

REGISTRATION NO. 2366670

SOUTHERN WATER SERVICES LIMITED

**DIRECTORS' REPORT AND
ACCOUNTS 1996 - 97**



SOUTHERN WATER SERVICES LIMITED

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REPORT OF THE DIRECTORS

The Directors present their report and the audited accounts for the year ended 31 March 1997.

RESULTS AND DIVIDEND

The profit for the financial year amounted to £132.7 million. The directors recommend a final dividend of £556.41 per ordinary share which together with an interim dividend of £278.20 per ordinary share makes a total dividend of £834.61 per ordinary share for the year. The balance of the profit for the year of £86.0 million has been transferred to reserves.

ACTIVITIES AND REVIEW

The Company's activities, which are expected to continue, are the provision of water supply and waste water services in the South East of England.

On 6 August 1996 Southern Water plc, the parent company, was acquired by Scottish Power plc.

RESEARCH AND DEVELOPMENT

The improvement of existing services and processes, together with the identification and development of new technology and solutions, are key aspects of the Company's strategy to enhance the quality of service to customers and improve methods of working. Research and development expenditure for 1997 amounted to £3.9 million.

DIRECTORS AND THEIR INTERESTS

The Directors who held office during the year were as follows:

Mr R F Clayton	
Mr R Collett	(Resigned: 4 October 1996)
Mr S Derwent	
Mr E J Hutchinson	
Mr M J Kinski	(Appointed: 16 December 1996)
Mr G H Setterfield	
Mr A L Smith	(Resigned: 4 October 1996)

None of the directors who held office at the end of the financial period had any disclosable interests in the shares of the Company.

Mr Kinski is a director of Scottish Power plc, the Ultimate Holding company, and his interests in the shares of that company are shown in its Annual Report and Accounts. Mr Kinski had no interest in the share capital of Southern Water plc prior to its acquisition.

The interests of the other serving directors, in the shares of Scottish Power plc at 31 March 1997 and the date of acquisition, together with their interests in the shares of Southern Water plc prior to the acquisition, are shown below.

REPORT OF THE DIRECTORS

Southern Water plc

	Ordinary Shares Held		Share Options						
			Executive Scheme				Sharesave Scheme		
	<u>1/4/96</u>	<u>1/4/96</u>	<u>Granted</u>	<u>Exercised</u>	<u>6/8/96</u>	<u>1/4/96</u>	<u>Granted</u>	<u>Exercised</u>	<u>6/8/96</u>
S Derwent	11,148	33,000	-	25,000	8,000	5,293	-	-	5,293
R F Clayton	6,777	27,000	-	-	27,000	8,170	-	-	8,170
E J Hutchinson	11,470	28,000	-	20,000	8,000	5,293	-	-	5,293
G H Setterfield	24,694	35,000	-	27,000	8,000	6,280	-	1,588	4,692

Scottish Power plc

	Ordinary Shares Held		Share Options							
			Executive Scheme				Sharesave Scheme			
	<u>6/8/96</u>	<u>31/3/97</u>	<u>6/8/96</u>	<u>Granted</u>	<u>Exercised</u>	<u>31/3/97</u>	<u>6/8/96</u>	<u>Granted</u>	<u>Exercised</u>	<u>31/3/97</u>
S Derwent	16,127	16,127	-	-	-	-	17,737	-	-	17,737
R F Clayton	-	-	-	-	-	-	-	-	-	-
E J Hutchinson	44,121	44,121	-	-	-	-	17,737	-	-	17,737
G H Setterfield	133,680	133,680	-	-	-	-	15,723	-	-	15,723

On acquisition by Scottish Power plc, options over Southern Water shares became exercisable at their pre-determined exercise price. Individuals participating in the Sharesave scheme had the additional option of converting their holdings into ScottishPower options. The options exercised or converted by the directors serving at the time of the acquisition are shown below.

