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North West Water

North West Water Group PLC

Annual Report 1995 – Progress with Responsibility

Contents

Cover We have embarked on a major campaign to consult more closely and regularly with our customers as part of our commitment to strike a more appropriate balance between their interests and those of our shareholders.

Registered in England and Wales
Registered No: 2366616
Registered Office: Dawson House
Great Sankey, Warrington
United Kingdom WA5 3LW

North West Water Group

- our work is with communities, worldwide, to safeguard public health and protect the environment
- our focus is on water and wastewater, the business we know best
- our proven skills and products and our long experience provide affordable solutions to water and wastewater problems
- through delivering greater value, we give shareholders better returns and customers a better deal

News highlights of the year

At home and abroad - 28m customers

With contracts overseas to serve another 21 million people, in addition to the 7 million served in the UK, we now rank amongst the world's top environmental businesses.

Regulator sets tough target for next 10 years

OFWAT

Ofwat's new price formula for the next five years capped annual increases in charges to customers at 2.5 per cent above inflation and at no more than inflation in the following five years: tough targets we believe we can meet.

Challenging fresh focus for growth

The Chief Executive's review of the business set a fresh focus with challenging new targets to achieve growth in earnings and increase dividends at a rate higher than that achieved since privatisation.

The UK's most efficient water business

Progress in restructuring the UK Utility Division resulted in it again outperforming Ofwat's targets and being independently rated as the UK's most efficient water and wastewater business.

A fairer balance for customers and shareholders

£180 million

In a landmark initiative, we announced that in each of the next five years we will share efficiency savings of £36 million between customers and shareholders through annual rebates and special dividends.

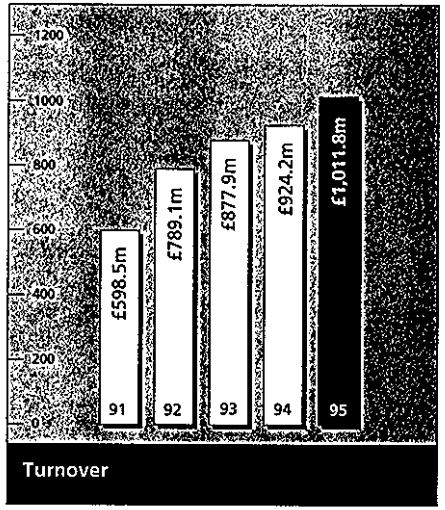
New alliance will take on the world

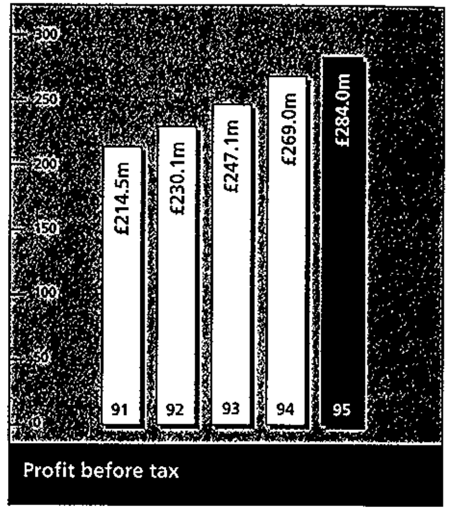
As a powerful enabler to a significant part of our plans, we embarked upon a deep-rooted alliance with Bechtel, a recognised world leader in the development, engineering and construction of major projects.

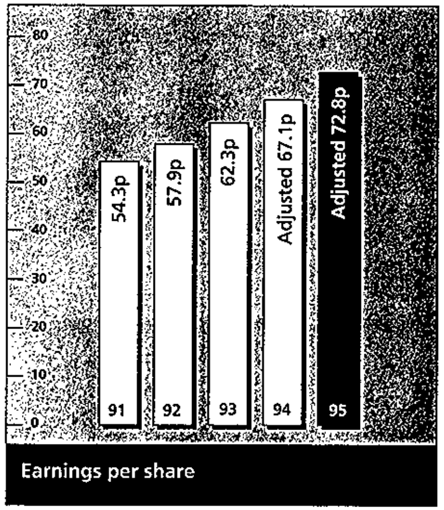
Financial highlights

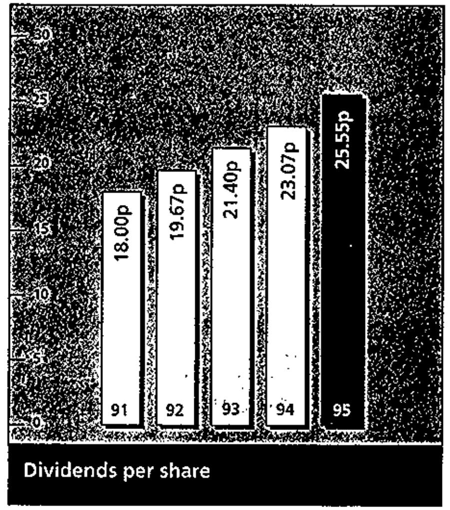
The year further extended our record of sound financial progress, born out of our continuing achievement of efficiency improvements in all aspects of our business.

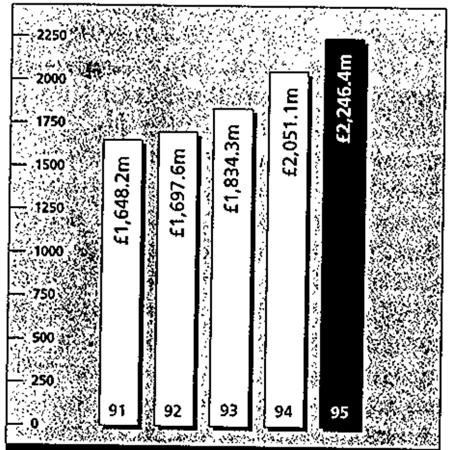
	1995	1994
Turnover	**£1,011.8m**	£924.2m
Profit before tax	**£284.0m**	£269.0m
Adjusted earnings per share	**72.8p**	67.1p
Ordinary dividends per share	**25.55p**	23.07p
Operating cash flow	**£421.7m**	£367.4m
Operating cash flow per share	**112.5p**	99.9p
Interest cover	**7.3**	6.1
Gearing	**27.4%**	27.3%



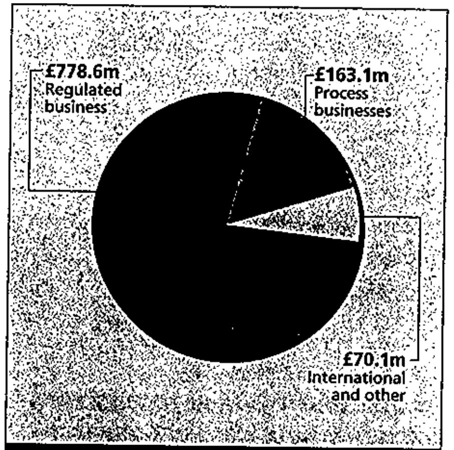




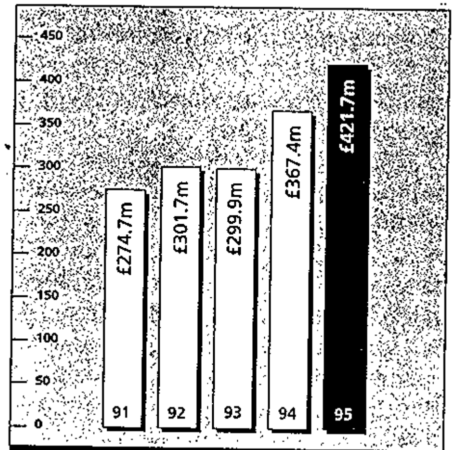




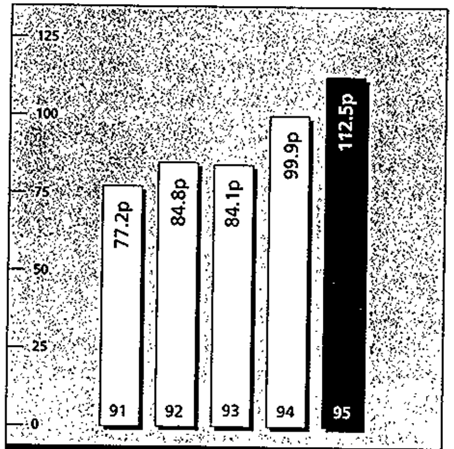
Shareholders' funds



Turnover 1995 (segmental)



Operating cash flow



Operating cash flow per share

North West Water business activities

The Group ranks as the world's third largest water and wastewater enterprise and, by market capitalisation, as the largest in the UK

UK Utility Division

Provides water and wastewater services to seven million people in North West England

Manages the biggest environmental improvement programme in the UK

Is independently rated as the most efficient of the privatised water and wastewater utilities

International Division

Is the Group's primary vehicle for expansion

Has won contracts to provide water and wastewater services to 2.1 million people overseas

Contracts now operational in Australia, Malaysia and Mexico

Process Equipment Division

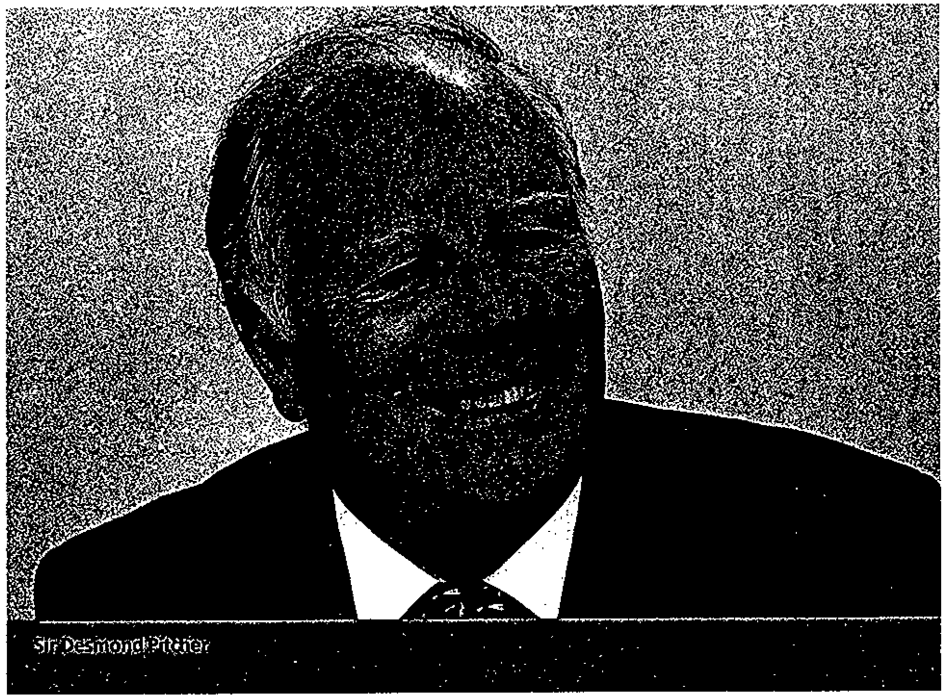
The world's largest integrated group of companies competing in the municipal, industrial and privatised water and wastewater markets

Our process companies are market leaders in water and wastewater processes, chemical feed, disinfection and solids handling

Chairman's statement

"Our first five years have seen a transformation from a public sector organisation into one of the leading water and wastewater companies in the world. That excellent progress provides the strong foundation for our continuing success."

Sir Desmond Pitcher *Chairman*



I am pleased to be able to report to you on a year of excellent progress for the Group.

The financial results were robust with profitability well ahead. Adjusted earnings per share increased by 8.5 per cent to 72.8 pence per share.

Based on that earnings strength and our stated intent to unlock shareholder value by the managed decline of dividend cover, the directors recommend a final dividend of 17.20 pence. This gives a total ordinary dividend for the year of 25.55 pence, an increase of 10.75 per cent.

In addition to these good financial results, the year was characterised by initiatives which I believe will provide a strong foundation for our continuing success.

In particular, in the UK Utility Division, we have built on our primary belief in the vital importance of serving our customers well, by now openly recognising the special responsibilities we carry in the management of a monopoly service. We believe that a balance has to be struck between the interests of our shareholders and our customers. That is particularly true in the distribution of the gains which the company makes by outperforming the efficiency targets set by the water industry's economic regulator, the Director General of Water Services.

Our operating efficiency leads the industry. We also ended our first five years with significant capital efficiency gains. Accordingly, on 30 March 1995, we announced an efficiency rebate for customers of £6.50 per household, matched by a special dividend for shareholders of 3.80 pence per share.

Some have seen our initiative as politically expedient, but that was not our motive. It is the correct way for us to act and will, I believe, produce better value for you, our shareholders, in the longer term. It is, of course, encouraging that subsequently the Labour Party has indicated that its thinking is developing along similar lines.

During the year, we also announced the formation of a global partnership with Bechtel of the US. They are a formidable force in the world marketplace and our ability to form the partnership is a reflection of our success internationally.

The International Division, concentrating on the provision of water and wastewater operating services, will be the major route for the Group's expansion in the coming years. The Bechtel partnership will be a powerful catalyst for our future success.

Whilst those were the major initiatives of the year, we have also been working hard to position the Group for future success, taking account of the Director General's price determination last July for the regulated business.

Our efforts in all those areas during the year have resulted in a favourable re-rating of our future prospects by the market, which in turn has delivered improved value to our shareholders. We aim to continue that progress and, in saying that, I do not overlook the fact that our industry will remain under critical scrutiny in the coming years. Undoubtedly there will be challenges ahead but increasingly we are better prepared to meet them.

Companies achieve progress through the efforts of their employees. We are no exception, and I am pleased to have this opportunity to recognise the efforts of our employees. In the five years since privatisation, they have been asked to accept major change and our success is a reflection of the open-minded way in which they have embraced new working practices and ever increasing levels of service to our customers.

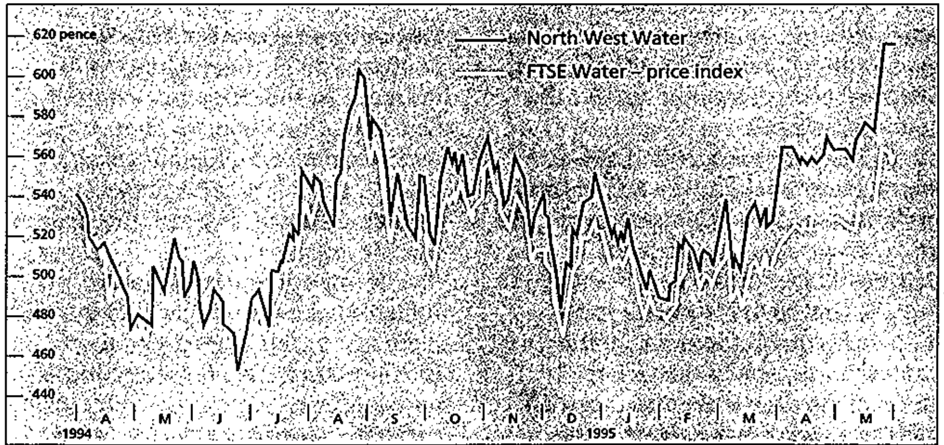
During the year, we filled the vacancies in the senior executive team with the appointments of John Beckitt and, more recently, Gerald Orbell as managing directors of the Process Equipment and International Divisions respectively. We now have a strong and vigorous team under the day to day leadership of the Chief Executive to carry us forward.

We were pleased to welcome John Beckitt to the Board in April this year.

Clare Bolton will be retiring from the Board at the annual general meeting after seven years of service, including chairmanship of the Audit Committee. We have been grateful for the valuable benefit of her advice and professional expertise.

The Group has now come to the end of its first five years as a private sector company. Those years have seen a transformation from a public sector organisation into one of the leading water and wastewater companies in the world. In the process, we have set new standards of efficiency in the United Kingdom, and been rewarded with international success on a scale which sees us today with contracts to serve 28 million customers around the world.

As we start upon our second five years, you may rest assured that we are fully committed to ensuring that the Group's success continues in a similar manner.



Share price performance relative to sector

D H. Pitcher

Sir Desmond Pitcher *Chairman*

Chief Executive's review

"The Group has a clear cut agenda, strong strategies and the people to deliver them. We have started upon the process of favourably differentiating ourselves. This will continue, underpinned by earnings growth and the delivery of first class shareholder returns. That is our goal."

Brian Staples *Chief Executive*

Brian Staples

I am pleased to be reporting to you on a year which was also my first as Chief Executive of the Group.

It happened as well to be, perhaps, the most significant year in the Group's history.

It brought to an end our first five year regulatory regime and saw us receive the Director General of Water Service's price determination for the coming ten years.

Against that background, it was appropriate to review the actions and performance of the Group thus far, and to chart a course designed to deliver still greater success in the future. That review resulted in a refinement and refocussing of the strategic direction of the Group, and the outcome was announced on 11 November 1994 under the title Progress with Responsibility.

Shortly afterwards, on 25 November, we announced our intention to form a global partnership with Bechtel, an initiative which will significantly influence the Group's future success.

At the same time, we were turning into reality the various ideas embodied in Progress with Responsibility and on 30 March 1995 we launched Facing up to the Future. This is a major initiative to unlock shareholder value whilst recognising that such an action has to be balanced by a similar distribution to customers.

All in all, a very full year of corporate activity in which the Group has laid the groundwork for its future success.

Regulatory regime for 1996 to 2000 and 2005 On 28 July 1994, we received the Director General's determination of the regulatory regime which would apply for the years 1996 to 2000 and, subject to a further review in 1999, for the years 2001 to 2005.

The key components are the K factor – the factor by which the regulated utility is permitted to increase its charges for water and wastewater services above inflation each year – and the estimated cost of the capital investment which the company will be required to make to meet the outputs determined by the Director General.

Those components in our case are:

	1996/2000	2001/2005
K factor	2.5%	0%
Estimated capital investment	£2.3bn	£1.45bn

The Director General incorporates within his K determination, targets for efficiency improvement in respect of operating costs. For both water and wastewater services, North West Water was recognised to be the clear industry leader and, accordingly, rewarded with the lowest efficiency targets for the coming years.

We could have sought a referral to the Monopolies and Mergers Commission if we had judged that the determination was unreasonably harsh. The Board carefully considered that option but concluded that we would accept the Director General's determination. We judged the determination to be tough but fair, and we took comfort from the fact that our proven ability to deliver efficiency savings would enable us to meet and subsequently outperform the Director General's targets.

The determination cleared the way for us to plan the progress of the regulated business for the coming five years, subject only to the risk of future unforeseen regulatory or governmental action to amend the new regime.

Progress with Responsibility The findings of my review of our activities were numerous and they led to a number of changes in the way the Group is managed on a day to day basis. I will restrict my report here to the items of strategic importance:

The Group centre should be slimmer in the future, devolving more responsibility to the managing directors under a new three divisional structure – UK Utility Division, International Division and Process Equipment Division.

The Group should not involve itself in construction risk in the future, other than as a client body. Therefore, the Group subsidiaries Water Engineering and Jones Environmental were to be disposed. A provision of £13.5 million was judged necessary to meet the write down of goodwill arising from those disposals, together with that of our membrane manufacturing activities.

The Group should be mindful of the social responsibilities inherent in owning and operating a business which is a monopoly. To do so, required a balance to be struck between the interests of our shareholders and our customers, thereby addressing political and media criticism of the water sector.

Action in that direction, coupled with much better communications with our customers, would serve to reduce the risk of external intervention in our affairs.

Already the sector leader in efficiency, the Division should further accelerate its rate of improvement, whilst at the same time embracing total quality management to achieve continually improving customer satisfaction. A powerful Customer Charter, offering financial compensation for service failures, would act as a catalyst to the achievement of standards as good as the best open market service suppliers.

faced into an excellent worldwide market for water and wastewater services, and the operation of those services should be the primary platform for the Group's expansion over the coming years.

North America would provide particular opportunities for growth.

should be the vehicle to draw together the Group's manufacturing companies, with the task of significantly improving the performance of each of those companies.

Many of the businesses are under-invested in both product development and manufacturing machinery and, as such, patience was needed since it would be a number of years before the Division reached acceptable levels of return.

