

SOUTHERN WATER SERVICES LIMITED

**DIRECTORS' REPORT AND
ACCOUNTS FOR THE YEAR ENDED
31 MARCH 1998**

Registered No. 2366670



SOUTHERN WATER SERVICES LIMITED

Directors' Report and Accounts for the year

ended 31 March 1998

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REPORT OF THE DIRECTORS

The directors present their report and the audited Accounts for the year ended 31 March 1998.

RESULTS AND DIVIDEND

The profit for the financial year amounted to £73.3 million (1997: £132.7 million). The directors recommend a final dividend of £516.91 per ordinary share (1997: £556.41) together with an interim dividend of £258.45 per ordinary share (1997: £278.20) makes a total dividend of £775.36 per ordinary share for the year (1997: £834.61). The balance of the profit for the year of £29.9 million (1997: £86.0 million) has been transferred to reserves.

ACTIVITIES AND REVIEW

The principal activities of the company are the provision of water supply and waste water services in the South East of England.

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 1998 amounted to £3.2 million (1997: £3.9 million).

DIRECTORS AND THEIR INTERESTS

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

Christopher Chapman	(Appointed: 1 November 1997)
Richard Clayton	
Barrie Delacour	(Appointed: 10 November 1997)
Stuart Derwent	
John Harris	(Appointed : 1 November 1997)
Eric Hutchinson	
Michael Kinski	(Resigned: 1 March 1998)
Ronnie Mercer	(Appointed: 1 March 1998)
Graham Setterfield	(Resigned: 10 November 1997)
David Stainthorpe	(Appointed: 10 November 1997)

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

The interests of the serving directors, in the shares of Scottish Power plc at 31 March 1998 and 31 March 1997 or the date of their appointment if later, are shown below.

REPORT OF THE DIRECTORS

	Ordinary		Share Options				*Long Term	
	Shares Held		Executive Scheme		Sharesave Scheme		Incentive Plan	
	1998	1997/Appt	1998	1997/Appt	1998	1997/Appt	1998	1997/Appt
Christopher Chapman	-	-	-	-	-	-	-	-
Richard Clayton	-	-	-	-	1,905	-	5,384	-
Barrie Delacour	18,952	20,092	-	-	13,638	13,638	4,423	4,423
Stuart Derwent	24,861	16,127	-	-	9,850	17,737	6,307	-
John Harris	-	-	-	-	-	-	-	-
Eric Hutchinson	45,928	44,121	-	-	9,850	17,737	4,500	-
Ronnie Mercer	1,000	1,000	698	698	6,581	6,581	18,222	18,222
David Stainthorpe	19,157	19,157	-	-	15,855	15,855	4,346	4,346

* These shares represent, in each case, the maximum number of shares which the directors may receive, dependent on the satisfaction of certain performance criteria as approved by the shareholders of Scottish Power plc in connection with the Long Term Incentive Plan.

DIRECTORS' RESPONSIBILITIES

The directors are required by UK company law to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company as at the end of the financial year 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 that reasonable and prudent judgements and estimates have been made in the preparation of the financial statements for the year ended 31 March 1998. 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 maintaining proper accounting records and sufficient internal controls to safeguard the assets of the company and to prevent and detect fraud or any other irregularities.

EMPLOYEES

Employee involvement and participation

The company has developed its communications processes with its employees to ensure greater understanding of and involvement in the business. This has been achieved through the "Waterline" staff magazine, produced to complement "Southern Water News", and by staff briefings. The influence of ScottishPower is now seen through the extension of the values based leadership development programme to Southern Water. The ScottishPower Learning business is now firmly established in Southern Water with programmes for school leavers and the long term unemployed to work alongside and learn from our employees. The Open Learning facilities at all the main company locations reinforce the commitment of the company to providing learning opportunities.

REPORT OF THE DIRECTORS

The company has been working with the trade unions to establish new consultation arrangements suitable for the changed organisation. These processes are aimed at improving the involvement and participation of staff in the business. The Managing Director meets the recognised trade unions at least twice per year to discuss the progress of the business in meeting its objectives.

The operating divisions continue to meet regularly with the trade union representatives to discuss local issues and also address health and safety matters.

Equal opportunity

Southern Water policy is to promote equality of opportunity in recruitment, employment continuity, training and career development. The published ScottishPower Equal Opportunity booklet is issued to all Southern Water employees. The policy is designed to ensure that equal opportunity in these areas extends as far as practicable to people with disabilities. The company is a member of the Employer's Forum on Disability, which supports the efforts to meet the needs of the disabled for employment and access to the company and its buildings.