	Executive share option scheme		Sharesave scheme	
	No. exercised	Exercise price (£)	No. exercised	Exercise price (£)
Mr S Derwent	4,000	6.39	3,024*	2.48
	4,000	5.25	2,269*	4.56
Mr R F Clayton	4,000	6.39	2,213	1.76
	4,000	5.25	3,258	2.36
	5,000	4.66	621	5.19
	7,000	3.10	65	5.37
	7,000	2.95		
Mr E J Hutchinson	4,000	6.39	3,024*	2.48
	4,000	5.25	2,269*	4.56
Mr G H Setterfield	4,000	6.39	1,512*	2.48
	4,000	5.25	1,461*	3.72
			756*	4.56
			963*	5.37
Mr A L Smith	4,000	6.39	3,024*	2.48
	4,000	5.25	756*	4.56
	5,000	4.66	1,284*	5.37

REPORT OF THE DIRECTORS

	Executive share option scheme		Sharesave scheme	
	No. exercised	Exercise price(£)	No. exercised	Exercise price(£)
Mr R Collett	4,000	6.39	2,386*	1.76
	4,000	5.25	907*	2.48
	20,000	4.66	1,142*	3.72
			664*	5.19
			756*	4.56

* Denotes options converted.

The Scottish Power plc offer price at 6 August 1996 was 1050p.

On acquisition by Scottish Power plc, shares in Southern Water plc, held in trust under the Southern Water plc Long Term Incentive Scheme and originally eligible for award in July 1998, were released to the following directors:

	<u>Shares</u>
S Derwent	2,000
R F Clayton	1,000
R Collett	1,000
E J Hutchinson	1,000
G H Setterfield	1,000
A L Smith	1,000

DIRECTORS' RESPONSIBILITIES

The directors are required by UK company law to prepare financial statements that give a true and fair view of the state of affairs of the Company as at the end of the financial period and of the profit or loss of the Company for that period.

The directors confirm that suitable accounting policies have been used and applied consistently and reasonable and prudent judgements and estimates have been made in the preparation of the financial statements for the period ended 31 March 1997. The directors also confirm that 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, for taking reasonable steps to safeguard assets of the Company and to prevent fraud and other irregularities.

EMPLOYMENT POLICIES

The Company is an equal opportunities employer and has a policy of non-discrimination in all forms of employment. Selection and promotion are based solely on merit and ability, and no job applicant or employee receives less favourable treatment. Disabled persons are considered for all types of work and modifications to jobs and equipment are made to enable them to be employed. Employees who become disabled are offered alternative work within the Company wherever possible.

REPORT OF THE DIRECTORS

With the future prosperity of the Company depending on the skills of its employees, we are committed to ensuring that the training required to fulfil career potential is provided. Training programmes are designed to meet specific needs, and include a range of in-house courses, beginning with an induction programme which introduces new employees to the fundamentals of customer service, teamwork and quality standards. The Open Learning programme of ScottishPower has been successfully implemented in Southern Water.

The Company places strong emphasis on effective employee communications and operates a number of formal and informal mechanisms, ranging from employee briefings to publications such as the corporate newspaper "Southern Water News". All employees are made aware of the objectives of the business and the contribution they themselves can make. Pay is related to company and individual performance and employees are encouraged to participate in the Employee Sharesave Scheme.

The health and safety of employees is of paramount concern and every effort is made to ensure safe working conditions and appropriate safety training. Additionally, all employees have the opportunity to undertake health and lifestyle checks at the Company's expense.

PAYMENT OF CREDITORS

The Company's current policy concerning the payment of the majority of its trade creditors is to follow the CBI's Prompt Payers Code. For other suppliers, the Company's policy is to

- (i) settle terms of payments with suppliers when agreeing the terms of transactions,
- (ii) ensure that suppliers are made aware of the terms of payment, and
- (iii) to comply with those contractual arrangements.

The Company's "creditor days" as defined in the Statement of Payment Practice Regulations of the Companies Act 1985 (as amended) were 53 days for the financial year ended 31 March 1997.

AUDITORS

A resolution to reappoint Coopers & Lybrand as auditors to the Company will be proposed at the Annual General Meeting.

By Order of the Board.



Mr K G Hall
Secretary
12th May 1997

REGISTERED OFFICE

Southern House, Yeoman Road, Worthing, West Sussex BN13 3NX

ACCOUNTING POLICIES

Basis of accounting

The accounts have been prepared under the historical cost convention and in accordance with applicable accounting standards in the United Kingdom and, subject to the treatment of infrastructure grants and contributions described below, with the requirements of the Companies Act 1985.

Statement of cash flows

The company is exempt from including a Statement of Cash Flows in its accounts as it is a wholly owned subsidiary of a company incorporated in the United Kingdom which has included a consolidated Statement of Cash Flows in its consolidated accounts.

