

WESSEX WATER SERVICES LTD

Accounts for the year to
31 December 1999

Registered in England and Wales No. 2366648



DIRECTORS' REPORT

The directors present their report and the audited accounts for the year to 31 December 1999.

PRINCIPAL ACTIVITIES

The main activities of the company are the supply of water and the treatment and disposal of waste water.

PROFIT AND DIVIDEND

The profit for the period after taxation was £104.2m. Dividends of £31.7m were paid during the year. The directors propose a final dividend of £37.8m.

OPERATIONAL REVIEW

The company has continued to provide an excellent service and high quality standards for customers. The last year has been important for the company as it prepared for the review of customer charges to be effective from 1 April 2000, and ensured that it had no problems with the millennium date change.

The Director General of Water Services announced on 25 November 1999 a 12.0% price cut for Wessex Water Services Ltd from 1 April 2000, before adjustment for inflation. The announcement also included level prices for the years commencing 1 April 2001 and 1 April 2002, with price increases of 3.8% and 4.7% for the years commencing 1 April 2003 and 2004 respectively.

EMPLOYMENT

Wessex Water Services Ltd offers equal opportunities to all applicants for employment. Disabled people are considered for employment, training, career development and promotion on the basis of their aptitude and abilities, in common with all employees.

A high priority is given to employee communications which include team meetings, an employee newspaper, newsletters and conferences.

ENVIRONMENT POLICY

Wessex Water Services Ltd protects, conserves and improves the environment and operates in a socially responsible manner. Working practices are continually revised as improved techniques and technologies become available. The company has an environmental advisory panel and an environmental and sustainability charter. A separate sustainability report is prepared indicating the progress made in this area during the year.

RESEARCH AND DEVELOPMENT

The company carried out research and development in support of existing activities to improve the reliability and effectiveness of water and waste water services.

CHARITABLE DONATIONS

During the year £128,000 was donated to UK charities (9 months to 31.12.98 - £84,000).

SUPPLIER PAYMENT POLICY

The company's policy in respect of its suppliers is to agree the payment terms for transactions in advance and to make payments in accordance with those terms. At 31 December 1999 trade creditors represented approximately 37 days trade purchases (31.12.98 - 46 days).

YEAR 2000

The company undertook a major project between 1996 and December 1999 to ensure that it had no problems with the year 2000 "Millennium Bug" in respect of computer systems, equipment and telemetry. In total £13.6m was spent on capital projects and £2.6m was charged to the profit and loss account. No such problems have arisen.

DIRECTORS

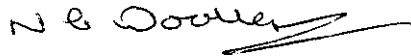
The following were directors of the company during the year to 31 December 1999:

C F Skellett - Chairman	
S M Allen	
L H Ames	Resigned 1 April 1999
P A Barrett	Resigned 22 October 1999
Mrs L C Bennett	
C J Bishop	
P J Costain	Appointed 1 December 1999
T K Harris	Appointed 20 April 1999
R N Hodge	
W N Hood	Resigned 29 October 1999
J G Jones	
Mrs K Morgan	
P L M Sherwood	
N A W Wheatley	Resigned 20 April 1999

There are no interests in shares of group companies that are disclosable in these accounts.

AUDITORS

A resolution to reappoint Arthur Andersen as auditors of the company will be proposed at the Annual General Meeting.



By order of the board
N G Wooller
Company secretary
14 April 2000

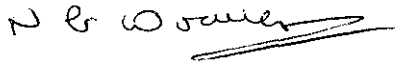
DIRECTORS' RESPONSIBILITIES

Company law requires the directors to prepare accounts for each financial year which give a true and fair view of the state of affairs of the company and of the company's profit or loss for the year. In preparing those accounts, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts; and
- prepare the accounts on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the accounts comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

By order of the board
N G Wooller
Company secretary
14 April 2000



AUDITORS' REPORT TO THE MEMBERS OF WESSEX WATER SERVICES LTD

We have audited the accounts on pages 4 to 14, which have been prepared under the historical cost convention, and the accounting policies set out on pages 6 and 7.

