

**FINANCIAL STATEMENTS**  
**NORTHUMBRIAN WATER LIMITED**  
**FOR THE YEAR ENDED 31 DECEMBER 1999**

Registered no: 2366703



Registered office  
Northumbria House  
Regent Centre  
Gosforth  
Newcastle Upon Tyne  
NE3 3PX

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# FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 1999

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## **DIRECTORS' REPORT**

### **For the year ended 31 December 1999**

The directors present their report and the audited financial statements for the year ended 31 December 1999.

#### **Results and dividends**

The group's profit after taxation for the year ended 31 December 1999 amounts to £125.5m (December 1998 (as restated) : £119.3m). The directors propose a final dividend on the ordinary shares of the company of £32.2m (December 1998: £30.7m) which, together with the interim dividend of £32.2m (December 1998: £30.7m), makes a total for the year of £64.4m (December 1998 £61.4m).

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

The principal activities of the business comprise the supply of potable water, and the collection, treatment and disposal of sewage and sewage sludge throughout the region.

Compliance levels remain high, the investment programme remains on target to deliver the required obligations by March 2000 and operating efficiencies as a result of further restructuring have been achieved during the year which have offset the impact of additional operating costs from new sewage and sludge treatment facilities on Teesside and the cost of ensuring year 2000 compliance. This has allowed a cumulative reduction of 10% to be made in customers' water bills from April 1999 representing the merger discount.

The future focus of the company remains on improving efficiency levels and driving down operating costs while maintaining high standards of customer service and developing the skills and effectiveness of its employees. Continuous improvement will be necessary to ensure the company is successful in the competitive market. The recent price review by Ofwat, which resulted in the company receiving the largest price reduction amongst the water and sewerage companies, has increased the pressure on the company to provide better customer service at lower cost. It also ensured that the company continues to provide water and sewage services at a very competitive price.

#### **Financial Statements Preparation and Going Concern**

The Directors consider that it is appropriate to prepare the financial statements for the financial year on a going concern basis. The Directors have arrived at their decision based on consideration of the company's detailed budget for 2000 and the five year business plan for the period from 2000 to 2004. Their analysis included a review of the capital expenditure and investment plans, the anticipated funding requirements and facilities available, and the reasonableness of the underlying assumptions of both the budget and business plans.

#### **Research and development**

The company places a high priority on research and technological innovation to serve the needs of customers. Research and development is now co-ordinated by a sister company, Northumbrian Lyonnaise Technology and Research Centre Limited, a specialist subsidiary, wholly owned by the company's immediate parent, which has links with other Suez Lyonnaise des Eaux group research organisations worldwide. The company incurred costs of Research and development in the period of £4.7m (December 1998: £4.5m).

#### **Northumbrian Water Limited payment policy**

The company's policy is to agree payment terms with suppliers when agreeing the terms of each transaction, also ensuring that suppliers are made aware of the terms of payment and abide by the terms of payment. The year end trade creditors expressed as a number of days of purchases made during the year is 29 days (December 1998: 33 days). This has been calculated by dividing the year end trade creditors balance of £1.8m by the aggregate of the average daily amounts invoiced by suppliers during the year.

#### **Fixed Assets**

Freehold land and buildings are carried in the accounts at historical cost with a net book value of £39.7m (December 1998: £39.5m). In the opinion of the directors, at 31 December 1999, there is no significant difference between the net book value and market value of property capable of disposal within the foreseeable future.

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

### **Year 2000**

The Northumbrian Water Group Year 2000 Programme, which was initiated in June 1997, achieved its objective of ensuring that there was no significant impact upon the company's business as a result of Year 2000 issues. Early in January 2000 we reported business-as-usual over the Millennium period with a few minor date related problems, some of which had been predicted and had solutions in place, and the rest of which are either now fixed or are of an inconsequential nature. Satisfactory customer service was achieved throughout the critical period.