Turnover

Turnover represents the invoice value of goods and services provided, excluding value added tax.

Research and development

Research and development expenditure is charged against profit in the year in which it is incurred.

Tangible fixed assets

Fixed assets are stated at cost and depreciated on the straight-line method over their estimated operational lives. The main depreciation periods used by the company are set out below:

Buildings	10 - 60 years
Operational structures	15 - 80 years
Fixed plant	10 - 40 years
Vehicles, computers and mobile plant	3 - 10 years

Freehold land and infrastructure assets are not depreciated. Infrastructure assets, being mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls are not depreciated because the network of systems is required to be maintained in perpetuity and, therefore, has no finite economic life. Expenditure on maintaining the operating capability of the network is charged as an operating cost.

Grants and contributions

Grants and contributions received in respect of additions to non-infrastructure fixed assets are included in creditors and released to profit over the useful lives of the relevant assets in accordance with the Companies Act 1985. The treatment of grants and contributions relating to infrastructure assets differs, since these assets are not depreciated and therefore no basis exists on which to recognise infrastructure grants and contributions as deferred income. Accordingly, grants and contributions relating to infrastructure additions are deducted from the cost of infrastructure assets in order to show a true and fair view. This treatment is in accordance with SSAP4 and the effect on the value of tangible fixed assets is disclosed in note 8.

ACCOUNTING POLICIES

Leased assets

Assets leased to the Company under finance leases are capitalised and depreciated in line with the Company's depreciation policy. The interest element of finance lease repayments is charged against profit in proportion to the balance of the capital repayments outstanding.

Rentals payable under operating leases are charged to profit and loss account as incurred.

Stocks

Stocks are valued at the lower of cost and net realisable value.

Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of transaction or at the forward cover rate where forward cover arrangements exist. Foreign currency balances are translated at the rate ruling at the balance sheet date or, where applicable, at the contracted rate. All foreign currency gains and losses are taken to the profit and loss account.

Taxation

Advance corporation tax in respect of dividends payable for the year is written off in the profit and loss account unless it can be recovered against mainstream corporation tax.

Provision is made for taxation deferred, using the liability method, in respect of timing differences to the extent that it is probable that a liability will crystallise in the foreseeable future. Such timing differences arise primarily from the different treatment for taxation and accounting purposes of provisions and the depreciation of fixed assets.

Pensions

Southern Water plc operates defined benefit and defined contribution pension schemes, which cover most employees of Southern Water Services Limited. A revaluation of the pension schemes is normally conducted by an independent actuary every three years. The regular cost of providing pensions and any variations from regular cost arising from the actuarial valuations are charged to the profit and loss account over the expected remaining service lives of current employees following consultations with the actuary. Payments to defined contribution schemes are charged against profit as incurred.

PROFIT AND LOSS ACCOUNT

For the year ended 31 March 1997

Notes	1997 £m	1996 £m	
1	Turnover from continuing operations	399.1	373.2
1	Cost of sales	(185.2)	(185.1)
	Gross profit from continuing operations	<u>213.9</u>	<u>188.1</u>
1	Administrative expenses	(29.8)	(29.9)
1	Other operating income	3.6	2.5
2	Operating profit from continuing operations	<u>187.7</u>	<u>160.7</u>
4	Net interest charge	(41.0)	(41.5)
	Trading profit	<u>146.7</u>	<u>119.2</u>
5	Exceptional item	(14.0)	-
	Profit on ordinary activities before taxation	<u>132.7</u>	<u>119.2</u>
6	Taxation	-	(9.5)
	Profit for the financial year	<u>132.7</u>	<u>109.7</u>
7	Dividends	(46.7)	(38.7)
15	Profit retained	<u>86.0</u>	<u>71.0</u>

A statement of total recognised gains and losses and a reconciliation to historical cost profits and losses are not shown as all gains and losses for 1996 and 1997 are recognised in the profit and loss account under the historical cost convention.

The accounting policies on pages 6 and 7, together with the notes on pages 10 to 16 form part of these accounts.