Respective responsibilities of directors and auditors

As described above, the company's directors are responsible for the preparation of the accounts in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board and by our profession's ethical guide.

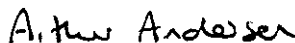
Basis of opinion

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 accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts 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 accounts.

Opinion

In our opinion the accounts give a true and fair view of the state of affairs of the company at 31 December 1999 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.



ARTHUR ANDERSEN
Chartered Accountants and Registered Auditors
1 Surrey Street
London
WC2R 2PS
14 April 2000

PROFIT AND LOSS ACCOUNT
For the year to 31 December 1999

	NOTE	12 months to 31.12.99 £m	9 months to 31.12.98 £m
Turnover	2	278.8	202.2
Operating profit	2, 3	152.9	112.5
Net interest payable	4	(28.5)	(21.9)
Profit on ordinary activities before taxation		124.4	90.6
Taxation on profit on ordinary activities	5	(20.2)	(17.1)
Profit attributable to shareholders		104.2	73.5
Dividends paid and proposed	7	(69.5)	(49.0)
Transfer to reserves	17	34.7	24.5

The company's turnover and operating profit were generated from continuing activities.

There were no recognised gains or losses in either period other than the profit for each period.

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

BALANCE SHEET
31 December 1999


	NOTE	31.12.99 £m	Restated 31.12.98 £m
Fixed assets			
Tangible assets	8	1,259.5	1,160.2
Investments	9	-	-
		<u>1,259.5</u>	<u>1,160.2</u>
Current assets			
Stock and work in progress	10	1.1	1.1
Debtors	11	62.3	63.6
		<u>63.4</u>	<u>64.7</u>
Creditors - amounts falling due within one year	12	(220.7)	(537.2)
		<u>(220.7)</u>	<u>(537.2)</u>
Net current liabilities	24	(157.3)	(472.5)
		<u>(157.3)</u>	<u>(472.5)</u>
Total assets less current liabilities		1,102.2	687.7
Creditors - amounts falling due after more than one year	13	(472.2)	(93.8)
Provisions for liabilities and charges	14	(10.2)	(8.6)
Deferred income	15	(22.3)	(22.5)
		<u>(22.3)</u>	<u>(22.5)</u>
Net assets	2	597.5	562.8
		<u>597.5</u>	<u>562.8</u>
Capital and reserves			
Called up equity share capital	16	81.3	81.3
Profit and loss account	17	516.2	481.5
		<u>516.2</u>	<u>481.5</u>
Equity shareholders' funds	17	597.5	562.8
		<u>597.5</u>	<u>562.8</u>

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

These accounts were approved by the board of directors on 14 April 2000 and signed on its behalf by:



C F Skellett
Chairman



T K Harris
Director

NOTES TO THE ACCOUNTS
For the year to 31 December 1999

1 Accounting policies

a. Basis of preparation

The accounts have been prepared under the historic cost convention and in accordance with applicable accounting standards in the United Kingdom and, except for the treatment of certain grants and contributions (see note 1e) in accordance with the Companies Act 1985. The company has adopted all applicable accounting standards up to and including FRS14 "Earnings per Share". The adoption of FRS12 "Provisions, Contingent Liabilities and Contingent Assets" has given rise to a prior year adjustment as set out in note 1c below.

Group accounts have not been prepared as under section 228 of the Companies Act 1985 the company and its subsidiary are included in the consolidated financial statements of Wessex Water Ltd (see note 23).

b. Turnover

Turnover represents income receivable in the ordinary course of business, excluding VAT, for services provided inclusive of transactions with Wessex Water Ltd and its other subsidiaries.

c. Tangible fixed assets and depreciation

Tangible fixed assets comprise infrastructure assets and other assets.

- i Infrastructure assets comprise a network of systems of mains and sewers, impounding and pumped raw water storage reservoirs, dams, sludge pipelines, sea outfalls and infrastructure investigations and studies. Expenditure on infrastructure assets relating to enhancements of the network is treated as additions which are included at cost after deducting connection charges and grants.