A number of those recommendations were founded in the belief that total shareholder returns in the medium and longer term would be significantly enhanced if the Group grew its non-regulated earnings over the coming years to a level which was material within the overall context of the Group's earnings, in order to offset the impact of any future decline in regulated earnings in the United Kingdom.

Finally, it was apparent that whilst the Group had been admirably consistent in its dividend policy in the past, the balance sheet contained the benefits of efficiency achievements and could support faster growth in dividends, providing a politically acceptable way could be found to achieve such a release.

The Bechtel partnership A dialogue had been opened in 1993 with Bechtel, one of the world's largest construction companies, to explore the possibilities of working together. Having provided those discussions with a fresh focus, in November 1994 we signed a Memorandum of Intent to enter into a global partnership with Bechtel:

Engineering resources Bechtel would purchase NWW Engineering, our design and project management operation, for a consideration of £15 million.

This step would mark our exit from construction risk, whilst at the same time providing the employees of NWW Engineering with more secure and progressive prospects.

Capital investment programme NWW Engineering, subsequently renamed Bechtel Water Technology, would continue to be our agent for the delivery of our £2.3 billion five year forward capital investment programme.

Through changed procurement practices and the addition of Bechtel's project management skills, that forward capital investment programme would be delivered for less cost than we could achieve alone.

International development Bechtel would become our construction partner in the international market outside North America.

Bechtel would relieve us of construction risk, whilst at the same time standing alongside us as an equity investor. They are present in 68 countries of the world, which will help to increase the pace of our international development whilst reducing our costs.

North America Bechtel would join with us to develop a significant business in water and wastewater operations in North America.

Our current business in that arena, US Water, provides a good core but the emerging market will be enormous. The goal of significant presence dictated that forming a partnership made sense in terms of resource, both human and financial. In addition, Bechtel's know how and experience would reduce our risk of investing in the US.

After the announcement, we turned our attention to making the partnership a reality and the sale of NWW Engineering was completed on 8 April 1995. That allowed Bechtel to commence their input to the capital programme. In North America, business planning is proceeding well, and the new management and operational structure will come into place as the year progresses.

Facing up to the Future Those, then, were the major strategic moves of the year, and on 30 March 1995 we turned words into actions for an important element of Progress with Responsibility. On that day, we launched our Facing up to the Future initiative:

Sharing benefits We promised to share with customers and shareholders the benefits which the Group will enjoy from the efficiency savings achieved in the execution of our capital investment programme over the last five years.

We calculated those benefits to equate to £36 million annually which we shall distribute equally in each of the five years up to 1999/2000:

Partnership Group directors visited the San Francisco headquarters of Bechtel to agree the basis of the global partnership between our two organisations. Here, Riley Bechtel, President (centre) with colleague John Carter (second left) describes his company's activities to North West Water's Chairman, Sir Desmond Pitcher (left), Group Finance Director, Robert Ferguson (second right) and Chief Executive Brian Staples (right).

- a special dividend to shareholders of 3.80 pence per share; and
- an efficiency rebate for each of our customers of £6.50 if they receive both our water and wastewater services or half of that sum if they only receive one of those services.

Both those measures will be continued subject only to there being no outside intervention in our affairs which prevents us doing so.

Customer Charter We made far reaching customer commitments which provide a powerful Charter under which our services will be delivered in the future.

The list of commitments is extensive and in many cases we will pay compensation, typically of £10, if we fail to live up to them.

Discretionary expenditure We committed to undertake £180 million of discretionary capital expenditure over the next five years, sharply focused to improve the worst problems experienced by our customers.

Examples are the elimination of repetitive foul flooding, relief of low pressure water supply, and the faster elimination of lead piping from our system.

Each of those measures was negotiated and agreed with the Director General and he has indicated his support of our initiative. Importantly, he has confirmed that none of them should give rise to any resetting of the regulatory accounts at the next price determination.

Dividend policy Your Board considers that the appropriate level of dividend cover for a Group with our trading characteristics is 2 times, and we will manage the decline of our cover to reach that level by the year 2000.

The actual levels of dividend growth delivered are, of course, dependent on the strength of the earnings growth the Group achieves and, therefore, on the success of our overall strategies. Our intent is to deliver progressive dividend growth for our shareholders.

1995 results The Group delivered again excellent results for the year, with profit before tax of £284.0 million, some 5.6 per cent ahead of the previous year. Adjusted earnings per share grew by 8.5 per cent, bringing our average annual earnings per share growth over the last five years to 7.6 per cent. That is an enviable record which owes a great deal to the successful policies of efficiency improvement followed by Derek Green and his team in the UK Utility Division.

The year's results enable us to measure our efficiency at delivering our capital investment programme over the first five years. It is especially pleasing to note that in completing the envisaged £2.5 billion programme for £400 million less, we have secured another strong sector leadership position, in addition to our clear industry leadership for operating efficiency. That capital efficiency together with our rigorous policies to conserve cash have enabled us once again to restrain the growth of our debt, and our gearing remains virtually unchanged from last year.

Summary The Group has had a busy year laying out the strategies we intend to follow and we have put a number of important building blocks in place. That said, I am conscious that whilst strategy is of vital importance, it is results which really count.

With the arrival of John Beckitt and Gerald Orbell, the senior executive team to deliver those results is now complete. Like me, they have joined an employee team which deserves full recognition. Our people are enthusiastic and open to change. They have already delivered a great deal and I am confident there is more to come as we move forward.

In conclusion, the Group now has a clear cut agenda, strong strategies and the people to deliver them. During the year, we started on the process of favourably differentiating ourselves from the other companies in our sector. That will continue in the future, supported by strong earnings growth which will enable us to deliver first class shareholder returns. That is our goal.

B e Staples

Brian Staples *Chief Executive*

Financial review

"Our continued focus on cash management and efficient application of funds has maintained a strong balance sheet and ensured that we are in a good position to continue to generate further growth in earnings and dividends."

Robert Ferguson *Group Finance Director*

Robert Ferguson (left) on one of his regular visits to the City as part of his continuing programme of contact with investors and the financial community.

Close cash controls remain at the heart of our financial procedures. They are central to ensuring the efficient management of our utility business whose key features are strong operating cash generation and high demands on corresponding cash investment.

The sound results for the year have benefited from this focus. All key financial areas have continued to improve and our gearing ratio (debt to shareholders' funds) has remained virtually level.

Dividends The dividends for the year of 25.55 pence per share represent a 7 per cent growth in real terms on the previous year. We believe this level of growth to be sustainable in the future.

We announced on 30 March 1995, a special dividend of 3.80 pence per share to be paid in each of the years from 1995/96 to 1999/2000 subject to no regulatory or legislative intervention in our affairs. The special dividend for 1995/96 will be paid on 3 October 1995.

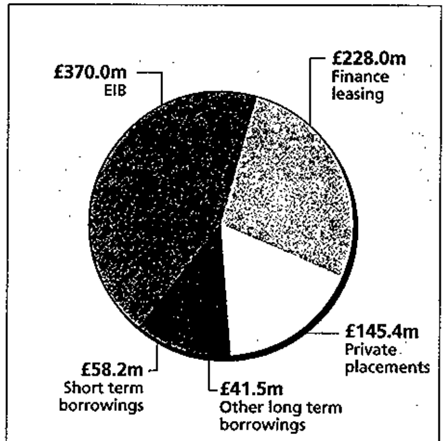
Comparatives In reviewing the results, the following items are of note:

Adjusted earnings per share Adjusted earnings per share, which increased by 8.5 per cent, has been calculated after excluding two non recurring items. These are the exceptional goodwill loss of £13.5 million in the year (which relates to the proposed disposal of Water Engineering, Jones Environmental and our membrane manufacturing activities) and the one off tax benefit of £13.4 million in the previous year (which resulted from the saving of advance corporation tax on the 1992/93 enhanced scrip dividend).

Consolidation of overseas contract The Bangkok wastewater project, which we have taken under our direct management control, is for the first time fully consolidated within the Group accounts. As a result, prudent provision has been made for the risk of a potential loss, recognising that the project will trade negatively before we commence recovery of additional costs outside our control. This project is included in the segmental analysis (page 43) under "Other activities".

Utility restructuring charge Charges for restructuring within the UK Utility Division have been a feature of our results over the past years. The year's charge of £11.8 million, which brings the year end provision for rationalisation to £33.7 million, is fractionally down on the previous year's charge.

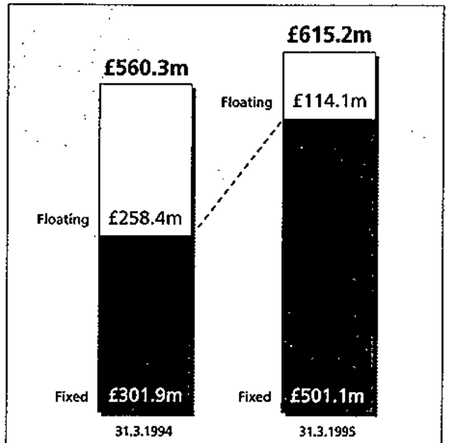
Infrastructure renewals charge The year's charge for the maintenance of our extensive infrastructure network was £66.2 million, compared to £62.8 million the previous year. It is our policy to ensure that the annual charge does not materially differ from cash spend over the medium term.



Gross debt by source £843.1m (March 1995)

Treasury management Treasury management policies are aimed at the prudent management of interest rates whilst ensuring optimal funding is secured.

The Group's treasury department does not act as a profit centre. Strategy is set by the Board and all major implementation programmes of the agreed strategy are authorised by the Board.



Net debt fixed vs floating (March 1995)

Interest rate management The Group's interest charge for the year fell by £5.9 million to £46.9 million. New borrowings created an additional interest expense of £4.5 million but this was more than offset by a reduction of £10.4 million in interest as a result of more favourable interest rates.

At 31 March 1995, approximately 80 per cent of our net debt was at rates fixed for more than one year, compared to 50 per cent the previous year. This reflects our policy of allowing only a proportion of interest rates to float where naturally hedged by revenues. The balance is fixed to ensure that interest rates are predictable and manageable.

In addition to this medium term strategy, the residual short term floating rate debt is predominantly fixed for each financial year at known, budgeted rates.

Foreign exchange Approximately 80 per cent of net debt is denominated in sterling. The balance, which is principally in US dollars, relates to debt raised in previous years. These borrowings match the debt service costs with that of the underlying overseas earnings.

Liquidity and operating cash flow Operating cash flow continues to be strong, showing an increase of 14.8 per cent over the previous year, with operating cash flow per share up 12.6 per cent to 112.5 pence per share. This is an important measure of the financial health of the Group and exceeds adjusted earnings per share by more than 50 per cent.

The net result of that strong cash flow was that gearing remained virtually level at 27.4 per cent. Net borrowings increased by £54.9 million to £615.2 million at year end.

The Group finished the year with £227.9 million of cash and short term deposits (£247 million at the previous year end).

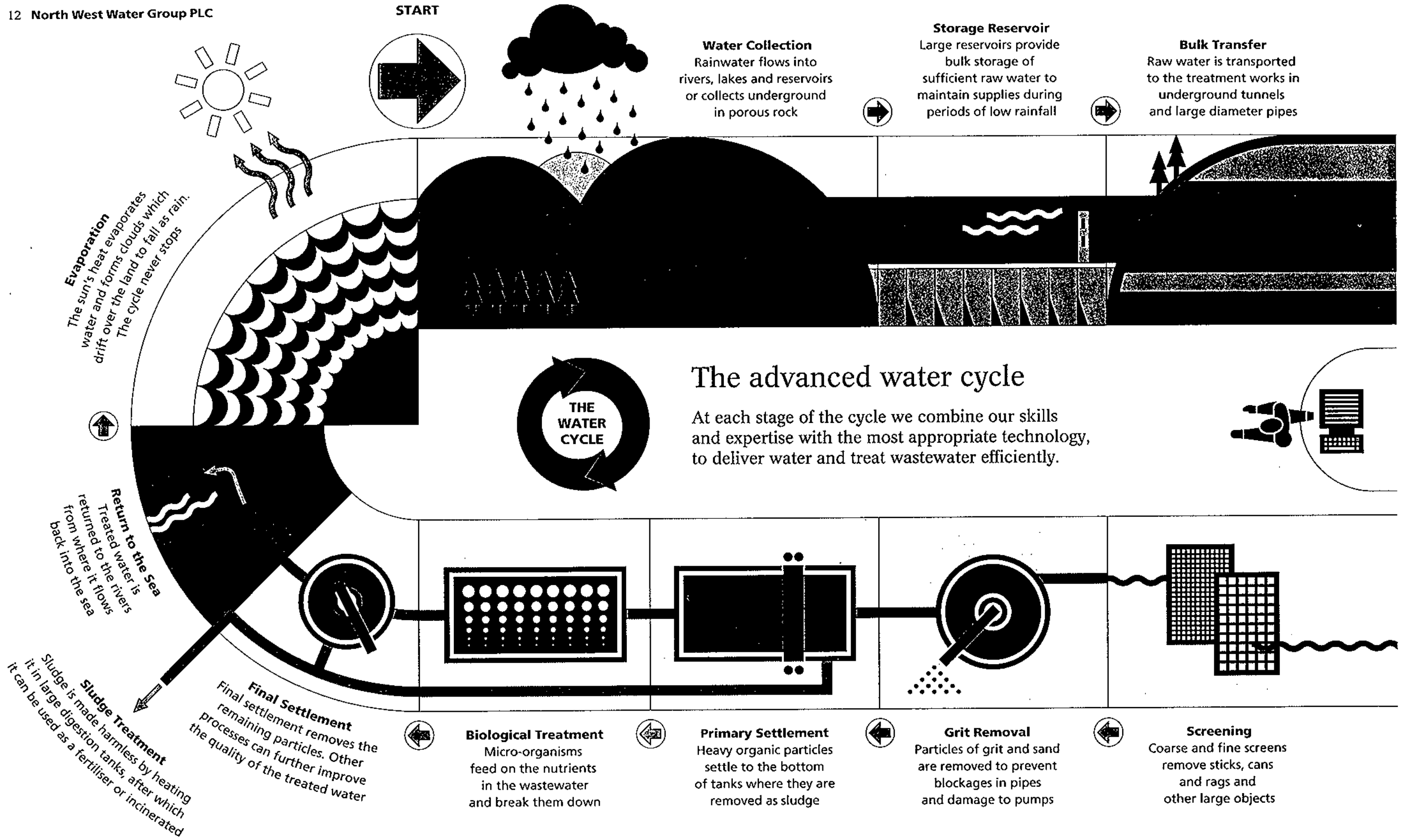
Tax The tax charge of £24.8 million mainly comprises advance corporation tax on dividends for the year. This is written off against profits because tax losses and allowances result in no corporation tax being payable. The advance corporation tax paid may only be recovered against future tax liabilities.

No provision for deferred tax is required since significant tax allowances are likely to be available for the foreseeable future.

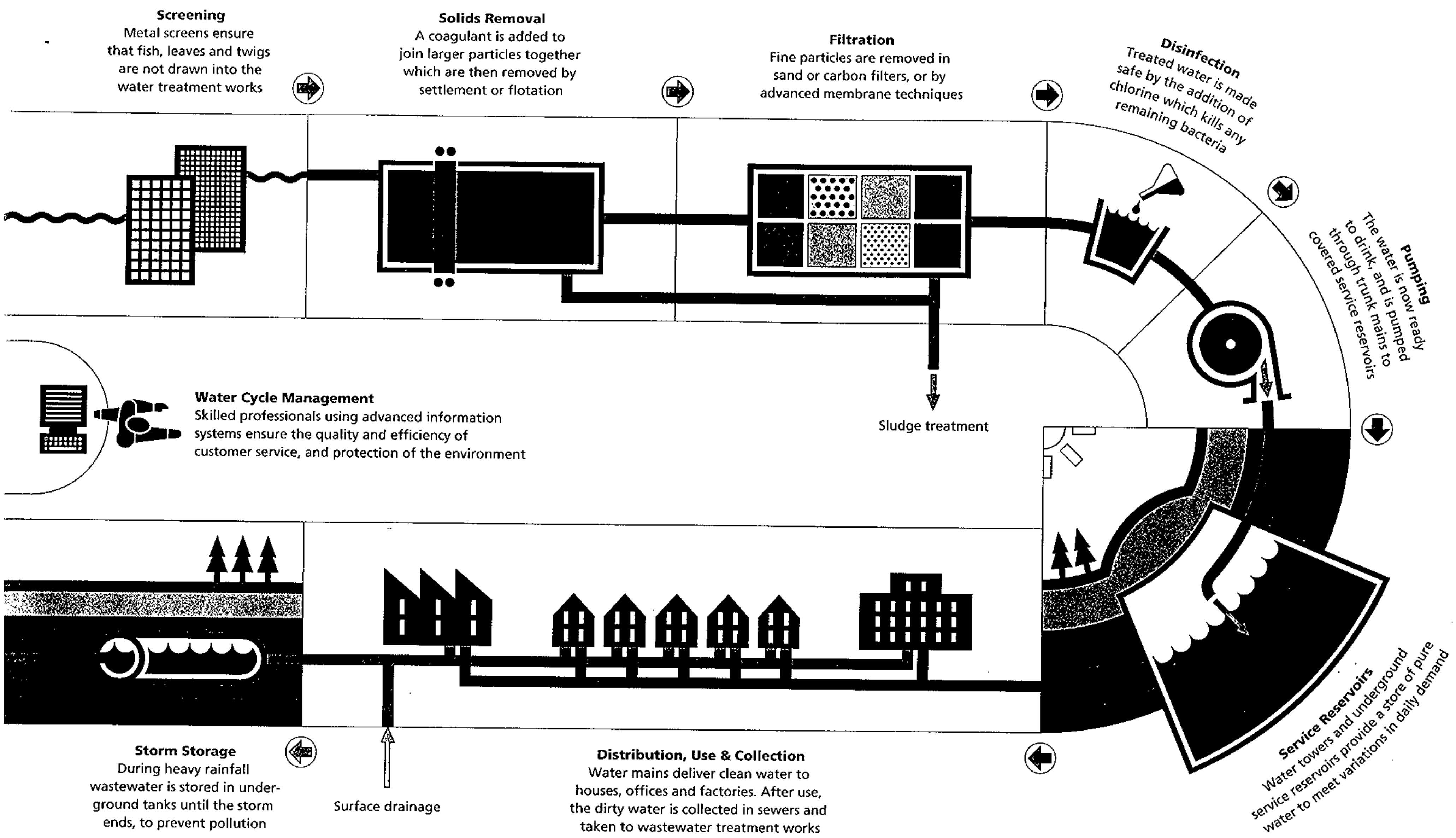
Summary Stringent financial controls and prudent management of cash resources have again delivered sound financial performance.

The advanced water cycle

At each stage of the cycle we combine our skills and expertise with the most appropriate technology, to deliver water and treat wastewater efficiently.



The advanced water cycle. The natural cycle provides free supplies of water, but only when and where it falls from the sky, not necessarily when it is needed, where it is needed or to guaranteed high standards of purity. So we use a wide range of technical, scientific and management skills to interrupt the natural cycle and create the advanced water cycle.



We apply with care our know how and skills to plan, design, equip and operate every stage of the advanced water cycle.

Our particular strengths are based on first hand experience of privatisation and regulation and on our efficient operations in the North West of England, safely delivering water and wastewater services to 7 million people, industry and commerce. Those strengths are now being applied to the benefit of communities around the world where we have contracts to serve a further 21 million people.

At the heart of the advanced water cycle, in the treatment of water and wastewater, is the equipment supplied by our process companies who are market leaders in water and wastewater processes, chemical feed, disinfection and solids handling.

Together, North West Water's business divisions are bringing affordable solutions to customers and communities around the world.

UK Utility Division

"Being a monopoly supplier places special responsibilities upon us. We will behave exactly as if we were in competition. Customers do not have a choice where to buy their water services, but by our behaving as if they do, we are improving our services in the way they expect."