Health and safety

The company has embraced the ScottishPower health and safety strategy, and every employee receives a copy of the corporate policy statement on health and safety. There are regular meetings of employee representatives and managers to consider all aspects of health and safety, and there is a health and safety management review group which ensures that there is an adequate system for meeting the company's responsibilities for health and safety to its staff, customers and members of the public.

Southern Water has its own internal occupational health service, including the provision of physiotherapy. These services are being developed to meet the needs of the business and our employees at work. In addition, voluntary health screening has been offered to staff and a fitness centre will be open in the near future.

MILLENNIUM

A year 2000 strategy has been established for the ScottishPower group, of which Southern Water Services is a member. Details are contained in the Operating and Financial Review within the 1997/98 Annual Report and Accounts of Scottish Power plc.

CREDITOR PAYMENT POLICY AND PRACTICE

The company's current policy and practice concerning the payment of the majority of its trade creditors is to follow the CBI's Prompt Payers Code, copies are available upon request from the Company Secretary. For other suppliers, the company's policy is to settle terms of payment when agreeing the terms of transactions, to include the terms in its contracts and to pay in accordance with its contractual and legal obligations.

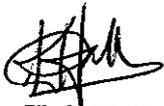
REPORT OF THE DIRECTORS

The company's "creditor days" as defined in the Statement of Payment Practice Regulations of the Companies Act 1985 (as amended) were 58 days for the financial year ended 31 March 1998.

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.



K G Hall
Secretary
5th May 1998

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 UK and, subject to the treatment of infrastructure grants and contributions described below, with the requirements of the Companies Act 1985.

Basis of preparation

The financial statements contain information about Southern Water Services Limited as an individual company and do not contain consolidated financial information as the parent of subsidiary companies. The company is exempt under section 228 of the Companies Act 1985 from the requirement to prepare consolidated financial statements as it and its subsidiary undertakings are included by full consolidation in the consolidated financial statements of the ultimate holding company Scottish Power plc, a company registered in Scotland.

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 UK which has included a consolidated Statement of Cash Flows in its consolidated accounts.

Turnover

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

Research and development

Expenditure on research is charged to the profit and loss account as it is incurred.

Tangible fixed assets

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

	<u>Years</u>
Buildings	10 - 60
Operational structures	15 - 80
Fixed plant	10 - 40
Vehicles, computers and mobile plant	3 - 10

Freehold land and water and wastewater infrastructure assets, being mains and sewers, 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. Infrastructure renewals, being the expenditure on maintaining the operating capability of the network, is charged as an operating cost based on the long run average charge implied by an asset management plan agreed with the water industry regulator as part of the price regulation process. The asset management plan is developed from historical experience combined with a rolling programme of reviews of the condition of the infrastructure assets.

ACCOUNTING POLICIES

The required renewals and the related costs are determined from these engineering estimates using indexed historic cost data. The allocation of costs to each period is also determined from the rolling programme of reviews of the condition of the infrastructure assets. Actuals costs incurred are charged against the related provision/prepayment account.

Grants and contributions

Capital grants and customer contributions in respect of additions to non-infrastructure fixed assets are treated as deferred income and released to the profit and loss account over the estimated operational lives of the related assets. 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 grants and contributions as deferred income. Accordingly, grants and contributions relating to infrastructure asset additions are deducted from the cost of infrastructure assets. This treatment is in accordance with SSAP 4 and the effect on the value of tangible fixed assets is disclosed in note 8. This is not in accordance with the Companies Act 1985 which requires assets to be stated at their purchase price or production cost. The departure from the requirements of the Act is, in the opinion of the Directors, necessary in order to give a true and fair view since infrastructure assets are not depreciated.

Leased assets

Fixed 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 to the profit and loss account 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.

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.

The charge for ordinary taxation is based on the profits for the year and takes into account 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.

ACCOUNTING POLICIES

Pensions

Southern Water plc operates defined benefit and defined contribution pension schemes, which cover the majority of the 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 related benefits 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. Any difference between the charge to the profit and loss account and the actual contributions paid to the pension schemes is included as an asset or liability in the balance sheet. Payments to defined contribution schemes are charged against profit as incurred.