It has been necessary to change the method of accounting for infrastructure maintenance expenditure following the introduction of FRS12, as it is no longer possible to account for the difference between planned and actual expenditure on infrastructure renewals as a provision or prepayment. As a consequence the balance sheet has been restated to take account of necessary changes since 1 April 1989, when renewals accounting was first adopted in the accounts, and any previous provisions or prepayments have been subsumed into fixed assets. Further information is given in note 8. This change of accounting policy has no effect on the profit and loss account other than to reclassify the renewals charge as depreciation.

The depreciation charge for infrastructure assets is the estimated level of average annual expenditure required to maintain the operating capability of the network, based upon the company's independently certified asset management plan. No other 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.

- ii Other assets include properties, plant and equipment and are shown at cost less accumulated depreciation. Freehold land is not depreciated. Other assets are depreciated evenly over their estimated economic lives, which are principally as follows:

Buildings and operational structures	15 - 80 years
Plant, machinery and vehicles	3 - 30 years
Other assets	4 - 15 years

d. Leased assets

Where assets are financed by leasing arrangements which transfer substantially all the risks and rewards of ownership of an asset to the lessee (finance leases), the assets are treated as if they had been purchased and the corresponding capital cost is shown as an obligation to the lessor. Leasing payments are treated as consisting of a capital element and finance costs, the capital element reducing the obligation to the lessor and the finance charge being written off to the profit and loss account over the period of the lease in reducing amounts in relation to the outstanding obligations. The assets are depreciated over the shorter of their estimated useful lives and the period of the lease.

All other leases are regarded as operating leases. Rental costs arising under operating leases are written off in the year they are incurred.

e. **Grants and contributions**

Grants and contributions in respect of specific expenditure on non-infrastructure fixed assets are treated as deferred income and recognised in the profit and loss account over the expected useful economic lives of the related assets.

Grants and contributions relating to infrastructure assets have been deducted from the cost of those assets. This is not in accordance with the Companies Act 1985 which requires assets to be stated at their purchase price or production cost, without deduction of grants and contributions which would be accounted for as deferred income. The departure from the requirement of the Act is, in the opinion of the directors, necessary to give a true and fair view. This is because infrastructure assets are not depreciated and accordingly the related grants and contributions would not be recognised through the profit and loss account. The effect on the value of fixed assets is disclosed in note 8.

f. **Investments**

Investments held as fixed assets are stated at cost less any provisions for impairment. Those held as current assets are stated at the lower of cost and net realisable value.

g. **Stock**

Stock and work in progress are stated at the lower of cost and net realisable value. In respect of work in progress, cost includes labour, materials and attributable overheads.

h. **Foreign currency**

All transactions denominated in foreign currencies are translated into sterling at the actual rates of exchange ruling at the dates of the transactions. Foreign currency balances are translated into sterling at the rates of exchange ruling at the balance sheet date.

i. **Research and development**

Research and development expenditure is written off in the year in which it is incurred.

j. **Taxation**

The charge for taxation is based on the profit for the period adjusted in accordance with tax legislation. Tax deferred or accelerated is accounted for in respect of all material timing differences to the extent that it is probable that a liability or asset will crystallise. Timing differences arise from the inclusion of items of income and expenditure in tax computations in periods different from those in which they are included in the accounts. Provision is made at the rate which is expected to apply when the liability or asset crystallises.

k. **Pensions**

The cost of providing benefits is charged to the profit and loss account on a basis designed to spread the cost over the expected average service lives of employees. Differences between the amounts funded and amounts charged to the profit and loss account are treated either as provisions or prepayments in the balance sheet. The pension schemes are of the defined benefit type, which are externally funded and valued by an independent actuary.

l. **Cash flow**

Under the provisions of FRS1 (revised) the company has not prepared a cash flow statement because its ultimate parent company Azurix Corp., which is incorporated in Delaware, USA, prepares consolidated accounts which include the accounts of the company and which contain a cash flow statement.