Derek Green *Managing Director* UK Utility Division

Derek Green launches the Facing up to the Future campaign to achieve increased customer satisfaction through a radical new deal that more appropriately balances their interests with those of our shareholders.

Profit before interest and tax up 6.8 per cent to £348.3 million

Rated most efficient operator by Ofwat

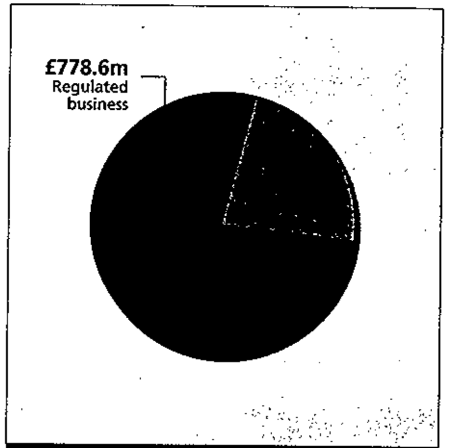
Efficiency savings worth £90 million to be shared with customers

New K factor for price increases to fund £2.3 billion investment

We passed a number of major milestones during the year. We agreed with the Director General of Water Services our strategic business plan for the next five years and a new price limit. As part of the Group partnership and as a consequence of the sale of NWW Engineering, we reached an agreement with Bechtel which will maximise efficiencies in the delivery of the capital programme. And we focused a great deal of attention on our commitments to customers, with a number of key announcements and developments.

As a result, we continued to fulfil our twin objectives:

- to increase customer satisfaction by providing good quality, value-for-money services; and
- to grow profitability by constantly and continuously improving our efficiency.



Turnover 1995

Business performance The business continued to perform strongly in all key financial areas – profitability, control of capital expenditure and working capital management.

Turnover increased by 6.8 per cent to £778.6 million following an average price increase of 6.3 per cent. Growth in new domestic connections and wastewater and trade effluent volumes offset a decline of 1.7 per cent in industrial and commercial water consumption. This is substantially better than the previous year's decline and gives some optimism for improved trading conditions.

Profit before interest and tax increased by 6.8 per cent to

£348.3 million. Depreciation and infrastructure renewals charges rose by 10 per cent reflecting the impact of our capital investment programme. Other operating expenses rose in line with inflation, with continued efficiency savings offset by the cost of capital schemes and improving customer service.

Working capital improved by £16 million, with better collection performance holding trade debtors flat. This, together with lower investment expenditure of £374 million, helped reduce net cash outflow to £15.4 million, leaving net borrowings at £426 million.

Quality initiatives have placed an upward pressure on operating costs since privatisation. These extra costs, totalling approximately £30 million in 1994/95, have been more than offset by efficiencies, resulting in a net reduction in operating costs over the period. We have reduced our controllable unit costs by 17 per cent since privatisation. This has been achieved by a reduction in manpower numbers of around 25 per cent and through continued efficiencies in power and material costs. Ofwat's latest analysis of unit operating costs places North West Water as the most efficient of the water and wastewater companies. On water supply, we were rated 23 per cent above average

Customer satisfaction campaign One of the main features of our drive to improve customer satisfaction is our commitment to listen and consult more. Research with our customers showed that 91 per cent wanted more information on how we spend their money, 76 per cent wanted us to listen and consult more and 75 per cent wanted more information about when and where investment work is carried out.

In response, we have launched one of the biggest ever consultation exercises by a utility. Through advertising and direct mail, all our customers have been invited to send for an information pack and questionnaire enabling them to register their views on a whole range of our activities. The results, together with other research, will help us plan further improvements in our services to customers.

efficiency and on wastewater, 13 per cent above average efficiency.

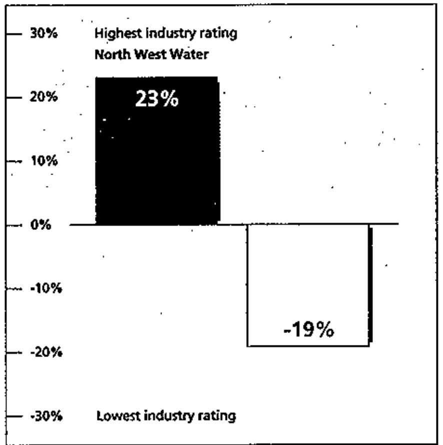
Organisational changes To achieve still further efficiencies, we are comprehensively reorganising our business and have been retraining and upskilling many of our people, supporting them with a major investment in technology. Our Information Services operation has been independently benchmarked as being in the top 7 per cent in the country for efficiency.

One of the key organisational changes has been in Operations, with the creation of three major functions. The new Water and Wastewater Management team actively manages our five year capital investment programme, acting as the interface between North West Water and Bechtel Water Technology. Field Operations has day to day responsibility for the delivery of water and wastewater services. Asset Maintenance is an essential support function with responsibility to maintain the infrastructure both above and below ground.

Investment efficiencies We successfully completed our first five year capital investment programme, estimated to cost £2.5 billion, with capital savings of £400 million.

The partnership with Bechtel will help us to deliver the second five year capital investment programme for less than the £2.3 billion planned, meeting our capital investment commitments at the lowest cost and highest quality.

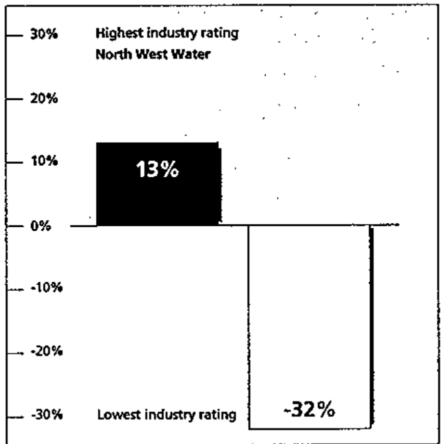
Regulation A focal point in the year was the Director General's response to the submission of our future plans, setting out the next phase of investment to meet higher standards. On the basis of the plan, the Director General determined the K factor, the maximum amount above inflation by which we may increase our charges to fund the investment.



Efficiency water (percentage) Source: Ofwat

Our K factor has been set at 2.5 per cent a year for the next five years, and zero for the five years after 2000. The average household bill for our customers in 1995/96 is £195, or about 53 pence a day. By 1999/2000, after the allowed increases, that would be £221 in today's terms, still only about 60 pence a day. Our charges remain the third lowest in the country.

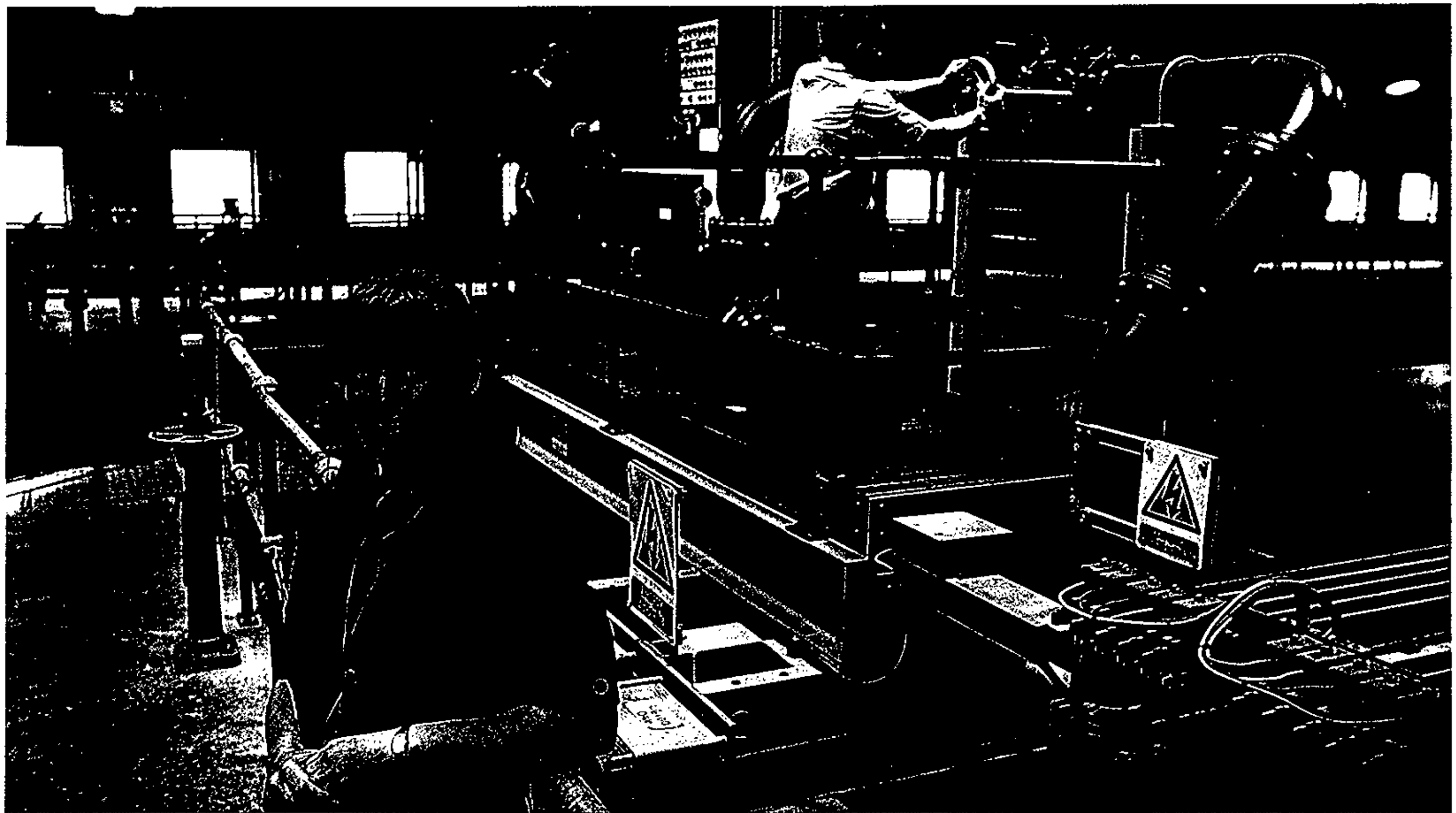
Our business planning process will continue to examine rigorously all aspects of our cost base, with the intention of continuing to be the most efficient water and wastewater company and delivering our regulatory outputs at lowest cost.



Efficiency wastewater (percentage) Source: Ofwat

Increasing customer satisfaction
We launched a radical new deal for customers which was welcomed by Ofwat and provides:

- cash payments of £6.50 a year to all customers we supply with water and wastewater services. It is worth a total of £90 million over five years and is a share of our past capital expenditure efficiency savings. The first payments were made to customers in May this year;
- extra investment of £180 million over the next five years to tackle priorities which concern customers, such as lead pipes, sewage flooding and smells, and poor water pressure. This is doing more than Ofwat allowed at the periodic review and will be paid for out of future capital expenditure efficiency savings; and
- commitments to higher standards of service, backed in many cases by compensation if we fail to meet them, to be paid for out of operating more efficiently.



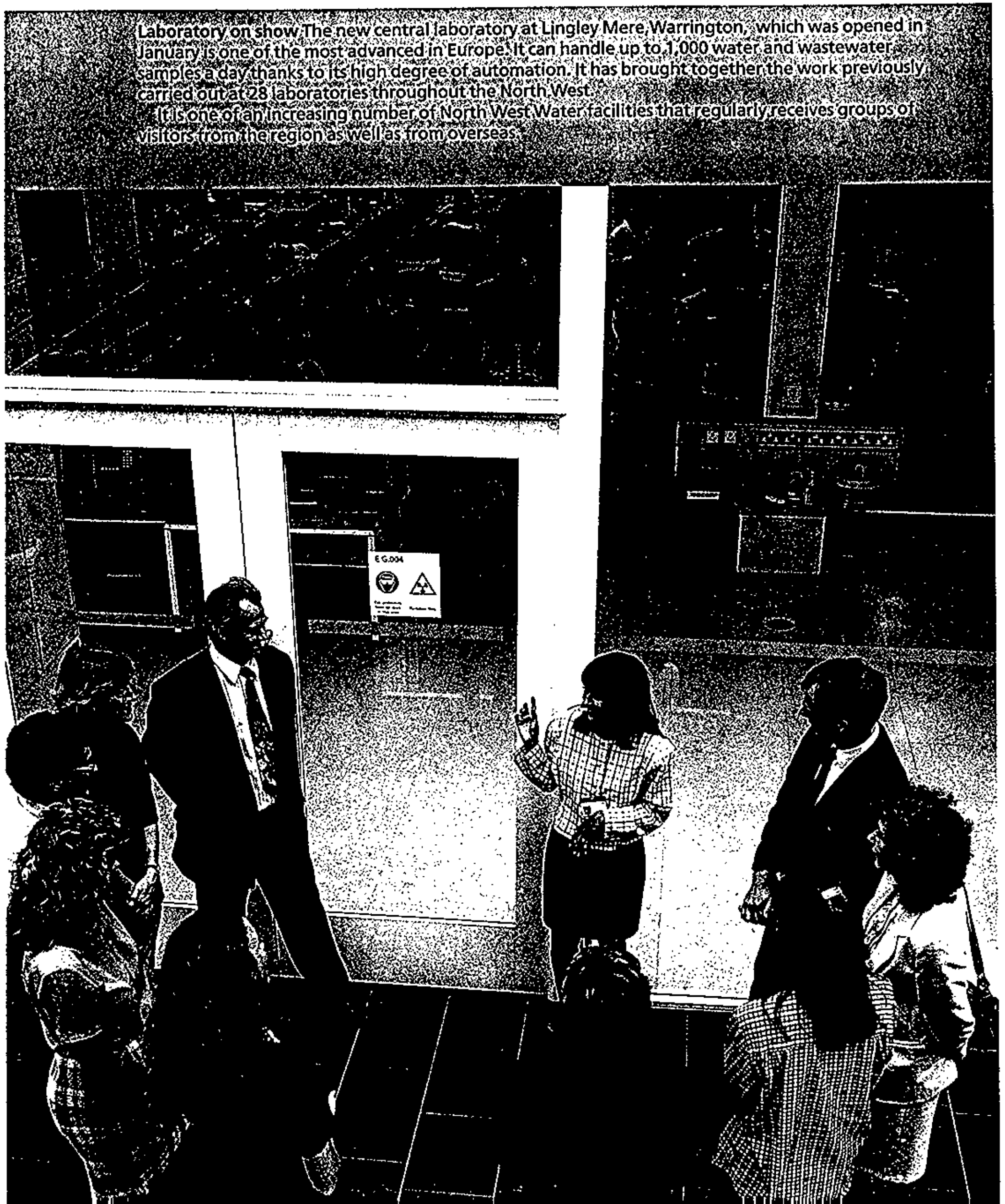
Territory managers A key element of our drive to work more closely with the communities we serve has been the creation of the new post of territory manager – 39 have been appointed to become the local "Mr or Ms North West Water", responsible for our operational and community activities within a specific area.
The managers took up their posts in August 1994 after the completion of a successful pilot scheme in Blackburn. One of them is Clare Whatley, who joined us under our graduate recruitment scheme and is now territory manager for the central Lancashire area. She is seen here during one of her regular visits to our new Rivington water treatment works.

We have embarked on a series of annual surveys to monitor and analyse customers' views and help us to measure and improve our performance.

That we 'listen and consult' will be a major theme of our communications with customers, which includes the use of regional television and press advertising as part of our public information campaign.

These new initiatives are underpinned by continued improvements in our service performance. We rose from tenth to seventh place in the 1993/94 league table of customer service standards compiled by Ofwat, the largest improvement of any of the companies.

The new customer services centre at Lingley Mere, Warrington, was officially opened in February and the phased transfer of activities from other offices will be completed over the next two years. The centre already houses over 500 staff handling more than



Laboratory on show The new central laboratory at Lingley Mere, Warrington, which was opened in January is one of the most advanced in Europe. It can handle up to 1,000 water and wastewater samples a day thanks to its high degree of automation. It has brought together the work previously carried out at 28 laboratories throughout the North West.

It is one of an increasing number of North West Water facilities that regularly receives groups of visitors from the region as well as from overseas.

1.6 million accounts and dealing with services enquiries from customers.

Water supply Every day we purify and supply about 2,400 million litres of water at 154 treatment works. During 1994, we made over half a million measurements of water quality and over 99 per cent of all samples complied with standards.

In the year, we invested £52 million on water treatment improvements and completed construction or major refurbishment at 13 water treatment works serving just over a million customers. We invested £83 million in water distribution, laying 230 kilometres of new mains, renewing or relining 550 kilometres of mains, providing over 55,000 new communication pipes and improving pressure for over 3,300 properties.

Water quality for more than a million customers has been improved by the introduction of an ozone plant at Oswestry, which supplies 205 million litres a day to Cheshire and Merseyside. The second largest in the UK, it has attracted interest from abroad.

Water resources Ofwat ranked us equal first in the industry in terms of adequacy and availability of supply to our customers, without restriction. Our water resources are considered adequate for our needs for the foreseeable future.

Wastewater During 1994, we again achieved a very high degree of compliance with National Rivers Authority consents for discharges from our wastewater treatment works, water treatment works and storm tanks. 98 per cent of final effluent samples complied with their consent conditions, and bathing water compliance was much better than in previous years with 24 of the region's 33 designated bathing waters meeting EU standards.

We invested £157 million in wastewater treatment projects, completing improvements to seven works providing treatment for a population equivalent of 1.8 million, and over £33 million on sewerage. This included the renovation of 18 kilometres of critical sewers and reduced the risk of flooding from sewers for over 335 properties. Over 140 kilometres of new sewers have been laid.

Sea Change, our £500 million coastal clean-up project, is being vigorously progressed. As part of the £150 million Fylde coast scheme, construction work began last summer on the new wastewater treatment works at Fleetwood and on the 11.7 kilometre long interceptor tunnel from Fleetwood to Blackpool.

In Cumbria, wastewater treatment improvements have already been completed at five locations and work is underway or due to start on a further eight.

In Liverpool, work is on schedule on the 21 kilometre interceptor sewer which will take wastewater to the treatment works at Sandon Dock. This will end the age-old practice of direct discharge to the estuary. The final phase of this £115 million scheme should be completed in 1996.

A public enquiry has begun into our proposal to build a sludge processing and incineration plant at Shell Green, Widnes, and the result is expected in autumn 1995. The £100 million plant will be essential to fulfil our obligation to end disposal of sludge at sea in 1998.

Employees The major progress we have made during the year would not have been possible without the support and dedication of our employees. They have been responsible for delivering the actions that have brought significant improvements in both the service we provide our customers and our business performance.

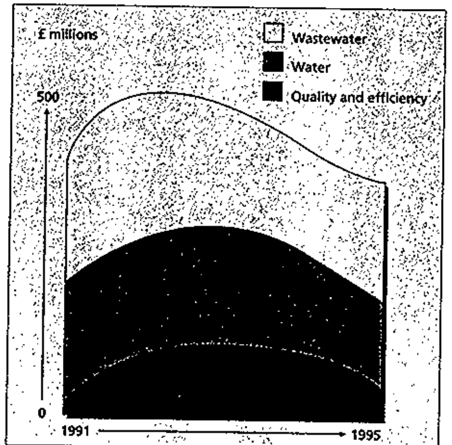
A key to this has been the investment we continue to make on training within the UK Utility Division. For the second successive year we won a National Training Award for our programme to create multi-skilled craftsmen. We also began to consolidate and take forward a drive for excellence, implementing a strategy based on the self-assessment model of the European Foundation for Quality Management.

Pipeline, the employee suggestion scheme, continued to grow and a North West Water employee again won a UK Association of Suggestion Schemes trophy for the best environmental idea.

