	33.5
Raw Water assets acquired	19.6	-	-	-	19.6
At 31 March 2002	795.6	12.4	-	60.2	868.2
Net Book Value at 31 March 2002	764.1	48.8	4,554.5	44.0	5,411.4
Net Book Value at 31 March 2001	705.9	52.9	4,310.3	39.2	5,108.3

Analysis by asset type

<b>Sewerage Services</b>	Specialised	Non	Infrastructure	Other	Total
	operational assets	specialised properties	assets	tangible assets	
	£'m	£'m	£'m	£'m	£'m
Gross Replacement Cost:					
At 1 April 2001	2,051.5	14.3	4,903.5	51.6	7,020.9
RPI Adjustment	27.4	0.2	65.5	0.7	93.8
Disposals	-	-	-	-	-
Additions	47.4	-	6.9	3.9	58.2
At 31 March 2002	2,126.3	14.5	4,975.9	56.2	7,172.9
Depreciation:					
At 1 April 2001	1,155.1	1.0	-	29.7	1,185.8
RPI Adjustment	15.4	-	-	0.4	15.8
Disposals	-	-	-	-	-
Charge for year	40.1	(0.9)	-	3.4	42.6
At 31 March 2002	1,210.6	0.1	-	33.5	1,244.2
Net Book Value at 31 March 2002	915.7	14.4	4,975.9	22.7	5,928.7
Net Book Value at 31 March 2001	896.4	13.3	4,903.5	21.9	5,835.1

**4. TANGIBLE FIXED ASSETS (continued)**

Analysis by asset type

<b>Total</b>	Specialised operational assets	Non specialised properties	Infrastructure assets	Other tangible assets	Total
	£'m	£'m	£'m	£'m	£'m
Gross Replacement Cost:					
At 1 April 2001	3,498.0	74.5	9,213.8	147.3	12,933.6
RPI Adjustment	46.7	1.0	123.1	2.0	172.8
Disposals	(0.3)	-	-	-	(0.3)
Additions	106.9	0.2	34.7	11.1	152.9
Raw Water assets acquired	34.7	-	158.8	-	193.5
At 31 March 2002	3,686.0	75.7	9,530.4	160.4	13,452.5
Depreciation:					
At 1 April 2001	1,895.7	8.3	-	86.2	1,990.2
RPI Adjustment	25.3	0.1	-	1.2	26.6
Disposals	(0.1)	-	-	-	(0.1)
Charge for year	65.7	4.1	-	6.3	76.1
Raw Water assets acquired	19.6	-	-	-	19.6
At 31 March 2002	2,006.2	12.5	-	93.7	2,112.4
Net Book Value at 31 March 2002	1,679.8	63.2	9,530.4	66.7	11,340.1
Net Book Value at 31 March 2001	1,602.3	66.2	9,213.8	61.1	10,943.4

**5. WORKING CAPITAL**

	2002 £'m	2001 £'m
Stocks	2.5	2.2
Trade debtors	57.4	65.7
Working cash balances	49.9	16.2
Trade creditors	(3.1)	(4.2)
Short term capital creditors	(31.9)	(34.3)
Provisions for liabilities and charges	(0.9)	(2.6)
Other trade accruals	(54.4)	(43.1)
Trade payments in advance	29.7	14.7
Payroll related taxes and DSS contributions	(1.2)	(1.7)
Other trade creditors	(64.2)	(52.3)
At 31 March	(16.2)	(39.4)

**6. MOVEMENT ON CURRENT COST RESERVE**

	<u>2002</u>	<u>2001</u>
	£'m	£'m
At 1 April	9,128.4	7,628.3
Transferred from Essex & Suffolk Water plc	-	1,226.1
AMP adjustment	-	(27.0)
RPI Adjustments:		
Fixed assets	307.3	327.2
Working capital	(0.5)	(0.5)
Financing	(15.1)	(24.0)
Grants and contributions	(0.8)	(1.7)
	<u>9,419.3</u>	<u>9,128.4</u>
At 31 March	<u><u>9,419.3</u></u>	<u><u>9,128.4</u></u>