2 **Segmental analysis**

	12 months to 31.12.99	9 months to 31.12.98
	£m	£m

Analysis by class of business

a. **Turnover**

Water supply	90.6	66.2
Waste treatment	187.9	135.5
Intra group income	0.3	0.5
	<u>278.8</u>	<u>202.2</u>

	12 months to 31.12.99 £m	9 months to 31.12.98 £m
b. Operating profit		
Water supply	40.4	30.5
Waste treatment	112.5	82.0
	<u>152.9</u>	<u>112.5</u>
Operating profit by class of business is determined after allocating central costs on the basis of estimated time spent on each class of business. Interest payable cannot be allocated to class of business.		
c. Net assets		
Water supply	377.3	347.1
Waste treatment	768.3	685.1
Interest bearing operating liabilities	(548.1)	(469.4)
	<u>597.5</u>	<u>562.8</u>
3 Operating profit		
a. Operating profit is shown after charging (crediting) the following items:		
Operational costs		
Manpower costs (note 6)	25.4	16.4
Materials and consumables	15.4	12.0
Other operational costs	37.5	27.9
	<u>78.3</u>	<u>56.3</u>
Depreciation		
Depreciation – as restated	47.3	33.3
Amortisation of grants and contributions	(0.7)	(0.6)
Loss on disposals of fixed assets	1.0	0.7
	<u>47.6</u>	<u>33.4</u>
	<u>125.9</u>	<u>89.7</u>
b. Operational costs include:		
Operating leases for plant and machinery	0.4	0.5
Other operating leases	0.4	0.3
Research and development	0.3	0.1
Directors' remuneration (note 6)	0.5	0.6
Audit fees	0.1	0.1
	<u>0.1</u>	<u>0.1</u>
4 Net interest payable		
Interest payable:		
To group companies	15.3	11.2
On bank loans	11.3	7.5
On other loans	0.5	0.3
On finance leases	4.5	3.9
Total interest payable	<u>31.6</u>	<u>22.9</u>
Interest (receivable)	(3.1)	(1.0)
Net interest payable	<u>28.5</u>	<u>21.9</u>
5 Taxation		
a. Taxation on profit on ordinary activities		
UK corporation tax at 30.25% (1998 – 31%)	4.2	5.7
Advance corporation tax due to parent company	8.5	11.0
Payment for group relief	7.5	0.4
	<u>20.2</u>	<u>17.1</u>

b. Deferred taxation

No deferred tax has been provided as projections indicate that the potential liability will not crystallise within the foreseeable future. The full potential amount of deferred taxation calculated at 30% on all timing differences is as follows:

	12 months to 31.12.99 £m	9 months to 31.12.98 £m
Accelerated capital allowances	225.7	215.3
Other timing differences	(4.5)	(4.8)
	<u>221.2</u>	<u>210.5</u>

Included in accelerated capital allowances are timing differences on infrastructure assets.

6 Directors and employees

a. Total employment costs of the company were:

Wages and salaries	34.3	21.5
Social security costs	2.5	1.7
Other pension costs	2.1	2.4
	<u>38.9</u>	<u>25.6</u>

b. Total employment costs are charged as follows:

Capital schemes	12.2	8.3
Infrastructure renewals expenditure	1.3	0.9
Manpower costs	25.4	16.4
	<u>38.9</u>	<u>25.6</u>

c. Total directors' remuneration

	12 months to 31.12.99 £000	9 months to 31.12.98 £000
Fees	98	24
Salary	305	400
Bonuses	58	136
Benefits in kind	23	31
	<u>484</u>	<u>591</u>

Seven directors have benefits accruing under defined benefit pension schemes (1998 - 7).

d. Highest paid director

Salary	85	119
Bonus	23	37
Benefits in kind	6	6
	<u>114</u>	<u>162</u>

The highest paid director had an accrued pension entitlement of £21,592 at 31 December 1999 (1998 - £11,041).

e. Monthly average number of employees during the period

	31.12.99	31.12.98
- Engineering department	213	185
- All other staff	1,188	1,181
- Total	<u>1,401</u>	<u>1,366</u>

7 Dividends

The dividend policy is to declare ordinary dividends of two thirds of the historic profit attributable to shareholders, subject to a current cost ordinary dividend cover of one.