The company compiled a brief project closure report, detailing lessons learned and business benefits achieved, as well as confirming a successful project outcome. These benefits have included the completion of updated and consolidated asset inventories, the removal of redundant processes and systems, an increase in the consideration given to business continuity planning, and the improvement of relationships with customers and suppliers.

The overall programme costs for Northumbrian Water Limited, over the two and a half years of the programme, was £7.1m, of which £4.4m related to the upgrade or replacement of assets and was capitalised. There are no significant costs still to be incurred.

The final cost of ensuring compliance was significantly lower than forecast in the previous year's accounts. This was mainly because the number of assets that were found to be non-compliant was lower than was initially predicted. It also reflected that only those non-compliant assets which were identified as being business critical were replaced or upgraded, whilst the remaining assets were subject to continuous monitoring over the millennium period *and only replaced or upgraded when required.*

### **Financial Review**

The level of capital expenditure which the company is obliged to incur is such that it cannot be wholly financed by internally generated sources. As a result, the company must rely upon raising additional finance on a regular basis, to be principally used to fund the long term assets required in its regulated businesses. The strategy of Northumbrian Water Group, of which the company is a subsidiary, is to finance such investment by raising medium to long term debt, to provide a balance sheet match with long term assets and to fix a major proportion of interest rates.

### **Post Balance Sheet Events**

Details of the Post Balance Sheet event is shown in note 30 of the financial statements.

## DIRECTORS' REPORT (continued)

### Directors

The directors who served during the year were as follows:

H D M Speed	(Chairman)
P Babin	
L M Caple	
J A Cuthbert	
J Graham	
A J Harding	(Managing Director)
A F Jones	(Resigned 1 January 1999)
G Neave	
Dr A C Price	(Resigned 1 April 1999)
S M Straw	(Appointed 1 January 1999)
Dr D A Trebilco	

Non executive directors were as follows:

P Babin  
HEC MBA

Managing Director, Northumbrian Water Group plc, January 1996; Corporate Director (Finance), Lyonnaise des Eaux, 1993; Finance Director, Essex and Suffolk Water plc and Lyonnaise Europe plc, 1990 – 1992. Patrick Babin joined Lyonnaise des Eaux in 1987, following several years in the oil industry.

L M Caple

Non Executive Director, January 1998  
Chief Executive of the Northumbria Ambulance Service NHS Trust.

J A Cuthbert  
BSc ACA MBA

Non Executive Director, 1996; Managing Director, Essex and Suffolk Water plc, 1996; Board Member, Managing Director, North East Water plc, 1993 – 1996; Finance Director and Deputy Managing Director, 1991 – 1993; Financial Controller, North Eastern Co-operative Society, 1986 – 1990.

H Speed OBE  
BSc MEng FICE FIWEM

Chairman, Northumbrian Water Limited and Non Executive Director, Northumbrian Water Group plc, 1996; Vice President, Lyonnaise International Water Division, 1993; Board Director, Essex and Suffolk Water plc; formerly Board Director and Managing Director of North East Water plc; Managing Director, Newcastle and Gateshead Water plc, 1986.

D A Trebilco

Non Executive Director, January 1998  
Director of the Aromatics, Imagedata and Propofilm business of ICI

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

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

### **Employees and Employment Policies**

#### Equal Opportunities

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

#### Training and Development

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

#### Communication

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

#### Health and Safety

Health and safety policies are maintained and implemented through the company's safety team. Employee health services are provided by the company's Medical Adviser. Most employees are members of a company wide corporate health care plan managed by CIGNA Healthcare. The company has also introduced HSA Healthplan, which is employee funded, with effect from 1 January 2000.

#### Employee Investment Schemes

During the financial year and for the third consecutive year, the company has operated an employee investment scheme. The structure of the employee share investment plan this year was different from the two preceding years.