**7. NET CASH INFLOW FROM OPERATING ACTIVITIES**

	<u>2002</u>	<u>2001</u>
	£'m	£'m
Current cost operating profit	128.3	120.5
Additional current cost depreciation	27.0	33.8
Working capital adjustment	(0.5)	(0.5)
	<u>154.8</u>	<u>153.8</u>
Historical cost operating profit	154.8	153.8
Aggregate of historical cost adjusting items	69.1	69.0
	<u>223.9</u>	<u>222.8</u>
	<u><u>223.9</u></u>	<u><u>222.8</u></u>

**8. ANALYSIS OF NET DEBT**

	At 1 April 2001	Cash Flow	Other non cash changes	At 31 March 2002
	£'m	£'m	£'m	£'m
Cash in hand and at bank	16.2	-	-	16.2
Loans due after one year	(920.2)	(281.7)	30.7	(1171.2)
Loans due within one year	(148.3)	148.3	(30.6)	(30.6)
Finance leases	(56.5)	3.2	(4.7)	(58.0)
Current asset investment	-	33.5	-	33.5
	<u>(1,108.8)</u>	<u>(96.7)</u>	<u>(4.6)</u>	<u>(1,210.1)</u>
Total	<u><u>(1,108.8)</u></u>	<u><u>(96.7)</u></u>	<u><u>(4.6)</u></u>	<u><u>(1,210.1)</u></u>

**9. DISCLOSURE OF TRANSACTIONS WITH ASSOCIATES****Services supplied by the appointee to associated companies:**

Associate	Service	31.12.01 Turnover	Terms of Supply	2001/02 Value
		£'m		£'m
Analytical & Environmental Services Ltd	Rental of laboratories and service charges	10.7	Negotiated	0.3
Macao Water Supply Company	Secondees	10.3	Negotiated	0.1
Safege	Secondees	49.4	Negotiated	0.2
Ondeo Services S.A.	Secondees	3,873.0	Negotiated	1.3
Vehicle Leasing Services Ltd	Rental of garage and service charges	9.3	Negotiated	0.1

**Services supplied to the appointee by associated companies:**

Associate	Service	31.12.01 Turnover	Terms of Supply	2001/02 Value
		£'m		£'m
Analytical & Environmental Services Ltd	Sampling and analysis	10.7	No market	7.3
Coquettale Property Investment Ltd	Property management	1.6	Other market testing	0.1
Ondeo Degremont	Construction and engineering design	517.3	Competitive letting	9.2
Entec UK Limited	Engineering design consultancy	30.6	Competitive letting	3.6
Entec UK Limited	Engineering design consultancy	30.6	Other market testing	4.3
Entec UK Limited	Engineering design consultancy	30.6	No market	0.8
Fastflow Pipeline Services Ltd	Mains renewals, sewer repairs	16.4	Competitive letting	12.3
Imass Limited	System development	5.9	Competitive letting	0.5
Imass Limited	System development, training and maintenance support	5.9	Other market testing	0.1
Imass Limited	System development, training and maintenance support	5.9	No market	0.1
Ondeo Nalco	Polyelectrolyte trials	1,832.0	Other market testing	0.4
SITA Holdings UK Ltd	Waste disposal	3,286.0	Competitive tendering	0.3
SITA Holdings UK Ltd	Disposal of contaminated materials	3,286.0	Other market testing	0.2
Ondeo Services S.A.	Group research and development costs	3,873.0	No market	6.9
Vehicle Lease & Service Ltd	Maintenance and capital finance charge	9.3	Other market testing	5.2

**10. ROLLING SUMMARY: CURRENT COST PROFIT AND LOSS ACCOUNT**

	1997/98	1998/99	1999/00	2000/01	2001/02
	£'m	£'m	£'m	£'m	£'m
Turnover	353.8	365.4	375.8	412.8	422.3
Operating costs	(211.3)	(194.5)	(204.5)	(289.2)	(294.5)
Exceptional items	(2.7)	(2.5)	(8.9)	(2.0)	-
Working capital adjustment	0.8	(2.0)	(2.0)	0.5	0.5
Infrastructure renewals adjustment	0.1	-	-	-	-
Operating profit	140.7	166.4	160.4	122.1	128.3
Net interest	(28.4)	(35.8)	(36.7)	(65.3)	(67.4)
Financing adjustment	12.6	12.6	11.7	24.3	15.1
Profit before taxation	124.9	143.2	135.4	81.1	76.0
Taxation	(24.5)	(27.0)	(26.2)	(46.7)	12.8
Profit on ordinary activities	100.4	116.2	109.2	34.4	88.8
Dividends	(40.4)	(54.6)	(55.6)	(65.9)	(72.8)
Profit retained	60.0	61.6	53.6	(31.5)	16.0

The rolling summary financial information for prior years has been compiled in accordance with Regulatory Accounting Guideline No 1, "Accounting for current costs", with adjustments being made to reflect changes in the general level of inflation as measured by changes in the RPI.