	12 months to 31.12.99 £m	9 months to 31.12.98 £m
Interim dividends of 38.97p on 81,350,000 ordinary shares (1998 - 29.50p)	31.7	24.0
Final dividend of 46.46p per share on 81,350,000 ordinary shares (1998 - 30.73p)	37.8	25.0
	<u>69.5</u>	<u>49.0</u>

8 **Tangible fixed assets**

	Freehold land & buildings	Infra- structure assets	Plant machinery & vehicles	Other assets	Payments on account & assets in course of construction	Total
	£m	£m	£m	£m	£m	£m
Cost						
At 1 January 1999 (restated)	380.4	601.8	399.4	31.6	92.9	1,506.1
Additions	4.7	31.9	27.2	4.0	84.7	152.5
Transfers on commissioning	8.2	26.2	16.0	0.5	(50.9)	-
Disposals	(0.7)	-	(6.3)	(1.4)	(0.8)	(9.2)
Grants and contributions	-	(3.7)	-	-	-	(3.7)
At 31 December 1999	<u>392.6</u>	<u>656.2</u>	<u>436.3</u>	<u>34.7</u>	<u>125.9</u>	<u>1,645.7</u>
Depreciation						
At 1 January 1999 (restated)	70.0	106.4	151.8	17.7	-	345.9
Provision for the period	6.3	11.2	25.1	4.7	-	47.3
Disposals	(0.3)	-	(5.4)	(1.3)	-	(7.0)
At 31 December 1999	<u>76.0</u>	<u>117.6</u>	<u>171.5</u>	<u>21.1</u>	<u>-</u>	<u>386.2</u>
Net book value						
At 31 December 1999	<u>316.6</u>	<u>538.6</u>	<u>264.8</u>	<u>13.6</u>	<u>125.9</u>	<u>1,259.5</u>
At 1 January 1999 (restated)	<u>310.4</u>	<u>495.4</u>	<u>247.6</u>	<u>13.9</u>	<u>92.9</u>	<u>1,160.2</u>

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

Other assets include furniture and fittings, laboratory and other equipment.

The net book value of assets held under finance leases is £80.4m (31.12.98 - £82.3m).

The depreciation charge for the year on assets held under finance leases is £1.9m (9 months to 31.12.98 - £1.4m).

The net book value of infrastructure assets at 31 December 1999 is stated after the deduction of grants and contributions amounting to £51.0 m (31.12.98 - £47.3m) in order to give a true and fair view (note 1e).

Included in the cost of infrastructure assets is £124.5m (31.12.98 - £109.9m) of expenditure on maintaining the network previously charged to the infrastructure renewals provision, and £117.6m (31.12.98 - £106.4m) of depreciation previously included in the profit and loss account as an infrastructure renewals charge (note 1c). This prior year adjustment has not had any impact on the profit of the company in either period.

Included in freehold land and buildings above is an amount of £6.3m (31.12.98 - £6.3m) in respect of land which is not depreciated.

	31.12.99	31.12.98
	£m	£m
9 Investments		
The company has an investment of £13,000 in Wessex Water Services Finance Plc, a company that was set up on 12 February 1999 for the purpose of issuing a bond, the proceeds of which were lent to the company.		
10 Stock and work in progress		
Stock	0.4	0.4
Work in progress	0.7	0.7
	<u>1.1</u>	<u>1.1</u>

11 Debtors

Amounts falling due within one year

Trade debtors	30.1	35.5
Owed by associated undertakings	0.8	-
Owed by ultimate parent company	1.0	-
Other debtors	4.7	5.7
Prepayments and accrued income	25.7	22.4
	<u>62.3</u>	<u>63.6</u>

An infrastructure renewals prepayment of £3.5m at 31 December 1998 has been reclassified in fixed assets (see note 8).