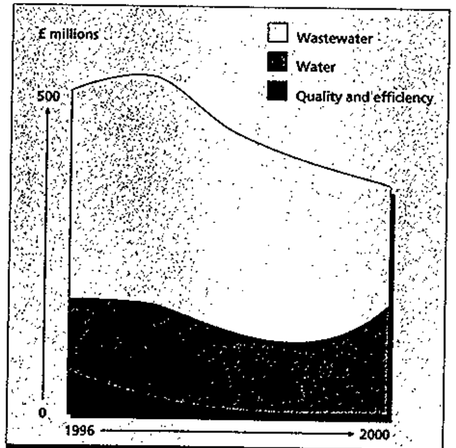
We also received eleven national and international awards for a wide range of community and public relations activities.

Energy initiatives implemented at Wigan wastewater treatment works won a British Gas Energy Management Award.

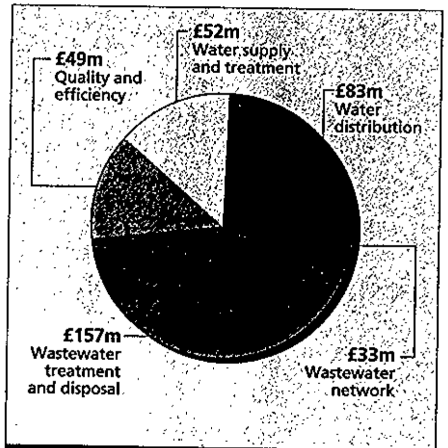
Many health checks for our employees can now be done in the workplace, thanks to a newly commissioned mobile health unit.



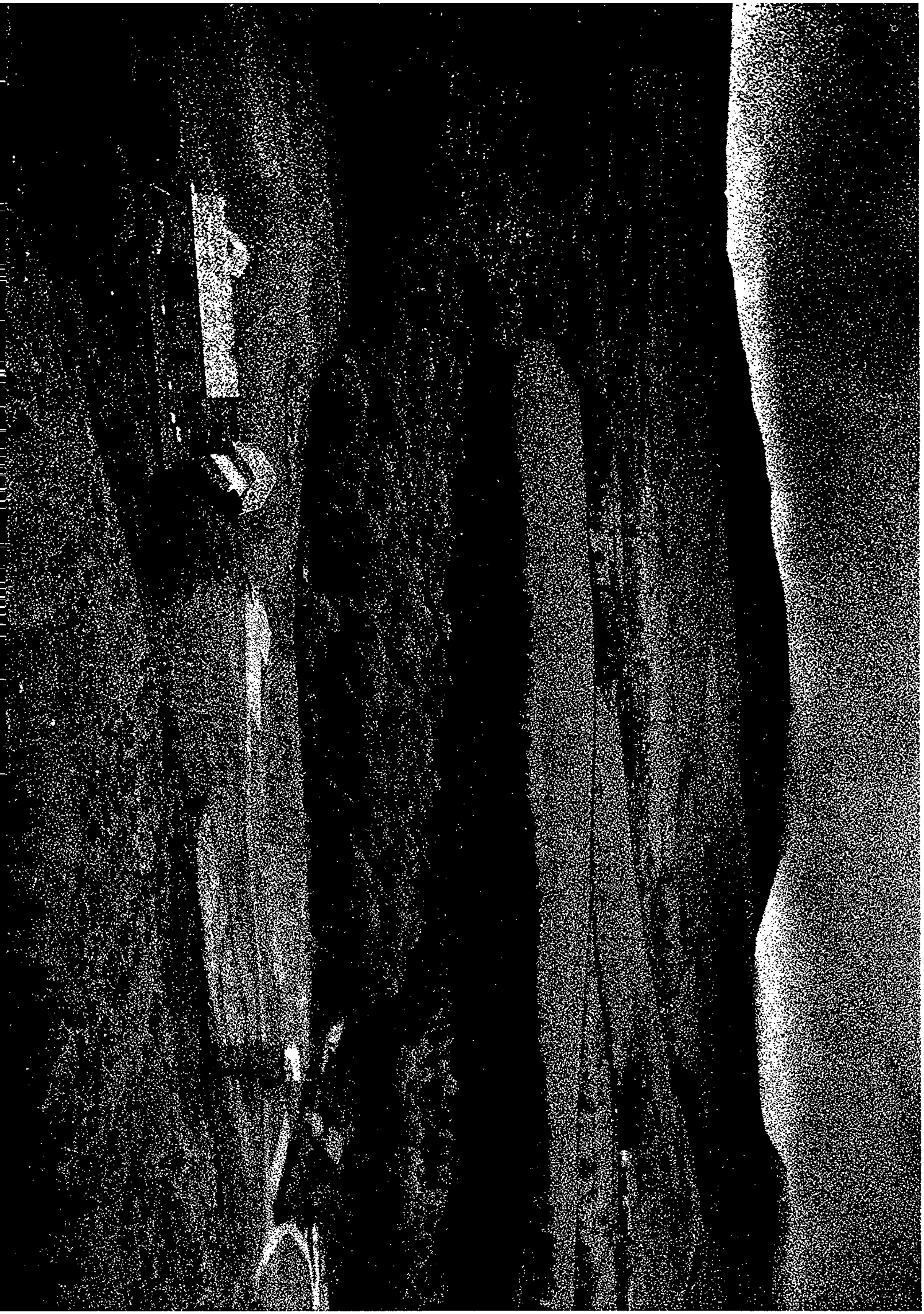
Analysis of investment 1991 – 1995

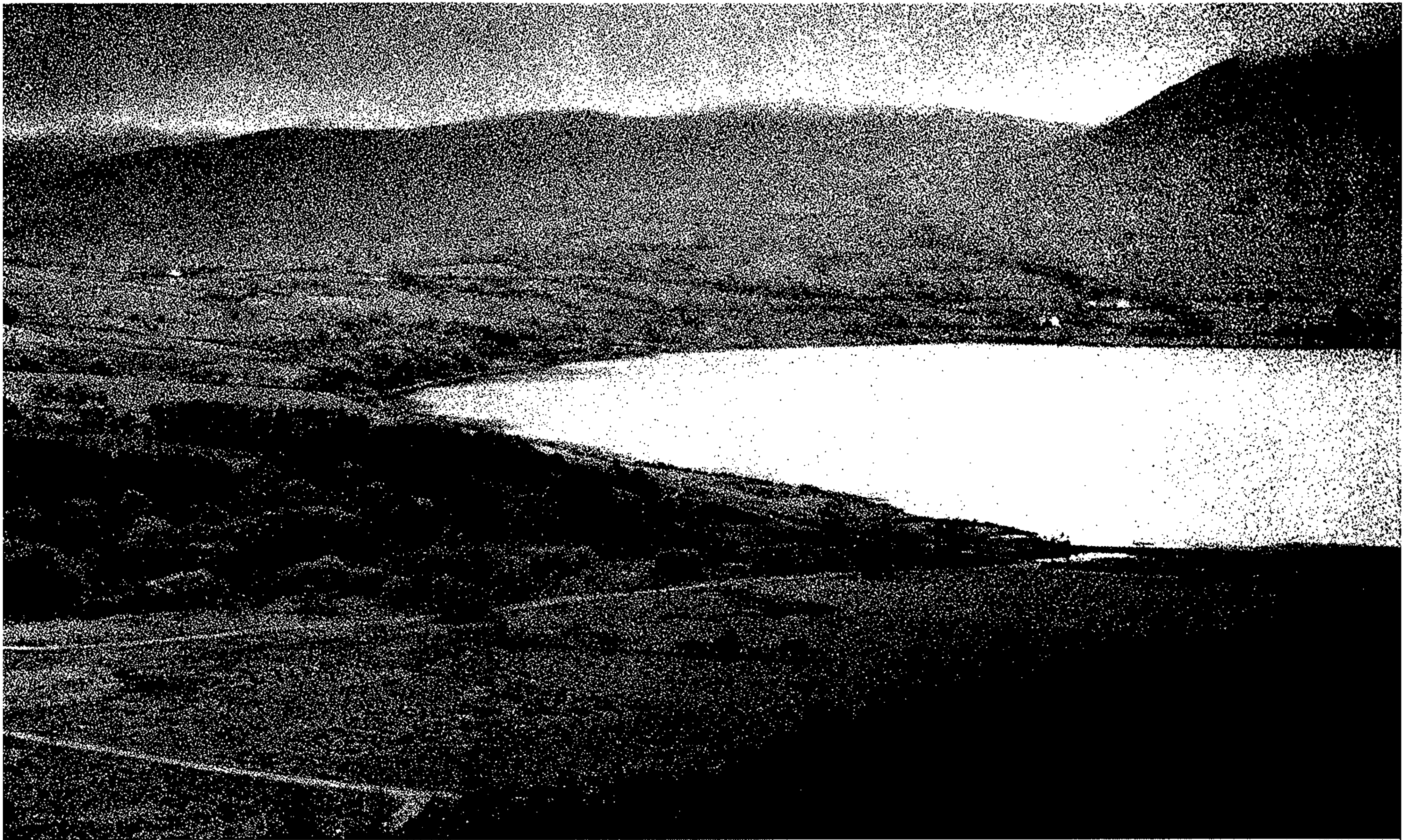


Analysis of investment 1996 – 2000



Analysis of investment 1995 £374m





Ennerdale Water in the English Lake District. A traditional Lakeland 'farmhouse' nestling in the remote and unspoiled Ennerdale valley disguises our state-of-the-art water treatment works. His Royal Highness The Prince of Wales, who opened the plant in May, said he was delighted by the sensitive way in which it had been built to ensure so little impact on the environment of one of the Lake District's most beautiful valleys.

That care is typical of our approach to planning new works and up-grading old ones in urban areas as well as in the countryside.

Picture courtesy of The Independent/Brian Harris

International Division

"Our goal is to grow a successful and profitable business by meeting the needs of communities around the world for the supply of safe drinking water and for the cleansing of wastewater to protect health and the environment."

Robert Ferguson *Acting Managing Director* International Division

Dr Gerald Orbell (left) was appointed Managing Director of the International Division on 1 May 1995 when he took over from Acting Managing Director Robert Ferguson, Group Finance Director

Yan Yean water treatment works opened ahead of schedule

Focus on consolidating contracts in Malaysia, Mexico and Australia

US Water increased sales during the year by 40 per cent

International partnership with Bechtel

The year was a period of consolidation. Very few opportunities emerged which sufficiently matched our demanding criteria for involvement. We have concentrated on optimising the operation of the contracts previously won. At the same time, we have continued our pro-active approach to the development of potential opportunities in those parts of the world we believe present a fertile market for our services.

Management During the year, we established a core team of internationally experienced professional managers to take the business forward. This culminated in May 1995 with the appointment of Dr Gerald Orbell, who has wide international experience, to lead the Division in what we expect will be a decade of intense activity.

World market The demand for the services the Division can provide is enormous. Statistics from the World Bank indicate that:
- one billion people lack access to safe drinking water; and
- two billion people lack adequate sanitation.

By any measure, the water and wastewater infrastructure requirements of the developing and developed nations of the world present a substantial challenge and opportunity for the foreseeable future.

The three criteria we apply as we seek to develop any opportunity are political and economic stability, political will to involve the private sector and, finally, affordability.

Affordability This, above all else, is the greatest challenge. Often, the countries that desperately need to improve, or indeed to establish, even basic water and wastewater services are those that can least afford it. We have spent much of the year in discussion with those bodies which can help to solve this dilemma. These include the World Bank, the International Finance Corporation, other multilateral funding agencies and the government departments that can facilitate the necessary sovereign support which will help to ensure that third party sources of finance will be available at a reasonable cost.

Our successes to date have shown that we have the capability and the expertise to deliver on time and within budget. Our challenge is not only to maintain that record but also to use it to our competitive advantage for the future.

Bechtel partnership We are developing with Bechtel our team approach to international business to ensure that our combined strength will be greater than the sum of the two parts.

Internationally, the partnership will build on our foundation of experience in the UK, Australia, Malaysia, Mexico and Thailand and Bechtel's extensive experience from working in more than 135 countries.

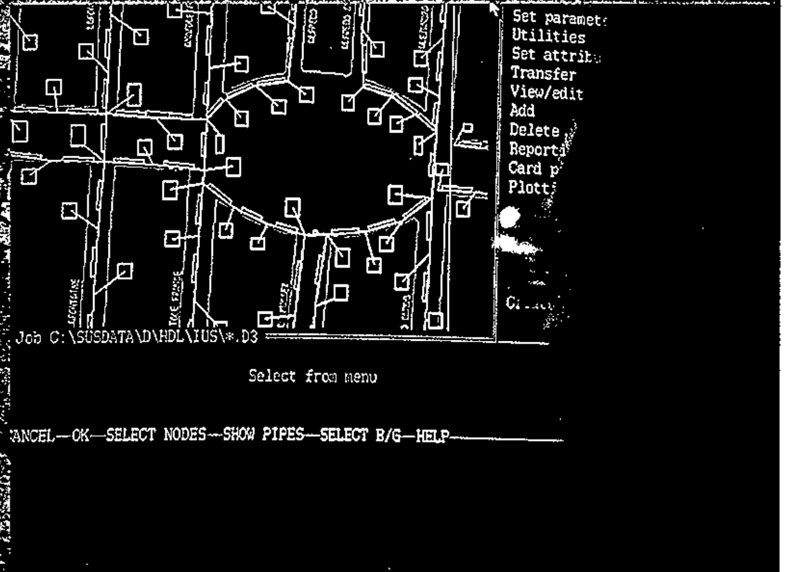
We are in the process of devising the scope and strategic direction of the joint development company to pursue opportunities in water and wastewater globally. Work has already begun on three prospects, in Indonesia, Argentina and Kuwait.

Progress on contracts Our portfolio of contracts is already contributing to earnings, following consolidation of

Mexico City Widespread installation of an electronic metering system will reduce needless waste, increase revenue and help alleviate the city's serious water shortage.

The latest computer aided design technology is being used by Agua de Mexico to help in the more efficient management of the water and drainage networks.

Vans equipped with computer systems able to scan meters by radio will read up to 5,000 meters in an hour.



operations in Melbourne, Mexico City and Malaysia.

After an intense period of securing contracts worldwide in the early 1990s, the focus in the year was on consolidating our position and investing high levels of energy and expertise to guarantee quality performance.

Australia The water treatment works at Yan Yean, Melbourne, was officially opened in December 1994, after one of the shortest design and construction periods ever achieved on a project of this type in Australia. The project was completed within budget and has the capacity to deliver 155 million litres daily to 300,000 people. The Macarthur water treatment works in Sydney began trials well ahead of the plant being commissioned in September 1995. When fully operational, Macarthur will supply 265 million litres of water daily to a rapidly growing suburb of Sydney with a population currently in excess of 400,000.

Malaysia In Malaysia, Indah Water Konsortium, for which we are the operator, is currently responsible for the operation of some 1,700 sewage treatment works and about 2,600 kilometres of sewers serving more than six million people in 63 local authority areas. The terms of the concession agreement provide for wastewater treatment for the entire country to be controlled by Indah Water by 1 June 1996.

Both water treatment works in the city of Ipoh, which we have operated since 1988, continue to perform well.

Mexico Progress on our Mexican contract has been slower than we had anticipated a year ago, due to the protracted negotiations between the client, the Federal District of Mexico City, and their financiers, which are only now drawing to a close. Having said that, of the four international consortia that each have a contract for one quarter of the city, our joint venture, Agua de Mexico (of which we own 49 per cent) has taken the lion's share of the available budget. Almost all the initial census and mapping work has been completed in our concession area and over 65,000 remote radio-read meters have been installed.

Agua de Mexico will be the first of the four concessionaires to commence the second phase of the contract – meter reading and billing – in the next few months, an encouraging indication of our progress. Contract revenues are largely protected from the impact of the recent financial upheavals in Mexico and every effort has been made to ensure that the high cost of interest is minimised wherever possible.

US market A 40 per cent increase in US sales made for a promising year for US Water, which was awarded a 10 year operation/maintenance contract in Pennsylvania for the city of Easton's water and wastewater facilities. This contract, which serves some 80,000 people and businesses, is the largest of its kind to date in this State. US Water's tenure has had a positive impact on the performance of the wastewater works, bringing into line this facility which had not met operating compliance in seven of the 12 months prior to our stewardship.

The US market has been restricted to short-term operation and maintenance contracts as a result of restrictions in State and Federal regulations. Regulatory changes anticipated this year are expected to remove existing impediments to the full scale privatisation of the £13 billion per year US water and wastewater market. US Water is well positioned to take advantage of this enormous opportunity.

Consultancy Consultancy work – notably in Lahore, Pakistan and Lagos, Nigeria – continues to perform well. We offer independent consultancy on all operational aspects to strengthen the management of existing water utilities.

Future development We have sought to project an image and maintain a reputation that is consistent with our international ambitions. In communicating with our key audiences, we have also sought to raise awareness around the world of the advantages, both economic and social, of privatisation.

Process Equipment Division

"Our aim is to grow profitably by providing the best integrated process solutions to municipal and industrial customers worldwide."

John Beckitt *Managing Director* Process Equipment Division

John Beckitt (centre) on a visit to Malaysia to discuss with local partners the supply of Envirex equipment for wastewater treatment

Division integrated as a single business

Sales increased by 8 per cent

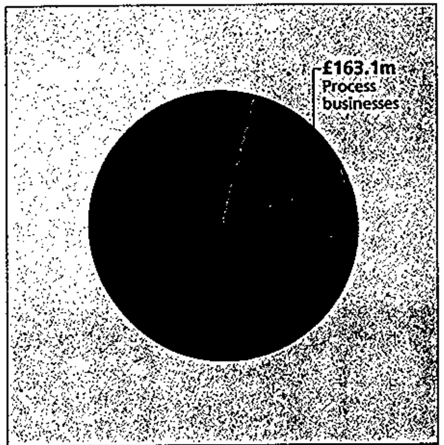
Companies develop innovative membrane filtration plant

In USA, Wallace & Tiernan recorded its largest ever sale

The world market for the Division's products and processes is estimated today to be worth around £7 billion and we expect it to grow to around £9 billion by the year 2000.

North America represents almost half the world market, with Europe around one third and the Middle East, Africa and Asia Pacific accounting for the balance. Within five years, we anticipate that these three major world regions will each account for one third of the total market.

The Division has a very substantial presence in North America and is well positioned in Europe. As the Asia Pacific region will grow rapidly over the coming decade, the Division is positioning itself for a substantial share of that growth.



Turnover 1995

Business performance Overall results for the year saw sales increasing by 4.6 per cent (8.3 per cent excluding the adverse effect of exchange movements) from £155.9 million to £163.1 million. Operating profit grew by 4 per cent despite the difficult trading conditions in certain key markets and our investment in product development, restructuring and territorial expansion.

Management During the year, the process businesses have been brought together into a single integrated business Division. Its organisation structure reflects the major world regions with regional directors responsible for the Americas; Europe, the Middle East and Africa; and the increasingly important Asia Pacific region.

Our goals are to internationalise the Division's business, accelerate the introduction of new products, further exploit the industrial market and capitalise on the integration of the companies within the Division.

Mexico Wallace & Tiernan and Acumem have worked together to develop a membrane filtration plant; its product, treated wastewater, is used to irrigate the Xochimilco agricultural area to the south west of Mexico City.

Some 2,000 filtration units are required for this project. The technology is unique in its capability to reduce the salt content of water, so that it is suitable for crop irrigation.

Integration In the past year, the benefits of integration have been clearly demonstrated and the pace has increased significantly.

In Mexico, a collaboration between Wallace & Tiernan and Acumem, the Group's membrane specialist, resulted in the commissioning of a highly innovative membrane filtration plant, which treats wastewater which is being used to irrigate the Xochimilco agricultural area south west of Mexico City.

In Canada, filtration technology developed by General Filter was supplied by Wallace & Tiernan to the Quebec region.

In Brazil, Wallace & Tiernan have secured substantial orders for process equipment for the treatment of wastewater. This equipment and process know how was supplied by Envirex, the Division's specialist in biological treatment processes.

To facilitate these synergies, we have established business teams whose task it is to internationalise our broad range of products and processes.

Business improvements and sales
The year has been characterised by a major programme of improvement initiatives, including the reorganisation of a number of our businesses and the achievement of ISO 9000 and equivalent third-party certifications.