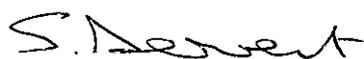
BALANCE SHEET

As at 31 March 1997

Notes	1997		1996	
	£m	£m	£m	£m
Fixed assets				
8		1,355.6		1,217.5
Tangible assets				
Current assets				
9		2.7		2.7
Stocks				
10		65.5		57.7
Debtors				
		-		32.2
Short term bank and other deposits				
		<u>68.2</u>		<u>92.6</u>
Creditors				
11		(358.8)		(286.2)
Amounts falling due within one year				
Net current liabilities				
		<u>(290.6)</u>		<u>(193.6)</u>
Total assets less current liabilities				
		<u>1,065.0</u>		<u>1,023.9</u>
Creditors				
11		(323.3)		(370.1)
Amounts falling due after more than one year				
12		(29.8)		(28.3)
Grants and contributions				
13		(5.8)		(5.4)
Provision for liabilities and charges				
Net assets				
		<u>706.1</u>		<u>620.1</u>
Equity shareholders' funds				
14		0.1		0.1
Called up share capital				
15		46.3		46.3
Share premium				
15		659.7		573.7
Profit and loss account				
		<u>706.1</u>		<u>620.1</u>

The accounting policies on pages 6 and 7, together with the notes on pages 10 to 16, form part of these accounts.

Approved by the Board on 12th May 1997 and signed on its behalf by:



S Derwent
Managing Director



E J Hutchinson
Finance Director

NOTES TO THE ACCOUNTS

1 Classification of turnover and revenue costs

Turnover represents the income receivable for providing water supply and wastewater services and is generated wholly in the United Kingdom.

Cost of sales reflects the direct costs of providing water supply and wastewater services. Administrative expenses comprise the indirect costs of the business. Other operating income refers to rents receivable and the profit on disposal of fixed assets.

2 Operating profit

Operating profit is stated after charging/(crediting):	1997 £m	1996 £m
Depreciation on		
- own fixed assets	28.7	28.9
- fixed assets held under finance leases	0.4	0.3
	<u>29.1</u>	<u>29.2</u>
Infrastructure renewals expenditure	18.4	17.9
Rentals under operating leases	7.8	5.9
Research and development expenditure	3.9	3.9
Release of grants and contributions	(1.1)	(1.1)
Profit on disposal of fixed assets	(2.5)	(1.1)
	<u>£000</u>	<u>£000</u>
Auditors' remuneration for statutory audit	70	85
Auditors' remuneration for non-audit services to the company	40	54

3 Employee information

	1997 £m	1996 £m
(a) Staff costs (including directors' emoluments):		
Wages and salaries	37.1	38.9
Social security costs	3.0	3.1
Pension contributions	4.3	4.5
	<u>44.4</u>	<u>46.5</u>
Total employee costs	44.4	46.5
Less: charged as capital expenditure	(4.1)	(4.6)
	<u>40.3</u>	<u>41.9</u>
	<u>1997</u>	<u>1996</u>
	Number	Number
(b) Average number of persons employed	1,961	2,048

NOTES TO THE ACCOUNTS

Southern Water Services Limited continues to bear the cost of staff transferred to Pipeworks Limited, a wholly-owned subsidiary and agent of Southern Water Services Limited. The associated cost in respect of the year ended 31 March 1997 was £7.7m (1996: £7.5m) which is excluded from the above total. The employee costs and average number of employees of Pipeworks Limited are shown in the financial statements of that Company.

4 Net interest charge

	1997 £m	1996 £m
Interest payable on bank loans, overdrafts and other loans:		
Repayable wholly within 5 years	(5.7)	(5.0)
Not wholly repayable within 5 years	(37.0)	(37.3)
Total interest payable	<u>(42.7)</u>	<u>(42.3)</u>
Interest receivable	1.7	0.8
	<u>(41.0)</u>	<u>(41.5)</u>

Interest of £42.5m (1996: £41.7m) was payable to Southern Water plc.

5 Exceptional items

	1997 £m	1996 £m
Reorganisation costs	14.0	-

Reorganisation costs relate to the fundamental restructuring of Southern Water Services Limited following the acquisition of Southern Water plc by Scottish Power plc.

6 Taxation

	1997 £m	1996 £m
United Kingdom taxation:		
Corporation tax in respect of the current year	-	26.1
Corporation tax provision in respect of prior years no longer required	-	(2.0)
	<u>-</u>	<u>24.1</u>
Advance corporation tax utilised relating to prior years	-	(14.6)
	<u>-</u>	<u>9.5</u>

No corporation tax is payable as tax losses are anticipated for the period ended 31 March 1997.