12 Creditors - amounts falling due within one year

Bank overdraft repayable on demand	1.7	31.6
Loans repayable	8.2	243.2
Obligations under finance leases	15.1	12.9
Trade creditors	1.5	9.6
Amounts owed to parent company	38.2	106.3
Amounts owed to subsidiary undertaking	13.3	-
Dividend	37.8	25.0
Other creditors	1.8	0.6
Corporation tax	21.7	22.6
Taxation and social security	0.8	0.7
Accruals and deferred income	80.6	84.7
	<u>220.7</u>	<u>537.2</u>

13 Creditors - amounts falling due after more than one year

Loans repayable	- within 1 - 2 years	33.3	3.2
	- within 2 - 5 years	1.6	34.9
	- over 5 years	100.0	-
		<u>134.9</u>	<u>38.1</u>
Obligations under finance leases	- within 1 - 2 years	17.6	15.2
	- within 2 - 5 years	20.3	37.9
		<u>37.9</u>	<u>53.1</u>
Inter company loan		296.7	-
Other		2.7	2.6
		<u>472.2</u>	<u>93.8</u>

The inter company loan is due to a subsidiary company Wessex Water Services Finance Plc in respect of the proceeds of a bond issue lent to the company at an interest rate of 5.875%, repayable in March 2009.

14 Provisions for liabilities and charges

	31.12.98 £m	Provided £m	Utilised £m	31.12.99 £m
Pensions	5.7	0.8	(0.1)	6.4
Office relocation	2.9	0.3	(1.5)	1.7
Restructuring costs – severances	-	2.1	-	2.1
	<u>8.6</u>	<u>3.2</u>	<u>(1.6)</u>	<u>10.2</u>

The adoption of FRS12 “Provisions, Contingent Liabilities and Contingent Assets” did not give rise to any restatement of provisions.

	31.12.99 £m	31.12.98 £m
15 Deferred income		
Grants and contributions		
At 1 January (1 April)	22.5	22.9
Received in the period	0.5	0.2
Less amortisation	(0.7)	(0.6)
At 31 December	<u>22.3</u>	<u>22.5</u>

16 Called up share capital

Ordinary shares of £1 each: Authorised, allotted, called up and fully paid	<u>81.3</u>	<u>81.3</u>
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17 Profit and loss account and shareholders' funds

	Profit & loss account £m	Share- holders' funds £m
At 1 January 1999	481.5	562.8
Transfer to reserves	34.7	34.7
At 31 December 1999	<u>516.2</u>	<u>597.5</u>

18 Financial instruments

Short term debtors and creditors have been excluded from the financial instruments disclosure other than £25.0m of short term borrowings.

The company has financed its activities through a combination of short term borrowings, long term loans and leases and a bond issued by its subsidiary company Wessex Water Services Finance Plc.

The company uses derivative financial instruments to reduce the exposure to foreign currency fluctuations and to limit exposure to floating interest rates.

The principal borrowings are both fixed rate and in sterling.

a. Interest rate and currency exposure

	Fixed rate borrowings £m	Floating rate borrowings £m	Total borrowings £m
Sterling	349.7	106.7	456.4
US dollar	30.0	-	30.0
Italian lira	8.1	-	8.1
At 31 December 1999	<u>387.8</u>	<u>106.7</u>	<u>494.5</u>

The interest rates and period to maturity of the fixed rate borrowings are as follows:

	Interest rate %	Period years
Sterling	6.06	8.3
US dollar	6.04	1.8
Italian lira	5.16	2.5
Weighted average	<u>6.04</u>	<u>7.6</u>

£6.7m of floating rate borrowings are short term, and £100.0m are long term with interest rates moving in line with LIBOR.

b. Fair values

Fair value is the amount at which a financial instrument could be exchanged in an arms length transaction between informed and willing parties, other than a forced or liquidation sale.