At Envirex, the first phase of a programme of business process re-engineering has been completed. Despite the inevitable disruption caused by a change programme affecting every part of the business, sales at Envirex grew by 11 per cent in the year.

Underpinning this performance was the award of major contracts for on-site wastewater treatment processes for industrial customers. Sales of Envirex equipment and processes in the UK, Thailand, Israel and Brazil emphasised the global appeal of its products.

Wallace & Tiernan, the Division's chemical feed and disinfection specialist, recorded its largest ever equipment sale to a single customer in the US domestic market, where sales increased by 5 per cent in the year. Sales in Mexico and Brazil were especially encouraging, with Brazilian sales growing by 200 per cent from a small base.

The home market for Wallace & Tiernan's UK operation was flat but the business was successful in its export markets, with sales to southern Africa, the Balkan States, Russia and the Ukraine contributing significantly.

Wallace & Tiernan's German operation experienced a slow-down in sales, primarily due to the downturn in the German market.

Wallace & Tiernan's Asia Pacific operations showed good growth, thanks to the rapidly developing market in that region.

We anticipate an acceleration of Wallace & Tiernan's growth across the world as it completes a major programme of product development. The coming year will see its fastest ever rate of new product introductions.

General Filter, the Division's potable water filtration specialist, maintained its strong position in the North American market. Sales to the UK, Australia, Canada and Brazil herald the beginning of the internationalisation of its business. In the US, General Filter won its second largest ever order in the face of fierce competition from its US-based rivals.

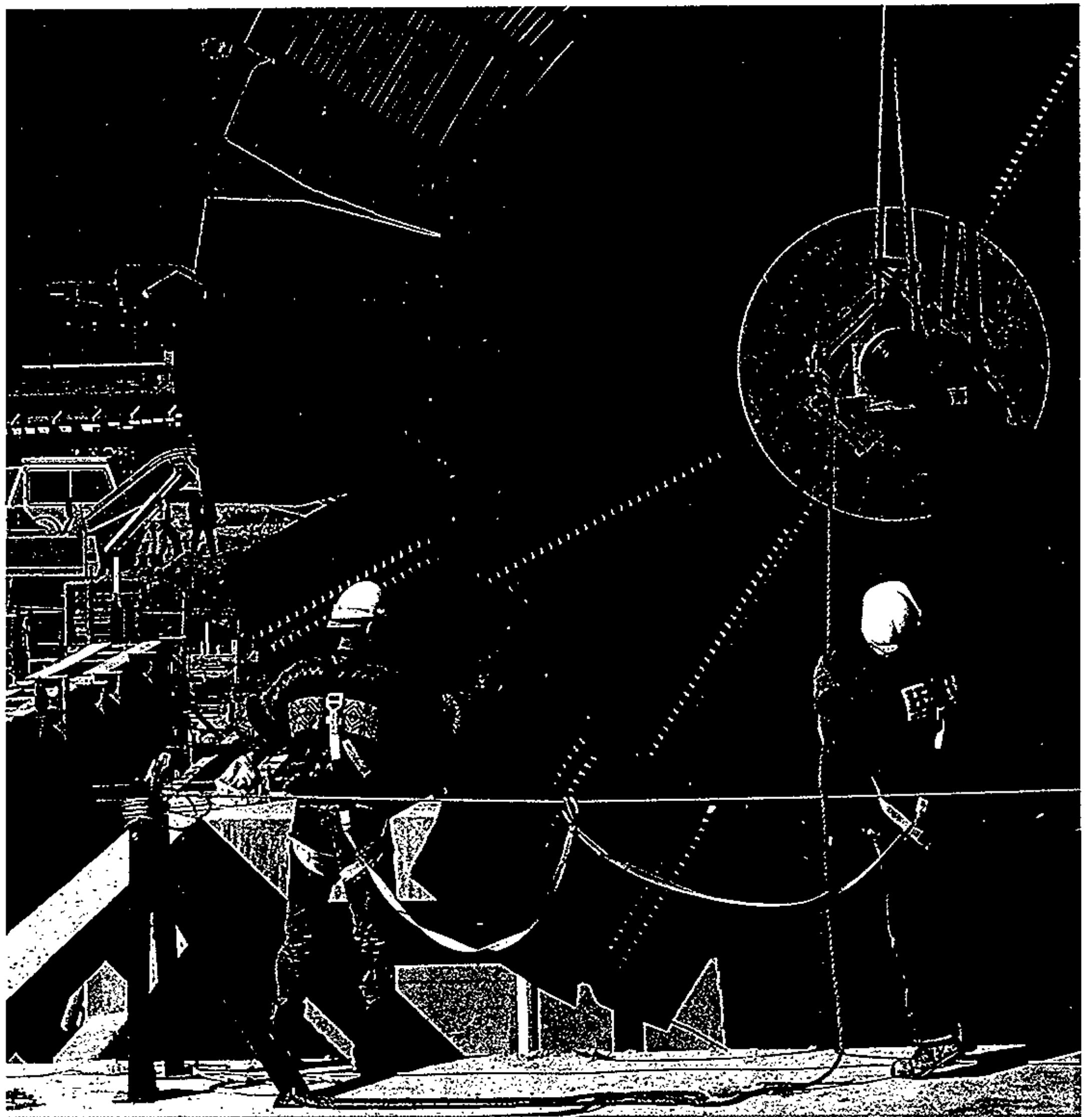
Edwards & Jones, the Division's filter press specialist, achieved sales growth of 38 per cent in the year. A highlight was the award of a prestigious contract for filter press plant at Thames Water's Beckton and Crossness wastewater treatment plant.

Asdor, the Division's Toronto-based solids handling specialist, aggressively increased its order intake by 400 per cent for the year. Prospects remain good for the current year, with Asdor opening with a 50 per cent increase in order backlog.

Acumem continues to develop innovative water and wastewater treatment systems based on its proprietary membrane technology. During the year, working with our process businesses, Acumem commissioned water treatment plants on sites in the UK, the US and Australia. Results from these trials are very encouraging.

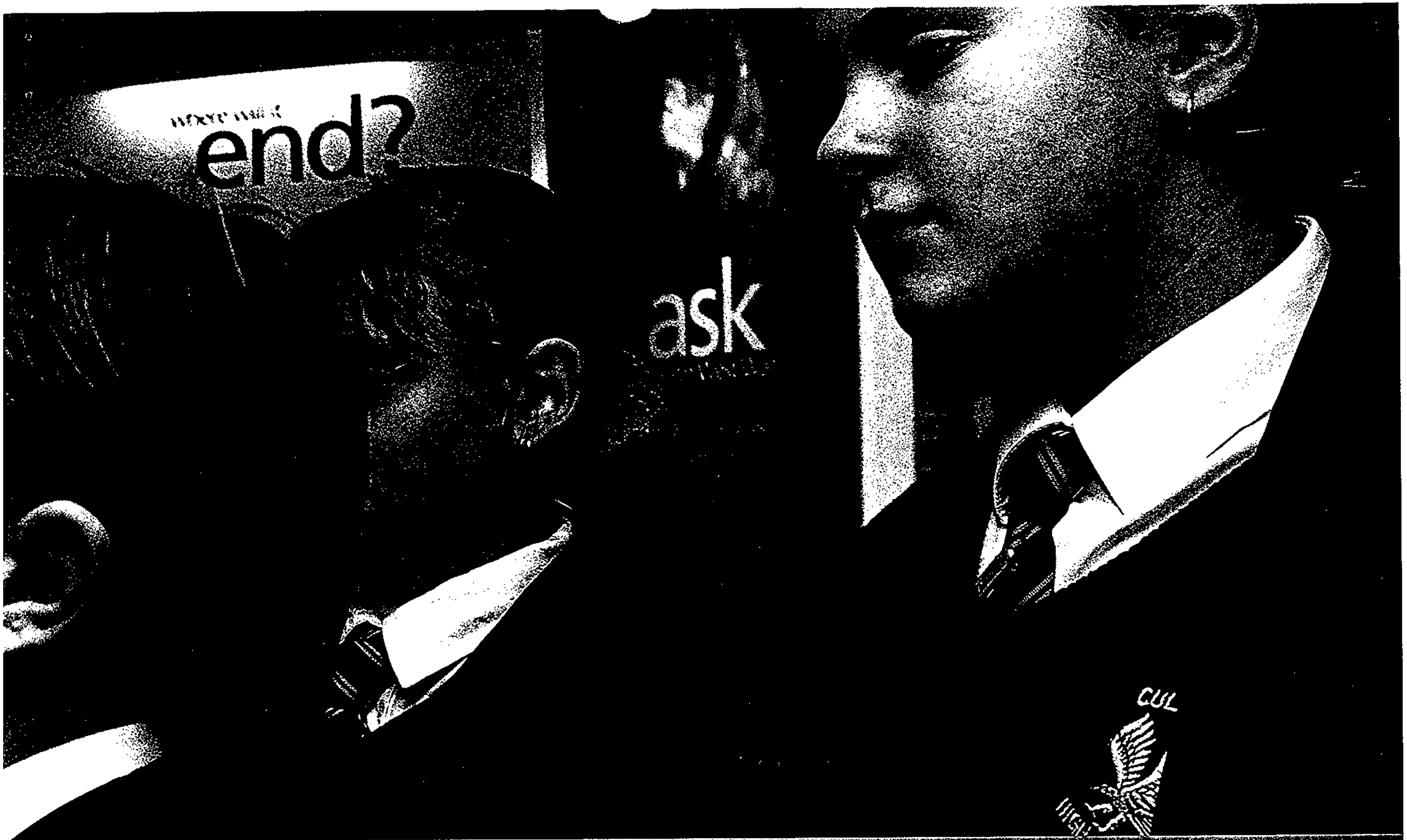
Acumem's sales of membrane systems for industrial applications grew strongly during the year and, overall, sales grew by more than 100 per cent. Acumem's results are included in the segmental analysis (page 43) under "Other activities".

Future development We are committed to achieve significant improvement in the Division's performance. We expect our new initiatives, the organisation we now have in place and our aggressive internationalisation and integration programmes will accelerate growth in sales and earnings in the coming years.



Cost saving technology During the year, increased sales of Envirex equipment and processes confirmed the appeal of the company's products, like this submerged biological contactor unit in Fleetwood, Lancashire. The use of this technology provides substantial economic and operating advantages over more conventional methods, including lower construction and running costs and minimal maintenance.


drain
keeps



Keeping our customers informed about what we do is a priority. Our mobile visitor centre is one of the most advanced and adaptable units of its kind in the country. It contains a permanent exhibition as well as a mini theatre for audio-visual presentations and a working model of the water cycle. It went on the road in October 1994 and since then has welcomed almost 20,000 visitors.

The interactive displays are particularly popular with children and the centre is in great demand for visits to schools. The exhibition reinforces the message of the importance of water in our lives.

The centre also tours areas where we are carrying out construction or rehabilitation work. Dedicated exhibitions show customers what work is going on and specialist staff are on hand to answer questions.

The community

We are committed to ensuring that we have a positive impact on the communities we serve through a range of activities which complement our operational role as a provider of water services.

Community programmes win national recognition

Extra support for Business in the Community

New environmental classrooms tell story of water

Improved access and facilities on our land

Our community relations policy focuses on education, community leadership and care of the countryside. Highlights in the year in the North West of England have included:

Education Our educational work concentrates on improving understanding of the water cycle and its importance to public health and to the environment.

The effectiveness of our work was recognised when we became the first overall North West winners of the Aim High Award. This is a national competition, run by Business in the Community, which highlights partnerships between businesses and schools.

We were also commended by the Institute of Public Relations and the Association for Business Sponsorship for the Arts for our support for the Walk the Plank ship-based theatre company. Their play about the place of water in people's lives was seen by over 10,000 schoolchildren in the region.

We opened our second environmental classroom, at Pex Hill near Widnes and began design work on a third at Hope Carr, near Leigh, to cater for secondary and higher education students. Over 3,000 schoolchildren have visited our classrooms this year. We plan to open two more in the next two years.

Our teacher placement programme has continued to be oversubscribed and we have introduced the new role of education co-ordinator and now have nearly 60 employees who liaise with local schools to arrange talks and visits.

Community leadership As one of the largest businesses in the North West, we work with organisations such as Inward, the Chambers of Commerce Association, the North West Business Leadership Team and the North West Tourist Board to support and promote the economic development of the region, in the UK and overseas.

Our community support is not confined to providing funding. We also give our time, employee expertise and facilities.

We have provided Business in the Community with offices and have seconded one of our managers to work for them full time on environmental matters. Many of our employees help local charities or voluntary organisations and we have introduced a Community Challenge Award to support this.

Amongst the major events we have supported were the National Trust's centenary year celebrations in the Lake District; the Corporate Forum for National Parks' annual seminar; and Morecambe's World of Drama and Music arts festival. We continue to support the Mersey Basin Trust.

Our Thirsty World fund-raising initiative for Ethiopia has now collected over £250,000 and has won the Institute of Public Relations' national Sword of Excellence award for best community campaign.

Care of the countryside As one of the North West's largest landowners, we work hard to protect and enhance the natural and man-made heritage in our care and continue to improve public access to our land and recreational facilities at our many sites.

We have maintained our annual funding of the British Trust for Conservation Volunteers, who carry out a wide variety of tasks for us, from fencing and tree-planting to repairing footpaths. We continue to fund the county Wildlife Trusts to manage our nature reserves and the Royal Society for the Protection of Birds to monitor and protect the rare birds of prey on our land.

We promote free public access to all our land, within operational and conservation constraints, but the increasing popularity of walking is taking its toll on the landscape. Major conservation projects in the year have concentrated on repairing eroded footpaths on Helvellyn, in the Lake District and on Anglezarke Moor, in the West Pennines.

Access to our land for people with disabilities is a particular priority and we are now working with the Fieldfare Trust, who are advising us on how access can be improved.

Access to the countryside Providing carriage rides for wheelchair users at a countryside activity day at Dunham Massey, Cheshire, is just one example of our work with people with disabilities.

We are increasing our contacts with disabled groups throughout the North West so that we can listen to and learn from their requirements as countryside users. We are also training our conservation staff and agency rangers to be more aware of the problems of access which people with disabilities can face.

The environment

Concern for the environment is an integral and fundamental part of our corporate business strategy. We are committed to safeguarding and improving the public health and the environment of the communities in which we operate and serve.

Progress as leading environmental contractor

Policy adopted for whole Group

Seven key commitments

New health and safety initiatives

As the North West of England's leading environmental contractor, we are bringing about the biggest and most dramatic improvements to the quality of water since the pioneering work of the Victorians.

And as we turn the tide of pollution, the positive changes in our rivers and coastal waters are clearly to be seen with the return of species of fish and other marine and bird life.

The £2.5 billion investment programme of the UK Utility Division over the last five years has brought major improvements to the quality of drinking water supplied to our customers in the North West of England and to the environment, which receives the 2,600 million litres of wastewater we treat in the region each day.

Our attention to environmental issues in the UK Utility Division is now being extended to our other two business divisions, following Board endorsement of a comprehensive environmental policy for the Group as a whole.

Among our specific commitments we will develop, design and operate facilities taking into consideration the efficient use of energy and materials, the sustainable use of renewable resources and the minimisation of adverse environmental impact.

We will also search for and employ low-polluting technologies whenever reasonably practicable, and adopt waste management practices including source reduction, recycling and safe disposal.

Each company within the Group has been tasked to prepare and review annually a plan for complying with this policy. Environmental performance will be monitored and reported at regular intervals to the Board, shareholders, employees, customers and the community at large. External suppliers of services and goods will be encouraged and, where appropriate, required to adopt the principles of this policy.

The environmental policy will complement that previously adopted for health and safety. We believe that injuries, occupational illness and damage to property can be prevented. We are determined to bring about safe working practices in all our activities around the world, and to see that employees, customers and the general public are not harmed by our activities, services or products.

Health and safety are no less important than any other measure of business performance. We have made considerable strides in the implementation of this policy since its inception in 1991, with sharp improvements in accident and lost-time performance. The Royal Society for the Prevention of Accidents' "Gold Award" presented to the UK Utility Division in June 1994 recognised the major improvement in safety achieved over a number of years. The December award of a Sword of Honour from the British Safety Council to NWW Engineering was equally encouraging.

A number of our companies succeeded in avoiding any lost-time accidents during the year. However, our safety performance overall during the year has not reached our highest expectations, with lost-time accidents to our employees 7 per cent higher than in the previous year.

Health and safety are firmly at the top of our management agenda and, driven forward by a series of new initiatives, we expect once again to match the progress of previous years.

Environmental policy

Principles

North West Water Group is committed to safeguarding and improving the public health and the environment of the communities in which it operates and serves worldwide. Concern for the environment is an integral and fundamental element of our corporate business strategy.

We will adopt environmentally responsible policies and practice throughout all our operations.

We are committed to the development and use of products, processes and services which reduce environmental damage and waste, and which conserve non-renewable resources.

We recognise our obligation to inform all our stakeholders of our policies, practices and performance in environmental matters.

Corporate objectives

It is the express policy of the Group to:

- develop, design and operate facilities and conduct activities taking into consideration the efficient use of energy and materials, the sustainable use of renewable resources and the minimisation of adverse environmental impact (including noise, odour, other emissions and visual intrusion).
- search for and employ low-polluting technologies whenever reasonably practicable, and adopt waste management practices including source reduction, recycling and safe disposal.
- meet all relevant national and local statutory obligations, working closely and constructively with regulating agencies, community interest groups and other institutions concerned with environmental issues.
- regularly monitor environmental performance and periodically provide appropriate information to the Board, shareholders, employees, customers and the community at large.
- develop and maintain emergency procedures, in co-operation with the appropriate external agencies and local community, for responding to major hazards.
- advise and, where relevant, educate customers, distributors, partners and the community at large on environmental issues associated with our products and services; and remain aware of local, national and global issues.
- recognise our obligations to conserve and protect the natural environment and, where appropriate, create opportunities for recreation by the local community.

Board of directors

Executive directors

Sir Desmond Pitcher *Chairman* (60)
Chairman of the Merseyside Development Corporation and a non-executive director of National Westminster Bank. Formerly group chief executive of The Littlewoods Organisation, and managing director of Plessey Telecommunications and Office Systems and of British Leyland (truck and bus division).

Brian Staples *Chief Executive* (50)
Formerly chief executive of Tarmac Construction and previously managing director of Tarmac Construction.

Robert Ferguson *Group Finance Director* (52)
Formerly deputy managing director and previously finance director of North West Water Limited.

John Beckitt *Managing Director of the Process Equipment Division* (47)
Formerly international business manager of ICI Klea.

Derek Green *Managing Director of the UK Utility Division* (55)
A non-executive director of Graham Group. Formerly Aggregates Group chief executive of BTR. Previously with AMEC and Fairclough Building.

Non-executive directors

Clare Bolton (43)
A tax partner at Coopers & Lybrand.

Eric Clark (60)
Chairman of BICC Cables, a director of BICC Group and a non-executive director of the Merseyside Development Corporation and of the Dana Corporation. Formerly managing director of Plessey Telecommunications and Office Systems.

Dr Rodney Leach *Chairman of the Audit Committee* (63)
Formerly a partner in McKinsey & Company, an executive director of P&O and chief executive and managing director of VSEL.

Sir Peter Middleton (61)
Chairman of Barclays BZW division, deputy chairman of Barclays Bank, a non-executive director of Bass and of General Accident and a member of the UK Advisory Board of the National Economic Research Associates. Formerly Permanent Secretary to H M Treasury.

Alan Pendleton (66)
A non-executive director of Independent British Healthcare and of Nord Anglia Education. Formerly managing director of West's Group International and a director of Tilbury Group.

Frank Sanderson *Chairman of the Remuneration Committee* (68)
Chairman of Acumen Technologies. Formerly divisional managing director (water engineering division) of Babcock International.






Directors' report

Principal activities North West Water Group is engaged in the planning, design, manufacture, installation and operation of water and wastewater systems and equipment in the United Kingdom and overseas.

The Chairman's statement, the Chief Executive's review and the financial, divisional, community and environmental reviews to be read in conjunction with this report, appear on pages 4 to 33.