PROFIT AND LOSS ACCOUNT

for the year ended 31 March 1998

	Notes	1998 £m	1997 £m
Turnover from continuing operations	1	420.4	399.1
Cost of sales	1	(175.1)	(185.2)
Gross profit from continuing operations		<u>245.3</u>	<u>213.9</u>
Administrative expenses	1	(26.8)	(29.8)
Other operating income	1	4.5	3.6
Operating profit from continuing operations	2	<u>223.0</u>	<u>187.7</u>
Net interest charge	4	(40.1)	(41.0)
Trading profit		<u>182.9</u>	<u>146.7</u>
Exceptional item	5	-	(14.0)
Profit on ordinary activities before taxation		<u>182.9</u>	<u>132.7</u>
Ordinary taxation	6	(33.2)	-
Profit after ordinary taxation		<u>149.7</u>	<u>132.7</u>
Exceptional taxation - windfall tax	6	(76.4)	-
Profit for the financial year		<u>73.3</u>	<u>132.7</u>
Dividends	7	(43.4)	(46.7)
Profit retained	16	<u>29.9</u>	<u>86.0</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 1997 and 1998 are recognised in the profit and loss account under the historical cost convention.

The accounting policies on pages 6 to 8, together with the notes on pages 11 to 18 form part of these accounts.

BALANCE SHEET

as at 31 March 1998

	Notes	1998 £m	1997 £m
Fixed assets			
Tangible assets	8	1,574.7	1,355.6
Investments	9	—	—
		—	—
Current assets			
Stocks	10	2.1	2.7
Debtors	11	210.1	65.5
		—	—
		212.2	68.2
Creditors, amounts falling due within one year			
Loans and other borrowings	12	(29.4)	(144.1)
Other creditors	12	(324.6)	(214.7)
		—	—
		(354.0)	(358.8)
Net current liabilities		(141.8)	(290.6)
		—	—
Total assets less current liabilities		1,432.9	1065.0
Creditors, amounts falling due after more than one year			
Loans and other borrowings	12	(485.1)	(323.3)
Convertible unsecured loan stock 1999	12	(177.5)	—
		—	—
Grants and contributions	13	(31.0)	(29.8)
		—	—
Provision for liabilities and charges	14	(3.3)	(5.8)
		—	—
Net assets		736.0	706.1
		—	—
Called up share capital	15	0.1	0.1
Share premium	16	46.3	46.3
Profit and loss account	16	689.6	659.7
		—	—
Equity shareholders' funds		736.0	706.1
		—	—

The accounting policies on pages 6 to 8, together with the notes on pages 11 to 18, form part of these accounts.

Approved by the Board on 5th May 1998 and signed on its behalf by:


Eric 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):	1998 £m	1997 £m
Depreciation on		
- fixed assets	33.1	28.7
- fixed assets held under finance leases	0.4	0.4
	<u>33.5</u>	<u>29.1</u>
Infrastructure renewals expenditure	19.0	18.4
Rentals under operating leases	6.2	7.8
Research and development expenditure	3.2	3.9
Release of grants and contributions	(1.2)	(1.1)
Profit on disposal of fixed assets	(3.5)	(2.5)
	<u>£000</u>	<u>£000</u>
Auditors' remuneration for statutory audit	92	70
Auditors' remuneration for non-audit services to the company	145	40

3 Employee information

	1998 £m	1997 £m
(a) Employee costs (including directors' emoluments):		
Wages and salaries	51.7	37.1
Social security costs	4.0	3.0
Pension costs	5.3	4.3
	<u>61.0</u>	<u>44.4</u>
Total employee costs	61.0	44.4
Less: charged as capital expenditure	(15.1)	(4.1)
	<u>45.9</u>	<u>40.3</u>
Charged to the profit and loss account	45.9	40.3

NOTES TO THE ACCOUNTS

	1998 Number	1997 Number
(b) Average number of persons employed	2,371	1,961

For the year ended 31 March 1997 Southern Water Services bore the cost of staff transferred to Pipeworks Limited a wholly owned subsidiary agent company. The associated cost for the year ended 31 March 1997 was £7.7m which is excluded from the above total. The employee costs and average number of employees of Pipeworks Limited for the year ended 31 March 1997 were shown in the financial statements of that company. In 1998 the costs of these staff are included in the figures shown above.

4 Net interest charge

	1998 £m	1997 £m
Interest payable on bank loans and overdraft	(3.3)	(0.3)
Interest payable on other loans	(37.4)	(42.4)
Total interest payable	(40.7)	(42.7)
Interest receivable	0.6	1.7
Net interest charge	(40.1)	(41.0)

Interest of £37.4m (1997: £42.4m) was payable to Group companies.

5 Exceptional items

	1998 £m	1997 £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 on 6 August 1996.

6 Taxation

	1998 £m	1997 £m
Corporation tax	33.2	-
UK corporation tax at 31% (1997: 33%)	76.4	-
Exceptional taxation - windfall tax	109.6	-
Total tax charge	109.6	-

NOTES TO THE ACCOUNTS

Exceptional taxation relates to the company's estimated share of the windfall tax according to the formula contained within the Finance (No 2) Act 1997. The first of two equal instalments of £38.2 million was paid on 1 December 1997 with the second instalment due on 1 December 1998.