The new plan called SPRING consisted of two elements, which gave employees a choice of two different types of investment. The first investment possibility was investing in a fund, SPRING Classic, which owned Suez Lyonnaise des Eaux shares purchased at a discount, a similar investment to that offered in previous plans. The second type of investment was in a specially created company, SPRING Multiple, which also purchased shares in the parent company. This investment guarantees the employee the return of their initial investment but gives the opportunity to increase their share in any growth in value of the ultimate parent company's shares through the existence of a matched investment by Credit Agricole Indosuez.

The opportunity to invest in the plan was limited to Suez Lyonnaise des Eaux group employees, and was offered to all such employees in the United Kingdom. To encourage participation in the plan the company made a discretionary contribution of up to £100 for all employees investing in SPRING Classic.

The Board of Directors believes that employee investment is a valuable method of strengthening the ties between its employees and Suez Lyonnaise des Eaux by providing the opportunity for employees to participate more closely in its economic performance and results. A total of 66% of employees participated in SPRING 1999.

### **Pensions**

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

## DIRECTORS' REPORT (continued)

### Charitable and Political Contributions

During the year the company made charitable donations of £29,706 (December 1998: £25,611). The company made no donations to any political party during the year (December 1998: £Nil).

### Auditors

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

### Directors' Responsibilities

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

The directors confirm that suitable accounting policies have been used and applied consistently, and reasonable, prudent judgements and estimates have been made in the preparation of the financial statements for the year ended 31 December 1999. The directors also confirm that applicable accounting standards have been followed and that the financial statements have been prepared on the going concern basis.

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

### Auditors' Responsibilities

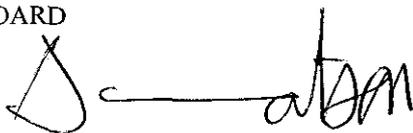
The auditors are responsible for forming an independent opinion on the financial statements presented by the Directors, based on their audit, and reporting their opinion to shareholders. Company law also requires the auditors to report to shareholders if the following requirements are not met:

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

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

BY ORDER OF THE BOARD

D J Watson  
Company Secretary  
28 March 2000



## REPORT OF THE AUDITORS

### To the shareholders of Northumbrian Water Limited:

We have audited the financial statements on pages 7 to 37, which have been prepared under the historical cost convention, and the accounting policies set out on pages 12 to 14.

### Respective responsibilities of directors and auditors

As described on page 5 the company's directors are responsible for the preparation of the financial statements 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 guidance.

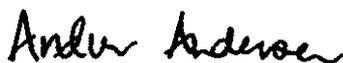
### Basis of opinion

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 circumstances of the company and the group, consistently applied and adequately disclosed.

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

### Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the company and of the group at 31 December 1999 and of the group's profit and cash flows for the year then ended and have been properly prepared in accordance with the Companies Act 1985.



Arthur Andersen  
Chartered Accountants and Registered Auditors  
Pearl Assurance House  
7 New Bridge Street  
Newcastle Upon Tyne  
NE1 8BQ

28 March 2000

**GROUP PROFIT AND LOSS ACCOUNT**  
**For the year ended 31 December 1999**

	Note	December 1999	December 1998 (as restated)
		£'m	£'m
Turnover	3	379.5	361.5
Operating costs	4(a)	(125.6)	(125.7)
Capital maintenance costs	4(b)	(54.4)	(49.8)
Exceptional operating costs	4(c)	(8.5)	(2.4)
<b>OPERATING PROFIT</b>		<b>191.0</b>	<b>183.6</b>
Net interest payable	5	(34.1)	(33.7)
<b>PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION</b>		<b>156.9</b>	<b>149.9</b>
Taxation	9	(31.4)	(30.6)
<b>PROFIT FOR THE FINANCIAL YEAR</b>		<b>125.5</b>	<b>119.3</b>
Dividends	10	(64.4)	(61.4)
<b>PROFIT RETAINED FOR THE YEAR</b>	<b>25</b>	<b>61.1</b>	<b>57.9</b>

All turnover and operating profit derive from continuing operations.  
The movement on reserves is shown in note 25.

**STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES**

	December 1999	December 1998 (as restated)
	£'m	£'m
Total recognised gains in the financial year	125.5	119.3
Prior year adjustment (note 2)	4.9	-
<b>Total gains and losses recognised since last annual report and financial statements</b>	<b>130.4</b>	<b>119.3</b>

The accompanying notes are an integral part of this consolidated profit and loss account and statement of total recognised gains and losses.

## GROUP BALANCE SHEET

At 31 December 1999

	Note	December 1999	December 1998 (as restated)
		£'m	£'m
<b>FIXED ASSETS</b>			
Tangible assets	11	1,719.7	1,562.4
<b>CURRENT ASSETS</b>			
Stocks	13	1.9	2.8
Debtors: amounts falling due within one year	14	70.7	68.6
Debtors: amounts falling due after more than one year	14	11.7	14.2
Investments	15	75.0	103.2
Cash at bank and in hand		3.7	-
		163.0	188.8
<b>CREDITORS</b>			
Amounts falling due within one year	16	(196.9)	(207.2)
<b>NET CURRENT LIABILITIES</b>			
		(33.9)	(18.4)
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>			
		1,685.8	1,544.0
<b>CREDITORS: Amounts falling due after more than one year</b>			
	17	(612.7)	(541.7)
<b>PROVISIONS FOR LIABILITIES AND CHARGES</b>			
	22	(17.8)	(12.2)
<b>ACCRUALS AND DEFERRED INCOME</b>			
	23	(84.7)	(80.6)
		(715.2)	(634.5)
<b>NET ASSETS</b>			
		970.6	909.5
<b>CAPITAL AND RESERVES</b>			
Called up share capital	24	122.7	122.7
Profit and loss account	25	847.9	786.8
<b>EQUITY SHAREHOLDERS' FUNDS</b>			
	26	970.6	909.5

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

Approved on behalf of the board on 28 March 2000

A J Harding  
Director



G Neave  
Director



## COMPANY BALANCE SHEET

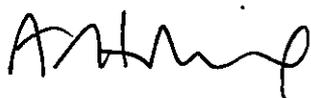
At 31 December 1999

	Note	December 1999	December 1998 (as restated)
		£'m	£'m
<b>FIXED ASSETS</b>			
Tangible assets	11	1,719.7	1,562.4
Investments	12	47.2	47.2
		1,766.9	1,609.6
<b>CURRENT ASSETS</b>			
Stocks	13	1.9	2.8
Debtors: amounts falling due within one year	14	70.7	68.6
Debtors: amounts falling due after more than one year	14	11.7	14.2
Investments	15	75.0	103.2
Cash at bank and in hand		3.7	-
		163.0	188.8
<b>CREDITORS</b>			
Amounts falling due within one year	16	(196.9)	(207.2)
<b>NET CURRENT LIABILITIES</b>			
		(33.9)	(18.4)
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>			
		1,733.0	1,591.2
<b>CREDITORS: Amounts falling due after more than one year</b>			
	17	(659.9)	(588.9)
<b>PROVISIONS FOR LIABILITIES AND CHARGES</b>			
	22	(17.8)	(12.2)
<b>ACCRUALS AND DEFERRED INCOME</b>			
	23	(84.7)	(80.6)
		(762.4)	(681.7)
<b>NET ASSETS</b>			
		970.6	909.5
<b>CAPITAL AND RESERVES</b>			
Called up share capital	24	122.7	122.7
Profit and loss account	25	847.9	786.8
<b>EQUITY SHAREHOLDERS' FUNDS</b>			
	26	970.6	909.5