The Group's principal operating subsidiary and associated undertakings are listed in note 12 to the accounts.

The disposal of NWW Engineering Limited to Bechtel Holdings Limited was completed on 8 April 1995.

Profit and dividends The results for the year, set out in the consolidated profit and loss account on page 39, show a profit on ordinary activities before tax of £284.0 million (1994 – £269.0 million), after making a restructuring charge of £11.8 million (1994 – £12.0 million) and providing for a goodwill loss of £13.5 million (1994 – nil) on proposed disposals. After a taxation charge of £24.8 million (1994 – £8.7 million), the profit for the year attributable to ordinary shareholders was £259.2 million and the retained profit of £165.3 million was transferred to reserves.

The directors recommend a final dividend on the ordinary shares of 17.20 pence per share for the year to 31 March 1995 for payment on 3 October 1995 to shareholders on the register at the close of business on 16 June 1995. This dividend, together with the interim dividend of 8.35 pence per share paid on 24 February 1995, makes a total dividend for the year of 25.55 pence per share, an increase of 10.75 per cent over the dividend per ordinary share for 1994.

Special dividend As part of the sharing of the benefits of efficiency gains between shareholders and customers announced on 30 March 1995, the directors recommend a special dividend on the ordinary shares of 3.80 pence per share for the year to 31 March 1996 for payment on 3 October 1995 to shareholders on the register at the close of business on 16 June 1995.

Share dividend plan The directors have agreed to implement the share dividend plan, which continues to be successful, for the 1994/95 final dividend and the 1995/96 special dividend.

Fixed assets Changes in tangible fixed assets during the year are shown in note 11 to the accounts.

Share capital Details of the company's share capital are set out in note 21 to the accounts. Since 31 March 1995, 397,346 shares have been allotted on the exercise of options and at 8 June 1995, the company's issued share capital, credited as fully paid, was £377,489,770.

The special rights redeemable preference share of £1 previously held by HM Government was redeemed on 31 December 1994.

The directors have a general authority to allot shares given by resolution passed on 22 July 1994 and valid until 21 July 1999. The number of ordinary shares authorised to be allotted which remain unissued is 97,510,230.

A special resolution (resolution 7) will be proposed at the annual general meeting to renew for a period of 15 months or, if earlier, until the conclusion of the 1996 annual general meeting the directors' power to allot shares for cash other than *pro rata* to existing shareholdings. If passed at the meeting, the resolution will facilitate the making of any rights issue of shares and will also empower the directors to issue shares, for cash, up to 18,874,000 ordinary shares being 5 per cent of the issued ordinary share capital at 8 June 1995. The directors believe it is in the interests of shareholders that the directors should be given this limited authority, providing them with a prudent measure of flexibility to act in the company's interests.

At 8 June 1995, the directors were not aware of any notifiable interest in the issued ordinary share capital of the company.

The company is not a close company within the meaning of the Income and Corporation Taxes Act 1988.

Research and development Through research and development teams harnessing the skills and expertise of the UK Utility and Process Equipment Divisions, the Group is seeking to improve existing and develop new practical and cost-effective water and wastewater processes and products, which will benefit customers and the communities in which the Group works around the world.

Directors The present directors are listed on page 34.

Mrs M C Bolton will be retiring from the Board at the conclusion of the 1995 annual general meeting and is not seeking re-election.

Mr J W Beckitt, who has been appointed to the Board since the last annual general meeting, is recommended by the Board for re-election. Mr Beckitt was appointed Managing Director of the Process Equipment Division in September 1994 and appointed to the Board in April 1995. He was formerly international business manager with ICI Klea.

Mr D Green, the director to retire by rotation, will on the recommendation of the Board offer himself for re-election.

Mr Green has a service contract with the company terminable by the company on two years' notice. Mr Beckitt has a service contract with the company, which at the date of commencement of his employment with the company was terminable by the company on three years' notice. The period of notice required declines evenly over time to a period of one year's notice on the second anniversary of his appointment. Thereafter, one year's notice will apply.

Full details of directors' interests in ordinary shares are set out in note 5 to the accounts. From the end of the financial year until 8 June 1995 no change took place in those interests.

At no time in the year did any director have a material interest in any contract or arrangement which was significant in relation to the Group's business.

During the year, a directors' and officers' liability insurance policy was in force.

Employees The Group is committed to improving the skills and potential of its employees through training and development and to effective communications with employees through, for example, briefings and employee newspapers.

The Group is also committed to equal opportunities in employment irrespective of gender, marital status, race, creed or disability.

The employee sharesave scheme continued to be popular and a further opportunity to join was offered in December 1994 and 1,304 new savings contracts were entered into. The five year savings contracts under the first offer of the sharesave scheme matured in and from March 1995 and options over 1,493,431 shares have subsequently been exercised by 810 employees. Further details are given in note 21 to the accounts.

During the year, further options were granted to executive directors and senior executives under the executive share option scheme and to some overseas executives in accordance with the overseas executive share option scheme. Further details concerning options granted under these schemes are set out in note 21 to the accounts.

Charitable donations Donations during the year for charitable purposes, as defined by the Companies Act 1985, amounted to £103,025 (1994 – £75,232).

Auditors On 6 February 1995, our auditors changed the name under which they practice to KPMG and, accordingly, have signed their report in their new name. A resolution to re-appoint KPMG as auditors to the company will be proposed at the annual general meeting.

By order of the Board

J R Tetlow *Secretary*
12 June 1995

J R Tetlow

Corporate governance

The company has complied in the year with the provisions of the Cadbury Committee's code of best practice to the extent that those provisions are fully in place.

The Board meets regularly during the year and is responsible for the overall strategy and direction of the Group and for approving business acquisitions and disposals, management performance, major capital expenditure and significant financing matters. It regularly reviews the financial performance of the company and the Group's business units and has approved formal delegation arrangements for effective management of the Group's business.

It has well established Audit and Remuneration Committees with defined terms of reference. The Audit Committee is made up entirely of non-executive directors and its membership is currently Dr Leach (Chairman), Mrs M C Bolton, Mr E Clark, Mr A G Pendleton and Mr F Sanderson. It reviews the internal and external audit activities, monitors compliance with statutory requirements for financial reporting, and reviews the half year and annual financial statements before they are presented to the Board for approval.

The Remuneration Committee is also made up entirely of non-executive directors, its current membership being Mr Sanderson (Chairman), Mr Clark and Mr Pendleton. The Committee deals with the terms and conditions of employment of executive directors and other senior executives (further information is given in note 5 to the accounts).

The directors are of the opinion that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt a going concern basis in preparing the accounts.

The directors are responsible for the Group's system of internal financial control. They consider that it is appropriately designed to provide reasonable, but not absolute, assurance that assets are safeguarded against misstatement or loss. The key procedures are:

- *control environment*: the culture and values of the Group are communicated through specific policies covering the quality, integrity and ethics of personnel. There are clear responsibilities and accountabilities within a defined organisational structure;
- *identification and evaluation of risks*: the key risk areas are reviewed on a regular basis by executive management and specific committees of the Board. Significant risk areas arising from the development of new activities are subject to consideration by the Board;
- *information and financial reporting systems*: there are comprehensive planning procedures which include detailed operational budgets for the year ahead and projections for subsequent years which are approved by the Board. Key performance indicators are reviewed by the Board monthly to assess progress towards objectives. The Group reports to shareholders half-yearly;
- *investment appraisal*: there are clear policies and procedures for capital expenditure, which include short and long term budgets, detailed appraisal and review procedures and defined levels of authority;
- *control procedures*: there are comprehensive policies and procedures which cover authorisation, segregation of duties, recording of data and physical security; and
- *monitoring systems*: all operating units prepare self-certification questionnaires which confirm compliance with required standards of internal control. The questionnaires are reviewed and substantively verified by both internal and external auditors, as part of their annual statutory audit. The auditors report to the Audit Committee.

The Group's auditors, KPMG, have confirmed that in their opinion, with respect to the directors' statement on going concern above, the directors have provided the disclosures required by paragraph 4.6 of the code of best practice as supplemented by the related guidance for directors, and the statement is not inconsistent with the information of which they are aware from their audit work on the financial statements. The auditors have also confirmed that the directors' statement above appropriately reflects the company's compliance with the other paragraphs of the code in force specified by the Listing Rules for their review. They have carried out their review in accordance with the bulletin issued by the Auditing Practices Board, which does not require them to perform any additional work to express a separate opinion on the effectiveness of the company's system of corporate governance procedures, or on the ability of the company to continue in operational existence.

Directors' responsibilities

in respect of the preparation of financial statements

The following statement, which should be read in conjunction with the statement of auditors' responsibilities included in the report of the auditors on this page, is made with a view to distinguishing for shareholders the respective responsibilities of the directors and of the auditors in relation to the accounts.

The directors are required by the Companies Act 1985 to prepare accounts for each financial year which give a true and fair view of the state of affairs of the company and the Group as at the end of the financial year and of the profit or loss for the financial year.

In preparing the accounts, the directors are required to select appropriate accounting policies, make judgements and estimates that are reasonable and prudent and state whether all accounting standards which they consider to be applicable have been followed. The directors are also required to use a going concern basis in preparing the accounts unless this is inappropriate.

The directors have responsibility for ensuring that the company keeps accounting records which disclose with reasonable accuracy at any time the financial position of the company and which enable them to ensure that the accounts comply with the Companies Act 1985.

The directors have a general responsibility at law for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Auditors' report

to the members of North West Water Group PLC

We have audited the financial statements on pages 39 to 54.

Respective responsibilities of directors and auditors

As described under 'Directors' responsibilities' 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 financial 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 Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations 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 the affairs of the company and of the Group as at 31 March 1995 and of the profit of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG
Chartered Accountants
and Registered Auditors
Manchester
12 June 1995

KPMG

Consolidated profit and loss account

For the year ended 31 March 1995	Note	1995 £m	1994 £m
Turnover	2	**1,011.8**	924.2
Net operating costs	3	**(671.3)**	(600.5)
Operating profit	2	**340.5**	323.7
Share of profits/(losses) of associated undertakings	2,12	**3.9**	(1.9)
Profit before exceptional item, interest and tax		**344.4**	321.8
Exceptional goodwill loss on proposed disposals	22	**(13.5)**	–
Profit on ordinary activities before interest		**330.9**	321.8
Net interest payable	7	**(46.9)**	(52.8)
Profit on ordinary activities before taxation		**284.0**	269.0
Taxation on profit on ordinary activities	8	**(24.8)**	(8.7)
Profit for financial year		**259.2**	260.3
Dividends	9	**(93.9)**	(86.1)
Transfer to reserves	22	**165.3**	174.2
Earnings per share – net basis	10	**69.2p**	70.8p
– nil basis	10	**75.1p**	72.8p
Adjusted earnings per share – net basis	10	**72.8p**	67.1p
– nil basis	10	**78.7p**	72.8p

All of the results derive from continuing operations.

The notes on pages 42 to 54 form part of these accounts.

Balance sheets

At 31 March 1995	Note	Group 1995 £m	Group 1994 £m	Company 1995 £m	Company 1994 £m
Fixed assets					
Tangible assets	11	**3,092.3**	2,854.8	**2.7**	2.1
Investments	12	**10.6**	5.0	**1,216.6**	1,214.3
		3,102.9	2,859.8	**1,219.3**	1,216.4
Current assets					
Stocks	13	**37.5**	38.0	**–**	–
Debtors	14	**224.2**	219.6	**574.6**	175.0
Investments	15	**225.6**	232.3	**9.8**	2.7
Cash at bank and in hand		**16.8**	17.4	**–**	–
		504.1	507.3	**584.4**	177.7
Creditors: amounts falling due within one year	16	**(516.9)**	(467.6)	**(210.6)**	(219.8)
Net current (liabilities)/assets		**(12.8)**	39.7	**373.8**	(42.1)
Total assets less current liabilities		**3,090.1**	2,899.5	**1,593.1**	1,174.3
Creditors: amounts falling due after more than one year	17	**(789.6)**	(787.7)	**(62.6)**	(62.6)
Provisions for liabilities and charges	19	**(54.1)**	(60.7)	**(4.3)**	(3.9)
		2,246.4	2,051.1	**1,526.2**	1,107.8
Capital and reserves					
Called up share capital	21	**377.1**	372.9	**377.1**	372.9
Share premium account	21	**3.0**	0.5	**3.0**	0.5
Profit and loss account	22	**1,866.3**	1,677.7	**1,146.1**	734.4
		2,246.4	2,051.1	**1,526.2**	1,107.8

Approved by the Board of directors on 12 June 1995 and signed on its behalf by

D H Pitcher

Sir Desmond Pitcher *Chairman*

R J Ferguson *Group Finance Director*

The notes on pages 42 to 54 form part of these accounts.

Consolidated cash flow statement

For the year ended 31 March 1995	1995 £m	1995 £m	1994 £m	1994 £m
Net cash inflow from operating activities		421.7		367.4
Returns on investments and servicing of finance				
Interest received	12.5		9.7	
Interest paid	(45.1)		(43.5)	
Interest paid on finance leases	(23.4)		(7.6)	
Dividends paid	(107.1)		(5.2)	
Net cash outflow from returns on investments and servicing of finance		(163.1)		(46.6)
Taxation				
Advance corporation tax paid	(19.5)		(8.2)	
Overseas tax paid	(0.6)		(1.8)	
Taxation paid		(20.1)		(10.0)
Investing activities				
Purchase of fixed asset investments	(8.9)		(5.1)	
Purchase of tangible fixed assets	(322.0)		(344.0)	
Grants and contributions received	18.2		15.1	
Sale of tangible fixed assets	3.4		3.8	
Acquisitions	0.6		(0.3)	
Net cash outflow from investing activities		(308.7)		(330.5)
Net cash outflow before financing		(70.2)		(19.7)
Financing				
Issue of ordinary share capital	5.0		1.1	
Share issue costs	(0.3)		(1.3)	
New loans	–		192.0	
New finance leases	37.5		53.8	
Repayment of loans	(6.6)		(141.0)	
Capital element of finance leases repaid	(7.2)		(10.8)	
Net cash inflow from financing		28.4		93.8
(Decrease)/increase in cash and cash equivalents		(41.8)		74.1

Notes to the cash flow statement

For the year ended 31 March 1995	1995 £m	1994 £m
Reconciliation of operating profit to net cash inflow from operating activities		
Operating profit	340.5	323.7
Depreciation	77.1	67.3
Profit on disposal of tangible fixed assets	(2.5)	(3.7)
Movement in stocks	(2.9)	0.4
debtors	(12.7)	0.3
creditors	22.2	(20.6)
Net cash inflow from operating activities	421.7	367.4
Analysis of changes in cash and cash equivalents		
At 1 April	223.2	148.9
Net cash (outflow)/inflow for the year	(41.8)	74.1
Exchange adjustments	1.3	0.2
At 31 March	182.7	223.2
Analysis of the balances of cash and cash equivalents		
Cash at bank and in hand	16.8	17.4
Bank overdrafts	(1.5)	(2.8)
Temporary borrowings repayable within 3 months	(43.7)	(21.0)
Current asset investments	211.1	229.6
	182.7	223.2

	Share capital (including share premium) £m	Loans and finance lease obligations £m
Analysis of changes in financing during the year		
At 1 April 1994	373.4	783.5
Shares issued in lieu of cash dividends	2.0	–
Cash inflow from financing	4.7	23.7
Exchange adjustments	–	(9.3)
At 31 March 1995	380.1	797.9

Statement of total recognised gains and losses

For the year ended 31 March 1995	Group 1995 £m	Group 1994 £m	Company 1995 £m	Company 1994 £m
Profit for the financial year	**259.2**	260.3	**499.6**	85.5
Exchange adjustments	**4.1**	(1.1)	**(0.3)**	(0.4)
Total recognised gains and losses for the financial year	**263.3**	259.2	**499.3**	85.1

Reconciliation of movements in shareholders' funds

For the year ended 31 March 1995	Note	Group 1995 £m	Group 1994 £m	Company 1995 £m	Company 1994 £m
Profit for the financial year		**259.2**	260.3	**499.6**	85.5
Dividends		**(93.9)**	(86.1)	**(93.9)**	(86.1)
Goodwill loss on proposed disposals	22	**13.5**	–	–	–
Net enhanced scrip dividend adjustment		–	31.3	–	31.3
Net share dividend adjustment		**5.7**	–	**5.7**	–
New share capital issued		**6.7**	14.7	**6.7**	14.7
Goodwill on acquisitions		–	(2.3)	**0.6**	–
Exchange adjustments		**4.1**	(1.1)	**(0.3)**	(0.4)
Net addition to shareholders' funds for the year		**195.3**	216.8	**418.4**	45.0
Opening shareholders' funds		2,051.1	1,834.3	1,107.8	1,062.8
Shareholders' funds at 31 March		**2,246.4**	2,051.1	**1,526.2**	1,107.8

Notes to the accounts

1 Accounting policies

(a) Basis of preparation of accounts

The consolidated accounts set out on pages 39 to 54 incorporate the accounts of North West Water Group PLC and its subsidiary undertakings. The results of businesses acquired during the year are included from the date of acquisition. The accounts have been prepared under the historical cost convention and in accordance with applicable accounting standards and, except for the treatment of certain grants and contributions, with the Companies Act 1985 ('the Act'). An explanation of this departure from the requirements of the Act is given in the 'Grants and contributions' section below.

(b) Turnover

Turnover represents the income receivable in the ordinary course of business for goods or services provided and excludes VAT and foreign sales tax.

(c) Research and development

Expenditure on research and development is written off against profits in the year in which it is incurred.

(d) International development costs

Costs incurred in the development of international activities are either written off or, where appropriate, capitalised and fully provided against until their recovery is considered to be secured by profitable contracts.

(e) Goodwill

The net assets of companies and businesses acquired are incorporated into the consolidated accounts at their fair value to the Group and after adjustments to bring the accounting policies of the companies and businesses acquired into alignment with those of the Group. Past fair value adjustments include provisions for reorganisation and restructuring costs. If the estimates on which these provisions are based prove to be in excess of actual expenditure, the unutilised surplus provisions will not be taken to profit and loss, but will be credited to reserves as a recalculation of goodwill.

(f) Tangible fixed assets

Tangible fixed assets comprise infrastructure assets (mains, sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines and sea outfalls) and other assets (including properties, overground plant and equipment).

(i) Infrastructure assets

Infrastructure assets comprise a network of systems. 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 related 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.

Charges for infrastructure renewals expenditure take account of planned expenditure on maintaining the operating capability of infrastructure assets in accordance with the operational policies and standards underlying the Group's investment programme. The timing of the investment programme and other operational considerations may result in uneven patterns of infrastructure renewals expenditure. Charges to the profit and loss account are adjusted by way of accruals or deferrals, as appropriate, to take account of any significant fluctuations between actual and planned expenditure.

(ii) Other assets

Additions are included at cost.

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

Buildings	30–60 years
Operational structures	10–80 years
Fixtures, fittings, tools and equipment	3–40 years
Pre-1974 assets	22–27 years

Capitalised computer software costs are depreciated over 3–10 years.

Assets in the course of construction with an estimated economic life of greater than 20 years are not depreciated until the year following commissioning.

(g) Grants and contributions

Grants and contributions relating to infrastructure assets have been deducted from the cost of fixed assets. This is not in accordance with schedule 4 to the Act, which requires fixed assets to be shown at their purchase price or production cost and hence grants and contributions would be presented as deferred income. This departure from the requirements of the Act is, in the opinion of the directors, necessary since complying with the Act would not give a true and fair view as no provision is made for depreciation and any grants and contributions relating to such assets would not be taken to the profit and loss account.

Grants receivable in respect of other tangible fixed assets are treated as deferred income, which is credited to the profit and loss account over the estimated economic lives of the related assets.

(h) Leased assets

Assets financed by leasing arrangements which transfer substantially all the risks and rewards of ownership to the lessee (finance leases) are capitalised in the balance sheet and the corresponding capital cost is shown as an obligation to the lessor. Leasing repayments comprise both a capital and a finance element. The finance element is written off to the profit and loss account so as to produce an approximately constant periodic rate of charge on the outstanding obligation. Such assets are depreciated over the shorter of their estimated useful lives and the period of the lease.