The figures from 2000/01 include the full year results of the business of Northumbrian Water Limited and of that previously carried out by Essex & Suffolk Water plc.

**11. ROLLING SUMMARY: CURRENT COST BALANCE SHEET**

	31 March	31 March	31 March	31 March	31 March
	1998	1999	2000	2001	2002
	£'m	£'m	£'m	£'m	£'m
Tangible fixed assets	9,109.6	9,225.0	9,389.6	11,089.6	11,340.1
Third party contributions since 89/90	(54.0)	(54.9)	(56.6)	(58.4)	(58.7)
Working capital	98.4	112.7	(17.8)	(39.9)	(16.2)
Net operating assets	9,154.0	9,282.8	9,315.2	10,991.3	11,265.2
Cash and investments	51.3	50.2	49.4	90.6	89.4
Non trade debtors	26.1	32.0	22.1	12.4	7.5
Non trade creditors	(26.4)	(45.7)	(36.9)	(171.6)	(33.1)
Creditors due after > 1 year	(674.4)	(713.0)	(689.4)	(986.4)	(1,227.1)
Provisions for liabilities and charges	-	-	-	(144.4)	(129.6)
Dividends payable	(13.4)	(27.4)	(27.1)	(34.7)	(36.8)
Net assets employed	8,517.2	8,578.9	8,633.3	9,757.2	9,935.5
Called up share capital	100.0	97.9	96.3	93.3	92.1
Profit and loss account	469.4	521.4	566.1	413.5	424.1
Current cost reserve	7,947.8	7,959.6	7,970.9	9,250.4	9,419.3
	8,517.2	8,578.9	8,633.3	9,757.2	9,935.5

The rolling summary financial information for prior years has been compiled in accordance with Regulatory Accounting Guideline No 1, "Accounting for current costs", with adjustments being made to reflect changes in the general level of inflation as measured by changes in the RPI.

The figures from 2000/01 include the impact of the transfer of assets and liabilities to Northumbrian Water Limited from Essex & Suffolk Water plc on 1 April 2001.

**12. REGULATORY CAPITAL VALUE AT 2001/2002 PRICES**

	<u>2001/2002</u>
	£'m
Opening regulatory capital value	2,052.0
Capital expenditure (excluding IRE)	159.0
Infrastructure renewals expenditure	34.0
Infrastructure renewals charge	(28.0)
Grants and contributions	(7.0)
Current cost depreciation	(75.0)
Out-performance of regulatory assumptions (5 years in arrears)	(85.0)
Closing regulatory capital value	<u>2,049.0</u>
Average year regulatory capital value	<u>2,043.0</u>

The table shows the regulatory capital value used by Ofwat in setting the price limits for 2001/2002. The numbers do not add due to rounding.

The numbers included above from capital expenditure to current cost depreciation (inclusive) are taken from Ofwat's final determination published in November 1999, and therefore do not agree exactly with the corresponding actual numbers in these financial statements.

Differences from the actual capital expenditure, infrastructure renewals expenditure, infrastructure renewals charge, grants and contributions and depreciation will not affect price limits in the current period. Capital efficiencies will be taken into account in the calculation for the next periodic review.

The opening regulatory capital value for 2001/2002 includes £37.0m in relation to the assets transferred from the non-appointed business at 1 April 2001 relating to the non potable water business.



**STATEMENT OF DIRECTORS' RESPONSIBILITIES**  
**For the year ended 31 March 2002**

The directors are responsible under Condition F of the Instrument of Appointment by the Secretary of State for the Environment of the company as a water and sewerage undertaker under the Water Industry Act 1991 for:

- (a) ensuring that proper accounting records are maintained by the Appointee to enable compliance with the requirements of Condition F and having regard also to the terms of guidelines notified by the Director General of Water Services ("the Director") to the Appointee from time to time;
- (b) preparing on a consistent basis for each financial year regulatory financial statements in accordance with Condition F, having regard also to the terms of guidelines notified by the Director from time to time, which so far as is reasonably practicable have the same content as the annual financial statements of the Appointee prepared under the Companies Act 1985 and which are prepared in accordance with the formats, accounting policies and principles which apply to those financial statements;
- (c) preparing financial statements on a current cost basis in respect of the same accounting period in accordance with guidelines issued by the Director from time to time;
- (d) preparing such other financial and related information as is required by Condition F having regard also to the terms of guidelines issued by the Director from time to time.