7 Dividend per ordinary share

	1998 £ per ordinary share	1997 £ per ordinary share	1998 £m	1997 £m
Interim dividend	258.45	278.20	14.5	15.6
Proposed final dividend	516.91	556.41	28.9	31.1
	<u>775.36</u>	<u>834.61</u>	<u>43.4</u>	<u>46.7</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 1997	501.9	389.7	1.1	586.9	171.5	1,651.1
Additions and transfers	60.4	81.5	1.1	98.1	17.0	258.1
Grants and contributions	-	-	-	(4.5)	-	(4.5)
Disposals	(1.1)	(0.1)	(0.5)	-	(0.3)	(2.0)
At 31 March 1998	<u>561.2</u>	<u>471.1</u>	<u>1.7</u>	<u>680.5</u>	<u>188.2</u>	<u>1,902.7</u>
Depreciation :						
At 1 April 1997	106.5	101.9	1.0	-	86.1	295.5
Charge for the year	10.4	12.2	0.6	-	10.3	33.5
Disposals	(0.3)	(0.1)	(0.3)	-	(0.3)	(1.0)
At 31 March 1998	<u>116.6</u>	<u>114.0</u>	<u>1.3</u>	<u>-</u>	<u>96.1</u>	<u>328.0</u>
Net book value :						
At 31 March 1998	<u>444.6</u>	<u>357.1</u>	<u>0.4</u>	<u>680.5</u>	<u>92.1</u>	<u>1,574.7</u>
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>

NOTES TO THE ACCOUNTS

Tangible fixed assets include £255.9m (1997: £183.1m) 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 at 31 March 1998 was £6.5m (1997: £6.8m). The charge for depreciation against these assets during the year was £0.4m (1997: £0.4m)

The net book value of infrastructure assets is stated after deducting grants and contributions since privatisation of £79.3m (1997: £74.8m).

(b) Capital commitments	1998	1997
	£m	£m
In respect of contracts placed	188.7	134.4
	—	—

9 Fixed asset investments

Southern Water Services Limited holds the entire issued share capital of Southern Water Services Finance plc, a company incorporated in the UK on 13 March 1998. The principal activity of the company is to raise debt finance. Southern Water Services Limited has guaranteed the £100m Variable Coupon Bond issued by Southern Water Services Finance plc.

10 Stocks	1998	1997
	£m	£m
Raw materials and consumables	1.9	2.1
Work in progress	0.2	0.6
	—	—
	2.1	2.7
	—	—

11 Debtors	1998	1997
	£m	£m
Trade debtors	37.9	31.8
Unbilled income	25.2	23.0
Amounts owed by parent company and fellow subsidiary undertakings	131.9	2.0
Prepayments - infrastructure renewals	5.4	-
Prepayments - other	0.2	1.7
Other debtors	9.5	7.0
	—	—
	210.1	65.5
	—	—

NOTES TO THE ACCOUNTS

12 Creditors

	1998	1997
(a) Amounts falling due within one year	£m	£m
Loans and other borrowings :		
Bank overdraft	19.4	134.4
Loans from parent company	10.0	9.7
	<u>29.4</u>	<u>144.1</u>
Other creditors :		
Trade creditors	19.4	16.8
Capital creditors and accruals	117.4	69.0
Amounts owed to parent company and fellow subsidiary undertakings	21.1	23.6
Corporation tax	37.1	3.7
Windfall tax	38.2	-
Other taxation and social security	0.7	0.5
Other accruals and deferred revenue	47.3	54.4
Dividends payable	43.4	46.7
	<u>324.6</u>	<u>214.7</u>
(b) Amounts falling due after more than one year	1998	1997
	£m	£m
Loans and other borrowings :		
Loans from parent company	385.5	323.3
Loans from subsidiary undertakings	99.6	-
	<u>485.1</u>	<u>323.3</u>
£200m Discounted Convertible Unsecured Loan Stock 1999	177.5	-
	<u> </u>	<u> </u>

The Convertible Unsecured Loan Stock 1999 is convertible at the option of the stockholder on 24 November 1999 into fully paid ordinary shares of £1 in Southern Water Services Limited at the rate of 97 fully paid ordinary shares for every £2,000,000 in nominal amount stock. The full amount of the Unsecured Loan Stock is held by Scottish Power plc, the ultimate parent company.