Operating lease rentals are charged to the profit and loss account as incurred.

(i) **Fixed asset investments**
Investments held as fixed assets are stated at cost less amounts written off for permanent diminution.

(j) **Current asset investments**
Current asset investments in externally managed interest bearing funds are stated at market value.

Other current asset investments are stated at the lower of cost and net realisable value.

(k) **Stocks**
Stores are stated at cost less any provision necessary to recognise damage and obsolescence.

Long term contract work in progress is stated at cost, net of amounts transferred to cost of sales, after deducting payments received in advance and making provision for foreseeable losses.

Finished goods and goods for resale are stated at the lower of cost and net realisable value and include appropriate production overheads.

(l) **Pensions**
Most of the Group's employees belong to pension schemes which provide for defined benefits based on final pensionable pay. Pension costs are charged against profits over the estimated remaining service lives of employees.

Details of pension arrangements and funding are set out in note 23.

(m) **Foreign currency**
On consolidation, the balance sheets of overseas subsidiary undertakings are translated into sterling at exchange rates applicable at the year end. The profit and loss accounts are translated into sterling using the average rate. Differences arising from the application of the closing rate to opening net assets, offset by translation differences on foreign currency loans which finance investments in overseas subsidiary undertakings, together with differences between profits and losses translated at average rates and at closing rates, are recorded as a movement in reserves.

(n) **Deferred taxation**
Provision is made for deferred taxation where a liability is considered likely to arise in the foreseeable future.

(o) **Associated undertakings**
The appropriate share of the results of associated undertakings are recognised in the consolidated accounts where the directors consider that the Group is in a position to exert significant influence over the associated undertaking.

2 Segmental information

Turnover, profit before exceptional item, interest and tax and net operating assets for each class of business and by geographical origin are:

	Turnover		Profit before exceptional item, interest and tax		Net operating assets	
	1995 £m	1994 £m	1995 £m	1994 £m	1995 £m	1994 £m
By business area:						
Regulated business	**778.6**	729.3	**348.3**	326.1	**2,960.8**	2,704.7
Process businesses	**163.1**	155.9	**7.8**	7.5	**67.4**	68.5
International operations	**7.3**	5.9	**3.0**	0.6	**8.0**	1.8
Other activities	**36.2**	5.9	**(7.5)**	(5.7)	**4.4**	(3.3)
Non-regulated activities	**206.6**	167.7	**3.3**	2.4	**79.8**	67.0
International development costs	**–**	–	**(7.8)**	(8.0)	**(3.7)**	(2.3)
Proposed disposals	**26.6**	27.2	**0.6**	1.3	**(2.2)**	2.7
Group total	**1,011.8**	924.2	**344.4**	321.8	**3,034.7**	2,772.1
By geographical origin:						
United Kingdom	**848.6**	771.6	**339.7**	318.0	**2,978.3**	2,709.5
Europe	**25.2**	23.9	**2.4**	3.3	**5.5**	3.8
The Americas	**117.1**	110.6	**2.6**	(0.9)	**41.2**	48.8
Rest of the world	**20.9**	18.1	**(0.3)**	1.4	**9.7**	10.0
Group total	**1,011.8**	924.2	**344.4**	321.8	**3,034.7**	2,772.1

(i) The segmental analysis by business area has changed in 1995 to exclude from the process business segment the construction companies, Water Engineering Limited and Jones Environmental (Ireland) Limited. These are included as proposed disposals. The 1994 analysis has been re-stated accordingly.

(ii) Profit before exceptional item, interest and tax comprises operating profit amounting to £340.5 million (1994 – £323.7 million) and share of profits of associated undertakings £3.9 million (1994 – loss of £1.9 million).

(iii) Intra-Group sales amounting to £16.8 million (1994 – £13.2 million) have been eliminated in arriving at the segmental analysis of turnover. These sales are primarily within the process businesses and from that business area to the regulated business.

(iv) The geographical destination of turnover does not differ materially from the geographical origin analysis above.

(v) Net operating assets comprise fixed assets and net current assets excluding net borrowings, investments, taxation and dividends.

Notes to the accounts continued

3 Net operating costs

	1995 £m	1994 £m
Employee costs:		
Wages and salaries	165.1	160.6
Social security costs	18.5	18.3
Pension contributions (note 23)	13.7	13.8
	197.3	192.7
Capital schemes	(34.3)	(36.4)
Infrastructure renewals	(6.1)	(9.3)
	156.9	147.0
Depreciation:		
Owned fixed assets	68.5	60.3
Fixed assets held under finance leases	8.6	7.0
	77.1	67.3
Infrastructure renewals expenditure	66.2	62.8
Other operating costs:		
Energy, rates and other operating costs	242.1	195.0
Raw materials and consumables	107.0	107.2
Auditors' remuneration	0.3	0.3
Research and development	8.6	7.8
Operating leases		
–hire of plant and machinery	3.8	4.3
–land and buildings	2.2	2.2
Restructuring charge	11.8	12.0
Other income (note 4)	(4.7)	(5.4)
	371.1	323.4
Total net operating costs	671.3	600.5

Fees payable to KPMG for non-audit services in 1995 were £0.2 million, of which £0.1 million related to the United Kingdom. In 1994, the previous auditors Price Waterhouse received £1.1 million, of which £1.0 million related to the United Kingdom.

4 Other income

	1995 £m	1994 £m
Profit on disposal of fixed assets	2.5	3.7
Net rents receivable	1.8	1.5
Other	0.4	0.2
	4.7	5.4

5 Directors

The Remuneration Committee, made up entirely of non-executive directors, deals with the terms and conditions of employment of executive directors. Its policy is to maintain remuneration arrangements in line with best practice, through a process of regular review. The Committee takes independent specialist advice to assist it in its work.

In formulating its recommendations to the Board on executive remuneration, the Committee takes account of comparative responsibilities and ranking, established through a job evaluation process, and levels of remuneration in the market, which are monitored as a continuing process.

The Committee is involved in the selection process for executive directors and approves the remuneration package before a final offer is made.

Remuneration comprises some or all of the following elements: basic salary, performance related bonus (up to a maximum of 40 per cent dependent on achievement of financial targets), pension (a final salary based scheme), share options (an executive scheme based on a multiple of salary and the employee sharesave scheme), car and health care. Individual performance is recognised through the performance related bonus and share option schemes.

Service contracts: the executive directors have service contracts all of which are, or in the case of J W Beckitt shortly will be, terminable by the company on two years' notice or less.

Performance related bonus scheme: the criteria set by the Committee for the executive directors' performance related bonus scheme are the increase in profit before tax and the return on capital employed.

Executive share option scheme: options under the executive share option scheme have been issued to executive directors up to four times salary. Of these, 75 per cent have been issued at the market value of the underlying shares at the time of grant and the remainder at a discount of up to 15 per cent of the relevant market value, as authorised by shareholders at the 1991 annual general meeting in accordance with changes introduced in the Finance Act 1991. Options are exercisable in a period beginning no earlier than three years (five years for discounted options) and ending no later than ten years from the date of grant.

Pensions: all executive directors are members of and contribute to the Water Pension Scheme (WPS) which provides an entitlement equal to 1/30th of pensionable emoluments for each completed year of service but subject to an overall maximum of 20 years. The normal retirement age is 60, but early retirement is possible from age 50. Under the rules of the WPS all performance related bonuses are pensionable.

5 Directors continued

As a consequence of changes made by the Finance Act 1989, the company is unable to provide pensions from the WPS for its executive directors who have joined the company since 1989 on the same basis as pensions for directors who joined the company before that date. In line with many other companies, the company has established separate arrangements for these executive directors. Accordingly, on the retirement of Sir Desmond Pitcher, B L Staples, D Green and J W Beckitt, the company has undertaken to pay the difference between their pension entitlements based upon the relevant proportion of their final salaries and the maximum amount payable under the rules of the WPS. At the present time, these separate arrangements remain unfunded.

This undertaking will not result in any greater or additional benefits for these directors than would have been payable had it been possible for their pensions to be provided fully within the WPS on the same basis as for directors who had joined the company prior to 1989.

Market rates: the company pays market rates against size of job at all levels. Annual increases are based on independently assessed market rates.

Group development: the range and depth of skills and experience required by the company to transform North West Water into a major international water and wastewater enterprise – to help cultural change, to improve efficiency, to raise capital and cash, to establish new business systems and to build new businesses – has meant that it has been necessary to recruit executive directors and other executives externally in competition with other major PLCs.

The emoluments of the directors are:

	1995 £000	1994 £000
Salaries	**788**	766
Fees	**158**	152
Performance related	**290**	155
Taxable benefits	**37**	49
Pension contributions	**86**	81
	1,359	1,203
The Chairman (and, in both years, the highest paid director):		
Salary	**250**	250
Performance related	**75**	75
Taxable benefits	**12**	13

The contributions to the pension fund in respect of the Chairman amounted to £23,600 (1994 – £22,500).

The non-executive directors do not participate in the performance related bonus scheme, pension or health care arrangements.

Emoluments (excluding pension contributions) of directors of the company were within the following bands:

£	1995 Number	1994 Number
5,001– 10,000	–	2
15,001– 20,000	–	2
20,001– 25,000	3	1
25,001– 30,000	1	1
30,001– 35,000	1	–
35,001– 40,000	1	–
50,001– 55,000	–	1
110,001–115,000	–	1
140,001–145,000	–	1
150,001–155,000	–	1
195,001–200,000	1	–
220,001–225,000	–	1
260,001–265,000	1	–
310,001–315,000	1	–
335,001–340,000	1	1

Notes to the accounts continued

5 Directors continued

At 31 March, the directors and their immediate families had the following interests, all of which were beneficial interests, in the company's ordinary shares and options to subscribe for ordinary shares. The non-executive directors are not eligible to be granted options to purchase fully paid ordinary shares under the employee sharesave scheme or the executive option scheme.

	1995			1994 or on appointment		
		Share options			Share options	
	Ordinary shares	**Executive option scheme**	**Employee sharesave scheme**	Ordinary shares	Executive option scheme	Employee sharesave scheme
Sir Desmond Pitcher	**5,811**	**216,450**	**3,787**	5,469	216,450	3,787
B L Staples	**1,000**	**160,500**	**–**	–	–	–
R J Ferguson	**19,636**	**102,999**	**5,161**	13,240	79,999	8,824
D Green	**1,111**	**169,750**	**4,744**	1,046	165,250	4,744
Mrs M C Bolton	**2,324**	**–**	**–**	2,187	–	–
E Clark	**4,832**	**–**	**–**	4,832	–	–
Dr R Leach	**10,951**	**–**	**–**	10,951	–	–
Sir Peter Middleton	**3,558**	**–**	**–**	–	–	–
A G Pendleton	**5,230**	**–**	**–**	5,230	–	–
F Sanderson	**6,101**	**–**	**–**	4,918	–	–

Further details of directors' options to subscribe for ordinary shares, including details of options granted to and exercised by directors during the year, are as follows:

	Share options as at 31 March 1994	Options granted during the year	Exercise price per share	First date exercisable	Last date exercisable	Options exercised during the year
Employee sharesave scheme						
Sir Desmond Pitcher	3,787	–	455.5p	1 Mar 1999	31 Aug 1999	–
B L Staples	–	–	–	–	–	–
R J Ferguson	6,136	–	176.0p	1 Mar 1995	31 Aug 1995	6,136
	2,688	–	279.0p	1 Feb 1997	31 Jul 1997	–
	–	2,473	418.5p	2 Mar 2000	1 Sept 2000	–
D Green	4,744	–	382.0p	1 Feb 1998	31 Jul 1998	–

	Share options as at 31 March 1994	Options granted during the year	Exercise price per share	First date exercisable	Last date exercisable	Options exercised during the year
Executive option scheme						
Sir Desmond Pitcher	162,338	–	462.0p	5 Jul 1996	5 Jul 2003	–
	54,112	–	393.0p	5 Jul 1998	5 Jul 2003	–
B L Staples	–	120,375	548.0p	19 Aug 1997	19 Aug 2004	–
	–	40,125	466.0p	19 Aug 1999	19 Aug 2004	–
R J Ferguson	2,750	–	315.5p	3 Dec 1993	3 Dec 2000	–
	21,750	–	335.0p	8 Jan 1995	8 Jan 2002	–
	7,250	–	285.0p	8 Jan 1997	8 Jan 2002	–
	17,437	–	479.0p	6 Jan 1996	6 Jan 2003	–
	5,812	–	407.5p	6 Jan 1998	6 Jan 2003	–
	18,750	–	586.0p	20 Jan 1997	20 Jan 2004	–
	6,250	–	498.5p	20 Jan 1999	20 Jan 2004	–
	–	17,250	496.0p	15 Dec 1997	15 Dec 2004	–
	–	5,750	422.0p	15 Dec 1999	15 Dec 2004	–
D Green	110,813	–	406.0p	18 Jun 1995	18 Jun 2002	–
	36,937	–	345.5p	18 Jun 1997	18 Jun 2002	–
	13,125	–	586.0p	20 Jan 1997	20 Jan 2004	–
	4,375	–	498.5p	20 Jan 1999	20 Jan 2004	–
	–	3,375	496.0p	15 Dec 1997	15 Dec 2004	–
	–	1,125	422.0p	15 Dec 1999	15 Dec 2004	–

The mid market price of a share at 31 March 1995 was 549.0p and at the date of exercise of options by R J Ferguson was 522.0p. The range during the year was 457.0p (low) to 602.0p (high).

J W Beckitt was appointed a director with effect from 25 April 1995 when he had options on 109,749 shares granted during the year under the terms of the executive option scheme (82,312 at an option price of 496.0p exercisable from 15 December 1997 to 15 December 2004 and 27,437 at an option price of 422.0p exercisable from 15 December 1999 to 15 December 2004).

Under the terms and conditions of the employee sharesave scheme, for every month (up to no more than six months) savings are behind, the last date exercisable will be delayed by one month.

No director had any interest in any share capital of any other Group company or in any debenture of any Group company.

6 Employees

	1995	1994
Average number of persons employed by the Group	**7,871**	8,013
By business area:		
Regulated business	**5,342**	5,426
Process businesses	**2,071**	2,132
International operations	**150**	102
Other activities	**167**	208
Proposed disposals	**141**	145
Non-regulated activities	**2,529**	2,587
Group total	**7,871**	8,013

The segmental analysis by business area has changed in 1995 to exclude from the process business segment the construction companies, Water Engineering Limited and Jones Environmental (Ireland) Limited. These are included as proposed disposals. The 1994 analysis has been re-stated accordingly.

7 Net interest payable

	1995 £m	1994 £m
Interest payable:		
On bank loans, overdrafts and other loans:		
Repayable within 5 years	**7.2**	5.4
Repayable wholly or partly in more than 5 years	**31.4**	40.3
	38.6	45.7
On finance leases	**22.6**	16.7
Total interest payable	**61.2**	62.4
Interest receivable	**(14.3)**	(9.6)
Net interest payable	**46.9**	52.8

8 Taxation

	1995 £m	1994 £m
UK corporation tax at 33%	**–**	–
Overseas tax	**2.6**	1.4
Unrelieved advance corporation tax	**22.2**	20.7
	24.8	22.1
Reduction in prior year advance corporation tax arising from the enhanced scrip dividend	**–**	(13.4)
	24.8	8.7

No UK tax liability or charge arises because of the tax allowances on the transfer of accumulated capital expenditure from the predecessor Authority and on expenditure incurred subsequently.

The exceptional goodwill loss on proposed disposals has no impact on the tax liability or charge.

The full potential deferred tax liability is:

Accelerated tax allowances on buildings, plant and equipment		
Infrastructure assets	**345.0**	290.0
Other assets	**146.0**	102.4
Losses and other timing differences	**(100.3)**	(104.3)
	390.7	288.1
Advance corporation tax recoverable	**(107.1)**	(86.5)
	283.6	201.6

No deferred tax asset or liability arises in the company's accounts.

No provision is made for taxation in respect of liabilities which might arise on the distribution of earnings retained overseas.

Notes to the accounts continued

9 Dividends

	1995 £m	1994 £m
Interim dividend of 8.35 pence (1994 – 7.67 pence)	**28.9**	28.6
Final dividend of 17.20 pence recommended (1994 – 15.40 pence)	**65.0**	57.5
	93.9	86.1

Provision is made for proposed final dividends and the related advance corporation tax payable on the basis that the dividends will be fully settled in cash. The adjustments required to reflect the take-up of dividends in the form of new shares are accounted for in the subsequent financial year.

10 Earnings per share

	1995	1994
Net basis:		
Profit for financial year attributable to ordinary shareholders	**£259.2m**	£260.3m
Earnings per ordinary share	**69.2p**	70.8p
	£m	£m
Adjusted earnings per share:		
Profit for financial year attributable to ordinary shareholders	**259.2**	260.3
Adjustments:		
Exceptional goodwill loss on proposed disposals	**13.5**	–
Advance corporation tax credit on the scrip dividend alternative to cash in respect of the 1993 final dividend	–	(13.4)
Adjusted profit for financial year attributable to ordinary shareholders	**272.7**	246.9
Adjusted earnings per ordinary share	**72.8p**	67.1p

	1995	1994
Nil basis:		
Profit on ordinary activities after the elimination of the charge for unrelieved advance corporation tax	**£281.4m**	£267.6m
Earnings per ordinary share	**75.1p**	72.8p
	£m	£m
Adjusted earnings per share:		
Profit on ordinary activities after the elimination of the charge for unrelieved advance corporation tax	**281.4**	267.6
Adjustment:		
Exceptional goodwill loss on proposed disposals	**13.5**	–
Adjusted profit on ordinary activities after the elimination of the charge for unrelieved advance corporation tax	**294.9**	267.6
Adjusted earnings per ordinary share	**78.7p**	72.8p

The adjustment to profit and earnings per share has been made to eliminate the impact of non-recurring items.

Earnings per ordinary share and the adjusted earnings per ordinary share on the net basis have been calculated by dividing profit and the adjusted profit for the financial year attributable to ordinary shareholders by 374.7 million, being the weighted average number of shares in issue during the year (1994 – 367.7 million).

Earnings per ordinary share and the adjusted earnings per ordinary share on the nil basis are calculated by eliminating the taxation charge of £22.2 million (1994 – £7.3 million) in respect of unrelieved advance corporation tax.

There would be no significant dilution of earnings per ordinary share if the outstanding share options were exercised.

11 Tangible fixed assets

Group	Land and buildings £m	Infra-structure assets £m	Opera-tional structures £m	Fixtures, fittings, tools and equipment £m	Pre-1974 assets £m	Assets in course of con-struction £m	Total £m
Cost:							
At 1 April 1994	127.8	1,243.9	990.0	324.4	177.4	375.3	3,238.8
Additions	3.5	69.2	32.8	18.3	–	203.3	327.1
Grants and contributions	–	(6.6)	–	–	–	(0.3)	(6.9)
Transfers	12.0	48.5	104.8	22.8	–	(188.1)	–
Transfers to other current assets	(4.1)	–	–	–	–	–	(4.1)
Disposals	(0.6)	–	(0.7)	(2.3)	–	–	(3.6)
Exchange adjustments	(0.1)	–	–	(0.2)	–	(0.1)	(0.4)
At 31 March 1995	**138.5**	**1,355.0**	**1,126.9**	**363.0**	**177.4**	**390.1**	**3,550.9**
Depreciation:							
At 1 April 1994	17.0	–	134.0	121.9	111.1	–	384.0
Charge for the year	5.2	–	29.4	37.0	5.5	–	77.1
Disposals	(0.4)	–	(0.6)	(1.7)	–	–	(2.7)
Exchange adjustments	0.1	–	–	0.1	–	–	0.2
At 31 March 1995	**21.9**	–	**162.8**	**157.3**	**116.6**	–	**458.6**
Net book value:							
At 31 March 1995	**116.6**	**1,355.0**	**964.1**	**205.7**	**60.8**	**390.1**	**3,092.3**
At 31 March 1994	110.8	1,243.9	856.0	202.5	66.3	375.3	2,854.8

Grants and contributions received relating to infrastructure assets have been deducted from the cost of fixed assets in order to show a true and fair view. As a consequence, the net book value of fixed assets is £66.6 million (1994 – £59.7 million) lower than it would have been had this treatment not been adopted.