ON BEHALF OF THE BOARD

M Parker  
Company Secretary

10th July 2002

# **INDEPENDENT AUDITORS' REPORT TO THE DIRECTOR GENERAL OF WATER SERVICES**

We have audited the financial statements of Northumbrian Water Limited for the year ended 31 March 2002, which include the historic cost accounts (Section B), comprising the profit and loss account, balance sheet, cash flow statement and related notes numbered 1 to 32, and the current cost accounts (Section C), comprising the profit and loss account, balance sheet, cash flow statement and related notes numbered 1 to 12. These financial statements have been prepared under the accounting policies set out therein.

## **Respective responsibilities of directors and auditors**

As described on pages 5 and 55 the Company's directors are responsible for the preparation of the historical cost and current cost financial information ("the Financial Statements"). It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion to you. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board and by our profession's ethical guidance.

## **Basis of opinion**

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

In conjunction with our audit of the historical cost financial statements we have performed an examination, on a test basis, of the supplementary regulatory current cost financial information to determine their consistency with the historic cost financial statements as appropriate, and their compliance with relevant regulatory accounting guidelines. We have also performed an assessment of the significant estimates and judgements made by the directors in their preparation of the supplementary statements.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

## **Audit opinion**

### **i) Unqualified opinion in respect of regulatory compliance**

In our opinion the financial statements contain the information for the year to 31 March 2002 required to be published and submitted to you by Northumbrian Water Limited to comply with Condition F of the Instrument of Appointment granted by the Secretary of State for the Environment of the company as a water and sewerage undertaker under the Water Industry Act 1991, as modified in respect of infrastructure renewals accounting by RD15/99, dated 21 April 1999, "Regulatory Accounts for 1998/9 Reporting Requirements – RAG 3.04."

In respect of this information, we report that in our opinion:

- a) proper accounting records have been kept by the Appointee as required by paragraph 3 of Condition F of the Instrument;
- b) the information is in agreement with the Appointee's accounting records, complies with the requirements of Condition F of the Instrument, as modified in respect of infrastructure renewals accounting by RD15/99, dated 21 April 1999, "Regulatory Accounts for 1998/9 Reporting Requirements – RAG 3.04" and has been properly prepared in accordance with the Regulatory Accounting Guidelines issued by the Office of Water Services; and
- c) the current cost financial information on pages 40 to 54 has been properly prepared in accordance with Regulatory Accounting Guideline No 1, "Accounting for current cost", issued in May 1992 by the Office of Water Services.

**INDEPENDENT AUDITORS' REPORT TO  
THE DIRECTOR GENERAL OF WATER SERVICES (continued)**

**ii) Qualified opinion on historic cost financial statements in respect of FRS12 and FRS15**

- d) As explained in note 1 (d) (i), in order to comply with the instructions of the Director General of Water Services, the financial statements do not comply with Financial Reporting Standard No.12 ("FRS12") and Financial Reporting Standard No.15 ("FRS15") in respect of infrastructure renewals accounting. Adoption of FRS12 and FRS15 would have required restatement of the cost and accumulated depreciation of infrastructure fixed assets to reflect infrastructure renewals expenditure, depreciation and retirement of assets since the year ended 31 March 1989, when renewals accounting was first adopted. The non-compliance with FRS12 and FRS15 in respect of infrastructure renewals accounting would have had no effect on the profit and loss accounts for the years ended 31 March 2001 and 31 March 2002, other than to reclassify the infrastructure renewals charge as depreciation.

Except for non-compliance with FRS12 and FRS15 in respect of infrastructure renewals accounting, in our opinion, the historical cost financial statements on pages 6 to 39 give, under the historical cost convention, a true and fair view of the revenues, costs, assets and liabilities of the Appointee and its Appointed Business.

Arthur Andersen  
Chartered Accountants and Registered Auditors

Pearl Assurance House  
7 New Bridge Street  
Newcastle Upon Tyne  
NE1 8BQ

10th July 2002