	Book value £m	Fair value £m
Borrowings less than 1 year	25.0	25.0
Floating rate borrowings over 1 year	100.0	100.0
Fixed rate borrowings over 1 year	369.5	304.5
At 31 December 1999	<u>494.5</u>	<u>429.5</u>

The fair value of short term and floating rate borrowings approximate to book value. The fair value of long term fixed rate borrowings has been calculated using market values or discounted cash flow techniques.

c. Interest rate and currency swaps

US dollar borrowings of \$51.0m at floating rates have been swapped into sterling borrowings of £30.0m at fixed rates, and through further interest rate swaps have been fixed at 6.04%.

Italian lira borrowings of ITL17,850 at fixed rates have been swapped into sterling borrowings of £8.1m at floating rates and through interest rate swaps have been fixed at 5.16%.

19 Commitments

a. Operating lease payments under leases on land and buildings due within the next year in respect of leases which expire:	31.12.99	31.12.98
	£m	£m
Between 2 and 5 years	0.3	0.2
Over 5 years	-	0.2
	<u>0.3</u>	<u>0.4</u>

b. At 31 December 1999 the company had interest rate and currency instrument agreements outstanding with commercial banks with a principal value of £169.9m (31.12.98 - £301.3m).

c. Capital expenditure contracted but not provided at 31 December 1999 was £78.1m (31.12.98 - £78.3m).

20 Contingent liabilities

There are no material contingent liabilities at 31 December 1999 for which provision has not been made in these accounts.

21 Pensions

The defined benefit schemes, which cover the majority of staff, are the Wessex Water Pension Scheme (WWPS), the Wessex Water Mirror Image Pension Scheme (WWMIS), and the Wessex Water Executive Pension Scheme (WWEPS). The assets are held in separate trustee administered funds. The pension cost charged to the profit and loss account has been determined on the advice of independent qualified actuaries and is such as to spread the cost of pensions over the service lives of members of the schemes.

The total pension cost of the company, including amounts set aside for employees retiring early, was £2.1m (9 months to 31.12.98 - £2.4m).

The latest actuarial valuations for WWPS, WWMIS and WWEPS were undertaken as at 31 December 1998. The projected unit method was used for the WWPS valuation and the attained age method for the WWMIS and WWEPS valuations. The assumptions which have the most significant effect on the results of a valuation are those relating to the rate of return on investments and the rates of increase in salaries and pensions. It was assumed that the investment returns would be 6.25% per annum for all schemes, that salary increases would average 3.5% per annum and that present and future pensions would increase at the rate of 2.5% per annum. The market value of the WWPS assets as at 31 December 1998 was £112.4m, for WWMIS £40.6m and for WWEPS £2.7m. The valuation showed that the actuarial value of the assets at 31 December 1998 represented 118%, 124% and 117% of the actuarial value of the accrued benefits for the WWPS, WWMIS and WWEPS respectively.

The WWMIS and the WWEPS have been merged into the WWPS with effect from 1 January 2000. Some benefit improvements were awarded as part of the merger process. The impact of the merger will be reflected in pension costs from 1 January 2000 onwards. The next actuarial valuation will be as at 31 December 2001.

22 Related parties

There are no related party transactions requiring disclosure in these accounts.

23 Ultimate parent company

The smallest group into which the accounts of the company are consolidated is that headed by Wessex Water Ltd a company incorporated in the United Kingdom whose registered address is Wessex House, Passage Street, Bristol, BS2 0JQ.

The directors consider the ultimate parent company to be Azurix Corp., a Delaware corporation, and the consolidated accounts of this company are available as part of its filing with the US Securities and Exchange Commission, which can be accessed through the Commission's office or its website www.sec.gov.

24 Going concern

The current liabilities of the company exceed its current assets. The directors have considered the financial position of the company and have concluded that it will be able to meet its liabilities as they fall due for the foreseeable future. For these purposes the foreseeable future is taken to mean a period of at least 12 months from the date of approval of these accounts.