Within tangible fixed assets are assets held under finance leases at the following amounts:

	1995 £m	1994 £m
Cost:		
Operational structures	**250.8**	213.4
Fixtures, fittings, tools and equipment	**26.8**	28.0
At 31 March	**277.6**	241.4
Accumulated depreciation:		
Operational structures	**40.5**	34.5
Fixtures, fittings, tools and equipment	**15.8**	14.8
At 31 March	**56.3**	49.3
Net book value:		
Operational structures	**210.3**	178.9
Fixtures, fittings, tools and equipment	**11.0**	13.2
At 31 March	**221.3**	192.1

An analysis of land and buildings between freehold and long and short leasehold is not readily available at 31 March 1995. Pre-1974 assets comprise a pool of assets which was transferred to the Group from North West Water Authority, which it acquired in 1974 from its predecessors. No analysis by asset category is available. The directors consider that the provision of the above information would incur expense out of proportion to the benefit it would provide to shareholders.

	1995 £m	1994 £m
Capital commitments:		
Contracted but not provided for	**268.7**	536.1
Authorised but not yet contracted for	**103.4**	69.0

Company	Fixtures, fittings, tools and equipment £m
Cost:	
At 1 April 1994	2.4
Additions	1.0
At 31 March 1995	**3.4**
Depreciation:	
At 1 April 1994	0.3
Charge for the year	0.4
At 31 March 1995	**0.7**
Net book value:	
At 31 March 1995	**2.7**
At 31 March 1994	2.1

Notes to the accounts continued

12 Fixed asset investments

Group	Investments in associated undertakings £m	Other investments £m	Total £m
Cost:			
At 1 April 1994	3.7	1.3	5.0
Additions	3.5	0.3	3.8
Share of profits	3.6	–	3.6
Exchange adjustments	(1.7)	(0.1)	(1.8)
At 31 March 1995	**9.1**	**1.5**	**10.6**

The investments in associated undertakings represent the Group's share of net assets and relate principally to international operations. Share of profits is stated after a taxation charge of £0.3 million.

Company	Shares in subsidiary undertakings £m	Other investments £m	Total £m
Cost:			
At 1 April 1994	1,214.0	0.3	1,214.3
Additions	2.2	0.1	2.3
At 31 March 1995	**1,216.2**	**0.4**	**1,216.6**

Details of principal operating subsidiary and associated undertakings, all of which are unlisted, are detailed below. These subsidiary undertakings are included within the consolidated Group accounts. A full list of subsidiaries is attached to the annual return of the company.

	Class of share capital held	Proportion of share capital owned/voting rights	Nature of business
Subsidiary undertakings:			
Great Britain:			
North West Water Limited	Ordinary	100%	Water supply and sewerage services
North West Water International Limited	Ordinary	100%	Consulting services and project management
Water Engineering Limited	Ordinary	100%*	Design and installation of water and wastewater treatment plants
Wallace & Tiernan Limited	Ordinary	100%*	Manufacture of equipment for water and wastewater treatment processes
Edwards and Jones Limited	Ordinary	100%*	
Republic of Ireland:			
Jones Environmental (Ireland) Limited	Ordinary	100%*	Design and installation of water and wastewater treatment plants
USA:			
Envirex Inc	Ordinary	100%*	
General Filter Company Inc	Ordinary	100%*	Manufacture of equipment for water and wastewater treatment processes
Wallace & Tiernan Inc	Ordinary	100%*	
Consolidated Electric Company	Ordinary	100%*	
US Water Inc	Ordinary	100%*	Contract operations and maintenance services
Mexico:			
Wallace & Tiernan de Mexico SA de CV	Ordinary	100%*	Manufacture of equipment for water and wastewater treatment processes
Australia:			
North West Water Australia Pty Limited	Ordinary	100%*	Technical and management services
Wallace & Tiernan Pacific Pty Limited	Ordinary	100%*	Manufacture of equipment for water and wastewater treatment processes

12 Fixed asset investments continued

	Class of share capital held	Proportion of share capital owned/voting rights	Nature of business
Canada:			
Asdor Limited	Ordinary	100%*	Suppliers of equipment for water and wastewater treatment processes
Wallace & Tiernan Canada Inc	Ordinary	100%*	
Germany:			
Wallace & Tiernan GmbH	Ordinary	100%*	Manufacture of equipment for water and wastewater treatment processes
Malaysia:			
North West Water (Malaysia) SDN BHD	Ordinary	100%	Technical and management services
Associated undertakings:			
Great Britain:			
WRc (Process Engineering) Limited	Ordinary	50%*	Design and construction of equipment for water and wastewater treatment processes
Australia:			
Yan Yean Water Pty Limited	Ordinary	50%*	Water treatment operations
NWT Water Pty Limited	Ordinary	50%*	
Malaysia:			
Indah Water Operations SDN BHD	Ordinary	50%*	Wastewater network and treatment operations
Mexico:			
Agua de Mexico SA de CV	Ordinary	49%*	Technical and management services
Spain:			
CIDA Hidroquimica SA	Ordinary	39.7%*	Design and installation of equipment and systems for water and wastewater treatment

The country under which each undertaking appears is both the country of its incorporation and of its principal operations. All of the Great Britain undertakings are registered in England and Wales. Shares are held directly by North West Water Group PLC except where marked with an asterisk where they are held by subsidiary undertakings.

13 Stocks

	Group 1995 £m	Group 1994 £m
Stores	**8.9**	10.1
Work in progress	**13.7**	8.1
Finished goods and goods for resale	**14.9**	19.8
	37.5	38.0

14 Debtors

	Group 1995 £m	Group 1994 £m	Company 1995 £m	Company 1994 £m
Amounts falling due within one year:				
Trade debtors	**132.5**	139.1	**–**	–
Amounts owed by subsidiary undertakings	**–**	–	**572.8**	174.1
Other debtors	**15.3**	13.5	**–**	–
Prepayments and accrued income	**64.6**	53.0	**1.8**	0.9
Infrastructure renewals prepayment	**–**	3.4	**–**	–
Amounts recoverable under contracts	**5.3**	2.0	**–**	–
Deferred tax	**–**	0.2	**–**	–
	217.7	211.2	**574.6**	175.0
Amounts falling due after more than one year:				
Amounts owed by associated undertaking	**3.2**	–	**–**	–
Other debtors	**3.3**	8.4	**–**	–
	6.5	8.4	**–**	–
Total debtors	**224.2**	219.6	**574.6**	175.0

Notes to the accounts continued

15 Current asset investments

	Group 1995 £m	Group 1994 £m	Company 1995 £m	Company 1994 £m
Managed funds and short term deposits	**211.1**	229.6	–	–
Other current asset investments	**14.5**	2.7	**9.8**	2.7
	225.6	232.3	**9.8**	2.7

16 Creditors: amounts falling due within one year

	Group 1995 £m	Group 1994 £m	Company 1995 £m	Company 1994 £m
Loans	**31.8**	0.9	–	–
Bank overdrafts and temporary borrowings	**58.2**	43.9	–	–
Trade creditors	**42.8**	45.8	–	–
Amounts owed to subsidiary undertakings	–	–	**112.8**	104.0
Obligations under finance leases	**8.1**	7.2	–	–
Dividends	**65.4**	86.1	**65.4**	86.1
Other creditors	**1.8**	3.0	–	–
Taxation and social security	**6.5**	6.0	–	–
Infrastructure renewals accrual	**15.8**	–	–	–
Accruals and deferred income	**263.1**	254.0	**9.0**	9.0
Advance corporation tax	**23.4**	20.7	**23.4**	20.7
	516.9	467.6	**210.6**	219.8

17 Creditors: amounts falling due after more than one year

	Group 1995 £m	Group 1994 £m	Company 1995 £m	Company 1994 £m
Loans	**525.1**	564.8	**62.6**	62.6
Obligations under finance leases	**219.9**	190.5	–	–
Other creditors	**11.4**	9.6	–	–
Deferred grants and contributions (note 18)	**33.2**	22.8	–	–
	789.6	787.7	**62.6**	62.6

18 Deferred grants and contributions

Group	£m
At 1 April 1994	22.8
Received in the year	11.3
Credit to profit and loss account for the year	(0.9)
At 31 March 1995	**33.2**

19 Provisions for liabilities and charges

	Group Restructuring £m	Group Other £m	Group Total £m	Company Other £m
At 1 April 1994	47.7	13.0	60.7	3.9
Utilised	(21.3)	(1.4)	(22.7)	–
Profit and loss account	11.8	4.3	16.1	0.4
At 31 March 1995	**38.2**	**15.9**	**54.1**	**4.3**

20 Borrowings

	Loans and overdrafts					
Group	Repayable by instalments partly after 5 years £m	Wholly repayable after more than 5 years £m	Wholly repayable within 5 years £m	Finance leases £m	1995 Total £m	1994 Total £m
Within one year	7.3	–	82.7	8.1	**98.1**	52.0
Between one and two years	16.5	–	–	9.1	**25.6**	42.4
Between two and five years	76.3	–	70.0	10.7	**157.0**	81.3
After more than five years	241.4	120.9	–	200.1	**562.4**	631.6
	341.5	120.9	152.7	228.0	**843.1**	807.3

Loans repayable by instalments partly after five years and loans wholly repayable after more than 5 years comprise bank and other loans repayable between 2000 and 2052. Interest rates range from 6.65 per cent to 14.83 per cent on £259.8 million and are at floating rates on £202.6 million.

Company

The company has loans totalling £174.5 million (1994 – £154.8 million) of which £111.9 million is owed to Group undertakings and falls due within one year. The remaining loans are wholly repayable in 2001. Interest rates are 11.625 per cent on £20.0 million and at floating rates on £42.6 million.

21 Called up share capital and share premium accounts

The authorised share capital of the company throughout the year ended 31 March 1995 was £475,000,001 divided into 475,000,000 ordinary shares of £1 each and one special rights redeemable preference share of £1.

The allotted and fully paid share capital of the company at 31 March was:

	1995 £	1994 £
Ordinary shares of £1	**377,092,424**	372,896,476
Special rights redeemable preference share of £1	–	1
	377,092,424	372,896,477

The movements on the allotted and fully paid share capital and the share premium accounts were:

	Share capital		Share premium
	Shares million	£m	£m
At 1 April 1994	372.9	372.9	0.5
Issued under share option and sharesave schemes	2.2	2.2	2.8
Issued in lieu of cash dividends	2.0	2.0	–
Share issue costs	–	–	(0.3)
At 31 March 1995	**377.1**	**377.1**	**3.0**

2,197,843 ordinary shares were allotted during the year ended 31 March 1995 following the exercise of options in accordance with the rules of the employee sharesave scheme and the executive share option scheme for a total consideration of £5.0 million.

On 6 April 1994 444,627 ordinary shares, on 3 October 1994 1,080,998 ordinary shares and on 24 February 1995 472,480 ordinary shares were issued to ordinary shareholders who elected to receive shares in lieu of cash for the 1994 interim dividend, the 1994 final dividend and the 1995 interim dividend respectively.

The special rights redeemable preference share issued to HM Government was redeemed by the company on 31 December 1994.

The company has two share option schemes – an employee sharesave scheme available to all eligible employees and an executive share option scheme for executive directors and senior executives. The former is based on SAYE contracts with options exercisable within a six month period from the conclusion of a five or seven year period as appropriate from the date of grant. Options under the latter scheme are exercisable in a period beginning no earlier than three years (five years for discounted options) and ending no later than ten years from the date of grant. Options outstanding under the two share option schemes at 31 March, together with their exercise prices and dates were:

	1995	1994	Option price	Normal dates of exercise
Employee sharesave	**955,973**	2,534,610	176.0p	1995 or 1997
	1,066,356	1,128,421	252.5p	1996 or 1998
	1,470,953	1,542,000	279.0p	1997 or 1999
	884,642	949,642	382.0p	1998 or 2000
	811,684	914,075	455.5p	1999 or 2001
	1,304,948	–	418.5p	2000 or 2002
Executive share option	**66,000**	66,000	278.0p	1993 to 2000
	36,800	36,800	286.5p	1993 to 2000
	96,900	159,150	315.5p	1993 to 2000
	54,500	54,500	330.0p	1994 to 2001
	579,732	1,149,462	335.0p	1995 to 2002
	358,528	370,963	285.0p	1997 to 2002
	296,245	296,245	406.0p	1995 to 2002
	98,744	98,744	345.5p	1997 to 2002
	503,938	512,937	479.0p	1996 to 2003
	167,963	170,962	407.5p	1998 to 2003
	347,577	347,577	462.0p	1996 to 2003
	115,851	115,851	393.0p	1998 to 2003
	825,543	830,418	586.0p	1997 to 2004
	273,916	276,416	498.5p	1999 to 2004
	305,241	–	548.0p	1997 to 2004
	101,741	–	466.0p	1999 to 2004
	561,199	–	496.0p	1997 to 2004
	186,999	–	422.0p	1999 to 2004
	11,471,973	11,554,773		

In the year ended 31 March 1995, options were granted under the two option schemes in respect of 2,464,300 ordinary shares, options for 2,197,843 shares were exercised and options for 349,257 shares lapsed.

Notes to the accounts continued

22 Profit and loss account

	Group £m	Company £m
At 1 April 1995	1,677.7	734.4
Profit for the year	165.3	405.7
Goodwill loss on proposed disposals	13.5	–
Adjustment to goodwill on acquisitions	–	0.6
Shares issued in lieu of cash dividends	5.7	5.7
Exchange adjustments	4.1	(0.3)
At 31 March 1995	**1,866.3**	**1,146.1**

The goodwill written back through the profit and loss account in the year of £13.5 million relates to the proposed disposals of Water Engineering Limited, Jones Environmental (Ireland) Limited and the membrane manufacturing activities.

Cumulative goodwill arising on the acquisition of subsidiary undertakings written off to the profit and loss account amounts to £134.0 million (1994 – £148.1 million). The company's adjustment to goodwill on acquisitions of £0.6 million represents the partial refund of purchase consideration relating to the Acumem membrane business.

As allowed by section 230 of the Companies Act 1985, the company has not presented its own profit and loss account. The amount of Group profit for the financial year dealt with in the company's profit and loss account was £499.6 million, after accounting for dividends receivable from subsidiary undertakings of £518.8 million.

23 Pensions

The Group operates a number of pension schemes in the UK, the USA, Europe, Australia and Canada. The major schemes are of the defined benefit type in the UK – the Water Mirror Image Pension Scheme (WMIS) and the Water Pension Scheme (WPS). The assets of these schemes are held in trust funds independent of Group finances.

For the major UK schemes, the employer's contributions and the pensions cost under the accounting standard SSAP24 have been assessed in accordance with the advice of William M Mercer Limited, using the projected unit method for the WPS and the attained age method for the WMIS. For this purpose, the main actuarial assumptions adopted are based upon investment growth of 9 per cent per annum, pay growth of 7 per cent per annum and increases to pensions in payment and deferred pensions of 5 per cent per annum.

The last actuarial valuation of the two schemes was carried out as at 31 March 1993. The total market value of the assets at the valuation date was £316.4 million. The combined actuarial value of the assets represented 98 per cent of the value of the accrued benefits after allowing for expected future earnings increases. In deriving the pension cost under SSAP24, the deficiency in the schemes is being spread over the future working lifetime of the existing members.

For the overseas schemes, the defined benefit arrangements have been reviewed on consistent assumptions and any balance of surplus spread forward to derive the pension cost.

The total pension cost for the period was £13.7 million (1994 – £13.8 million).

The Group has two overseas subsidiary undertakings which offer post retirement medical and life insurance benefits. The benefits payable under these schemes have now been capped and are no longer offered to new employees. The liability in respect of all future benefit obligations of £1.8 million has been actuarially determined and was fully provided for on acquisition of the subsidiary undertakings.

Information about the pension arrangements for executive directors is contained in note 5.

24 Operating leases

Subsidiary undertakings are committed to making the following payments during the year ending 31 March 1996:

	Land and buildings £m	Plant and machinery £m
Leases which expire:		
Within one year	1.6	0.7
Between two and five years	1.1	3.0
After five years	1.0	–
	3.7	3.7

25 Contingent liabilities

The company and certain of its subsidiary undertakings have, in the ordinary course of business, entered into performance bonds relating to the Group's own contracts.

The company also guaranteed certain loans and overdrafts of Group undertakings up to a maximum amount of £567.3 million, including £370.0 million relating to North West Water Limited's loans from the European Investment Bank.

In accordance with Irish companies legislation, the company has guaranteed the liabilities (as defined in section 5(c)(ii) of the Companies (Amendment) Act, 1986) of Jones Environmental Limited and Jones Environmental (Ireland) Limited availing of the exemption under section 17(i)(c) of that Act. The amount covered by the guarantees at the year end was £2.8 million.

Five year summary

	1991 £m	1992 £m	1993 £m	1994 £m	1995 £m
Profit and loss accounts					
Turnover	599	789	878	924	**1,012**
Net operating costs	(412)	(543)	(590)	(600)	**(671)**
Operating profit	187	246	288	324	**341**
Share of (losses)/profits of associated undertakings	–	–	–	(2)	**4**
Exceptional goodwill loss on proposed disposals	–	–	–	–	**(14)**
Net interest receivable/(payable)	28	(16)	(41)	(53)	**(47)**
Profit before tax	215	230	247	269	**284**
Tax on profit on ordinary activities	(22)	(24)	(25)	(9)	**(25)**
Profit for financial year	193	206	222	260	**259**
Dividends	(64)	(70)	(76)	(86)	**(94)**
Transfer to reserves	129	136	146	174	**165**
Balance sheets					
Fixed assets	1,834	2,221	2,564	2,860	**3,103**
Net current assets/(liabilities)	124	39	18	40	**(13)**
Creditors falling due after more than one year	(263)	(499)	(674)	(788)	**(790)**
Provisions for liabilities and charges	(47)	(63)	(74)	(61)	**(54)**
	1,648	1,698	1,834	2,051	**2,246**
Ordinary share capital and share premium	356	356	358	373	**380**
Reserves and retained profits	1,292	1,342	1,476	1,678	**1,866**
	1,648	1,698	1,834	2,051	**2,246**

Shareholder information

Financial calendar The 1995 annual general meeting will be held on 28 July 1995 at 10.30 am at the Holiday Inn Crowne Plaza (the Midland Hotel), Manchester. The notice of meeting is enclosed with this report.

Other forthcoming key events are:

- payment of the 1994/95 final dividend and the 1995/96 special dividend, on 3 October 1995;
- announcement of the half-year results, in November 1995;
- payment of the 1995/96 interim dividend, in February 1996;
- preliminary announcement of the full-year results, in May 1996;
- publication of the annual report and accounts, in June 1996; and
- the annual general meeting, in July 1996.

Information about shareholdings If you wish to enquire about or need any information about your shareholding in the company, please contact the company's registrar, Lloyds Bank Registrars, 54 Pershore Road South, Kings Norton, Birmingham B30 3EP (telephone: 0121 433 8000).

Personal equity plans (PEPs) Details of the North West Water single company and general PEPs are available from the Plan Manager, Halifax Investment Services Limited (a member of IMRO), Halifax Building Society, Trinity Road, Halifax HX1 2RG (telephone: 01422 335991).

Publications In addition to this annual report describing the Group's activities overall, we produce other reports, leaflets and factsheets which describe particular areas of activity or aspects of our business in greater detail.

These are outlined in our comprehensive information resources catalogue, 'Take a closer look'. If you would like a copy of 'Take a closer look' or other publications, please contact the company's Corporate Communications Director at Dawson House, Great Sankey, Warrington WA5 3LW (telephone: 01925 234000).

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North West Water

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