Repayments fall due as follows:

Between one to two years	188.5	10.0
Between two and five years	41.7	37.2
After five years not by instalments	348.7	175.0
After five years by instalments	83.7	101.1
	<u>662.6</u>	<u>323.3</u>
	<u> </u>	<u> </u>

NOTES TO THE ACCOUNTS

The rates of interest payable on loans from the parent company due after five years range from 6.35% to 11.1%. The rate of interest on the loans from subsidiary undertakings is 6.9%.

13 Grants and contributions

	£m
At 1 April 1997	29.8
Receivable in year	2.4
Released to profit and loss account	(1.2)
	<hr/>
At 31 March 1998	31.0
	<hr/>

Grants and contributions relate to non-infrastructure assets.

14 Provision for liabilities and charges

	Infrastructure Renewal £m	Other £m	Total £m
At 1 April 1997	2.4	3.4	5.8
Provided in year	19.0	-	19.0
Utilised in year	(21.4)	(0.1)	(21.5)
	<hr/>	<hr/>	<hr/>
At 31 March 1998	-	3.3	3.3
	<hr/>	<hr/>	<hr/>

No provision for deferred taxation is considered necessary at 31 March 1998, since future taxation depreciation is expected to exceed accounting depreciation and therefore no deferred taxation liabilities are expected to crystallise in the foreseeable future. Total potential deferred liabilities, calculated at the prevailing rate of corporation tax of 30% (1997: 33%) are as follows:

	1998 £m	1997 £m
Accelerated capital allowances (non-infrastructure assets)	156.8	161.4
Other timing differences	(6.8)	(7.9)
Advance corporation tax	-	(2.2)
	<hr/>	<hr/>
	150.0	151.3
	<hr/>	<hr/>

15 Share capital

	1998 £m	1997 £m
Authorised		
46,050,000 ordinary shares of £1 each	46.1	46.1
	<hr/>	<hr/>
Allotted, called up and fully paid		
56,000 ordinary shares of £1 each	0.1	0.1
	<hr/>	<hr/>

NOTES TO THE ACCOUNTS

16 Reconciliation of movement in shareholders' funds

	Called up share capital £m	Share premium £m	Profit and loss account £m	Total £m
At 1 April 1997	0.1	46.3	659.7	706.1
Profit retained	-	-	29.9	29.9
At 31 March 1998	<u>0.1</u>	<u>46.3</u>	<u>689.6</u>	<u>736.0</u>

17 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.

18 Contingent liabilities

	1998 £m	1997 £m
Contractors' claims	4.0	4.4

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

19 Financial commitments

	1998 £m	1997 £m
Annual commitments under operating leases:		
Expiring within one year	0.8	2.9
Expiring between two and five years	2.5	2.4
Expiring after five years	0.3	0.7
	<u>3.6</u>	<u>6.0</u>

20 Directors' emoluments

	1998 £000	1997 £000
Aggregate emoluments (including benefits in kind)	363	376
Compensation for loss of office	-	179
	<u>363</u>	<u>555</u>

NOTES TO THE ACCOUNTS

Retirement benefits are accruing to five directors under a Southern Water defined benefit scheme.

Aggregate highest paid director emoluments and benefits (excluding gains made on exercise of share options)	97	90
Defined benefit scheme: Accrued annual pension at 31 March	44	35

Retirement benefits are accruing to the highest paid director under a Southern Water defined benefit scheme.

Directors' interests in share options of Scottish Power plc.

<u>Executive director</u>	<u>At 1/4/97 or date of appointment if later</u>	<u>Granted</u>	<u>Exercised</u>	<u>At 31 March 1998</u>
Long Term Incentive Plan				
Richard Clayton	-	5,384	-	5,384
Barrie Delacour	4,423	-	-	4,423
Stuart Derwent	-	6,307	-	6,307
Eric Hutchinson	-	4,500	-	4,500
David Stainthorpe	4,346	-	-	4,346
Ronnie Mercer	18,222	-	-	18,222
Executive Share Option Scheme				
Ronnie Mercer	698	-	-	698
Sharesave Scheme				
Richard Clayton	-	1,905	-	1,905
Barrie Delacour	13,638	-	-	13,638
Stuart Derwent	17,737	2,247	10,134	9,850
Eric Hutchinson	17,737	2,247	10,134	9,850
David Stainthorpe	15,855	-	-	15,855
Ronnie Mercer	6,581	-	-	6,581

21 Related party transactions

Scottish Power plc has ultimate control over the company. The company has taken an exemption, as allowed by Financial Reporting Standard 8, not to disclose related party transactions with other group companies as the parent company publishes full consolidated financial statements.

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 18.

Respective responsibilities of directors and auditors

As described on page 4, the company's directors are responsible for the preparation of the 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 1998 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
5th May 1998