NOTES TO THE ACCOUNTS

7 Dividend per ordinary share

	1997 £ per ordinary share	1996 £ per ordinary share	1997 £m	1996 £m
Interim dividend	278.20	230.32	15.6	12.9
Proposed final dividend	556.41	460.64	31.1	25.8
	<u>834.61</u>	<u>690.96</u>	<u>46.7</u>	<u>38.7</u>

8 Fixed assets and capital commitments

(a) Tangible assets	Freehold land & buildings £m	Plant & machinery £m	Vehicles and Equipment £m	Infra- structure assets £m	Other £m	Total £m
Cost :						
At 1 April 1996	469.5	322.7	1.5	523.8	167.8	1,485.3
Additions and transfers	32.7	67.3	-	66.8	4.1	170.9
Grants and contributions	-	-	-	(3.7)	-	(3.7)
Disposals	(0.3)	(0.3)	(0.4)	-	(0.4)	(1.4)
At 31 March 1997	<u>501.9</u>	<u>389.7</u>	<u>1.1</u>	<u>586.9</u>	<u>171.5</u>	<u>1651.1</u>
Depreciation :						
At 1 April 1996	97.2	91.8	1.3	-	77.5	267.8
Charge for the year	9.6	10.4	0.1	-	9.0	29.1
Disposals	(0.3)	(0.3)	(0.4)	-	(0.4)	(1.4)
At 31 March 1997	<u>106.5</u>	<u>101.9</u>	<u>1.0</u>	<u>-</u>	<u>86.1</u>	<u>295.5</u>
Net book value :						
At 31 March 1997	<u>395.4</u>	<u>287.8</u>	<u>0.1</u>	<u>586.9</u>	<u>85.4</u>	<u>1,355.6</u>
At 31 March 1996	<u>372.3</u>	<u>230.9</u>	<u>0.2</u>	<u>523.8</u>	<u>90.3</u>	<u>1,217.5</u>

Tangible fixed assets include £183.1m (1996: £166.9m) of assets in the course of construction which are not depreciated until commissioning.

The net book value of tangible fixed assets held under finance leases was £6.8m (1996: £7.2m).

The net book value of infrastructure assets is stated after deducting grants and contributions since privatisation of £74.8m (1996: £71.1m).

NOTES TO THE ACCOUNTS

(b) Capital commitments

	1997 £m	1996 £m
In respect of contracts placed	134.4	93.3
	—	—

9 Stocks

	1997 £m	1996 £m
Materials and consumables	2.1	2.3
Work in progress	0.6	0.4
	<u>2.7</u>	<u>2.7</u>
	—	—

10 Debtors

	1997 £m	1996 £m
Trade debtors	31.8	30.3
Unbilled income	23.0	20.3
Amounts owed by parent company and fellow subsidiary undertakings	2.0	2.8
Other debtors	7.0	3.9
Prepayments	1.7	0.4
	<u>65.5</u>	<u>57.7</u>
	—	—

11 Creditors

	1997 £m	1996 £m
(a) Amounts falling due within one year		
Bank overdraft	134.4	-
Loans from parent company	9.7	3.9
Trade creditors	16.8	12.0
Capital creditors and accruals	69.0	38.6
Amounts owed to parent company and fellow subsidiary undertakings	23.6	128.9
Corporation tax	3.7	12.7
Other taxation and social security	0.5	-
Other accruals and deferred revenue	54.4	51.4
Dividends payable	46.7	38.7
	<u>358.8</u>	<u>286.2</u>
	—	—

NOTES TO THE ACCOUNTS

(b) Amounts falling due after more than one year	1997	1996
	£m	£m
Loans from parent company	323.3	370.1
Repayments fall due as follows:	—	—
Between one to two years	10.0	8.7
Between two and five years	37.2	32.8
After five years not by instalments	175.0	215.0
After five years by instalments	101.1	113.6
	<u>323.3</u>	<u>370.1</u>
	—	—

The Company has agreed loan facilities with Southern Water plc. The rates of interest payable on loans due after five years range from 6.5 % to 11.1%.

12 Grants and contributions

	£m
At 1 April 1996	28.3
Receivable in year	2.6
Released to profit and loss account	(1.1)
At 31 March 1997	<u>29.8</u>
	—

Grants and contributions relate to non-infrastructure assets.

13 Provision for liabilities and charges

	Infrastructure Renewal £m	Other £m	Total £m
At 1 April 1996	2.0	3.4	5.4
Provided in year	18.4	-	18.4
Utilised in year	(18.0)	-	(18.0)
At 31 March 1997	<u>2.4</u>	<u>3.4</u>	<u>5.8</u>
	—	—	—

The full potential deferred taxation liability, for which no provision is considered necessary, calculated under the liability method at a tax rate of 33% is:

	1997	1996
	£m	£m
Accelerated capital allowances (non-infrastructure assets)	161.4	124.8
Other timing differences	(7.9)	(10.3)
Advance corporation tax	(2.2)	-
	<u>151.3</u>	<u>114.5</u>
	—	—

NOTES TO THE ACCOUNTS

14 Share capital	1997	1996
	£m	£m
Authorised		
46,050,000 ordinary shares of £1 each	46.1	46.1
	—	—
Allotted, called up and fully paid		
56,000 ordinary shares of £1 each	0.1	0.1
	—	—

15 Reconciliation of movement in shareholders' funds

	Called up share capital £m	Share premium £m	Profit and loss account £m	Total £m
At 1 April 1996	0.1	46.3	573.7	620.1
Profit retained	-	-	86.0	86.0
At 31 March 1997	0.1	46.3	659.7	706.1

16 Pensions

The Company's pension arrangements are administered through three schemes operated by Southern Water plc, the Immediate Holding company. Actuarial information concerning these schemes is disclosed in the financial statements of Southern Water plc.

17 Contingent liabilities

	1997	1996
	£m	£m
Contractors' claims	4.4	3.3
	—	—

The Company is party to mutual cross guarantees for any monies owed by Group companies to National Westminster Bank plc.

18 Financial commitments

	1997	1996
	£m	£m
Annual commitments under operating leases:		
Expiring within one year	2.9	2.1
Expiring between two and five years	2.4	2.4
Expiring after five years	0.7	0.4
	—	—
	6.0	4.9
	—	—

NOTES TO THE ACCOUNTS

19 Directors' emoluments	1997	1996
	£000	£000
Aggregate emoluments (including benefits in kind)	376	525
Compensation for loss of office	179	-
	<u>555</u>	<u>525</u>
Aggregate highest paid director emoluments and benefits (excluding gains made on exercise of share options and value of shares received under long-term incentive schemes)	90	97
Defined benefit scheme: Accrued annual pension at 31 March	<u>35</u>	<u>28</u>

Six directors exercised share options in Southern Water plc, as set out on pages 3 and 4 of the Director's Report. No directors became entitled to receive shares under the Southern Water long-term incentive scheme. Retirement benefits are accruing to four directors under a Southern Water defined benefit scheme.

20 Windfall levy

On May 2 1997, the Labour Party was invited to form the Government of the United Kingdom. The Labour Party's election manifesto contained proposals for a "windfall levy" of unspecified amount to be imposed on United Kingdom utility companies. It is probable that the windfall levy will be reflected in the Government's legislative proposals for 1997-98. However, details of the application of the proposed levy and its basis of calculation have not been published. Therefore it is not possible for the company to ascertain whether or not it will be liable to a levy, and if it were, the amount that would be charged. Provision for the company's liability, if any, in respect of any such levy will therefore be charged in arriving at the results for the company once the details of the levy and its application have been determined.

21 Related party transactions

As a wholly owned subsidiary, the Company is exempt from the requirement to disclose related party transactions with other Southern Water and ScottishPower group undertakings under Financial Reporting Standard Number 8.

22 Ultimate holding company

The Company is a wholly owned subsidiary of Southern Water plc, which is itself wholly owned by Scottish Power plc, the ultimate holding company.

(Copies of Scottish Power plc's consolidated financial statements may be obtained from the Company Secretary at 1 Atlantic Quay, Glasgow G2 8SP).

REPORT OF THE AUDITORS

To the members of Southern Water Services Limited

We have audited the financial statements on pages 6 to 16.

Respective responsibilities of directors and auditors

As described on page 4, the Company's Directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with 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 Company's circumstances, consistently applied and adequately disclosed.

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.

Opinion

In our opinion, the financial statements give a true and fair view of the state of affairs of the Company at 31 March 1997 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Coopers & Lybrand

Coopers & Lybrand
Chartered Accountants and Registered Auditors
London
12th May 1997