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

Approved on behalf of the board on 28 March 2000

A J Harding  
Director



G Neave  
Director



**GROUP CASH FLOW STATEMENT**  
**For the year ended 31 December 1999**

	Note	December 1999	December 1998 (as restated)
		£'m	£'m
<b>NET CASH INFLOW FROM CONTINUING OPERATING ACTIVITIES</b>			
	a	250.3	211.4
<b>Return on investments and servicing of finance</b>			
Interest received		8.5	8.8
Interest paid		(37.0)	(28.1)
Interest element of finance lease rentals		(1.6)	(0.5)
Net cash outflow from returns on investments and servicing of finance		(30.1)	(19.8)
<b>Taxation</b>			
United Kingdom corporation tax paid		(33.5)	(36.4)
Net cash outflow from taxation		(33.5)	(36.4)
<b>Capital expenditure and financial investment</b>			
Purchase of tangible fixed assets		(212.2)	(190.9)
Sale of tangible fixed assets		1.4	1.6
Grants, contributions and connection charges		6.6	7.6
Net cash outflow from capital expenditure and financial investment		(204.2)	(181.7)
		(62.9)	(45.5)
<b>Equity dividends paid</b>			
<b>Management of liquid resources</b>			
Purchase of short term deposits		(813.4)	(541.4)
Sale of short term deposits		841.6	443.4
Net cash inflow/(outflow) from management of liquid resources		28.2	(98.0)
<b>Financing</b>			
New loans	b	75.0	194.2
New leases	b	11.5	-
Loan repayment receipts from other Group company		2.4	2.0
Loan repayments	b	(26.7)	(34.0)
Capital element of finance lease rental payments	b	(3.0)	-
Net cash inflow	b	59.2	162.2
<b>INCREASE /(DECREASE) IN CASH IN THE YEAR</b>		<b>7.0</b>	<b>(7.8)</b>

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

Prior year cash flows relating to infrastructure are now included in the purchase of tangible fixed assets (note 2).

**NOTES TO THE CASH FLOW STATEMENT**  
**For the year ended 31 December 1999**

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

	Note	December 1999	December 1998 (as restated)
		£'m	£'m
Operating profit		191.0	183.6
Depreciation of tangible fixed assets	4(b)	55.7	50.4
Amortisation of capital grants	4(d)	(2.4)	(2.3)
Profit on sale of fixed assets	4(b)	(1.3)	(0.6)
Decrease in stock	13	0.9	1.1
Increase in debtors		(2.3)	(8.7)
Increase/(Decrease) in creditors		3.1	(11.0)
Restructuring provision	22	5.6	(1.1)
Net cash inflow from operating activities		<u>250.3</u>	<u>211.4</u>

The operating cash flows are all from continuing operations.

**b ANALYSIS AND RECONCILIATION OF NET DEBT**

	1 January 1999	Cash Flow	Other non-cash changes	31 December 1999
	£'m	£'m	£'m	£'m
Cash at bank and in hand	-	3.7	-	3.7
Overdrafts	(3.3)	3.3	-	-
	<u>(3.3)</u>	<u>7.0</u>	<u>-</u>	<u>3.7</u>
Debt due after 1 year	(495.2)	(75.0)	10.2	(560.0)
Debt due within 1 year	(26.7)	24.3	(8.0)	(10.4)
Finance leases	(47.1)	(8.5)	(0.8)	(56.4)
	<u>(569.0)</u>	<u>(59.2)</u>	<u>1.4</u>	<u>(626.8)</u>
Current asset investments	103.2	(28.2)	-	75.0
Net debt	<u>(469.1)</u>	<u>(80.4)</u>	<u>1.4</u>	<u>(548.1)</u>

**Reconciliation of cash flow movement to net debt:**

	December 1999
	£'m
Increase in cash in the year	7.0
Cash inflow from increase in debt and lease financing	(59.2)
Cash inflow from reduction in liquid resources	(28.2)
Change in net debt resulting from cash flows	(80.4)
Finance costs incurred during the year	(0.2)
Finance lease interest capitalised	(0.8)
Movement in loan acquired from debt reorganisation	2.4
Movement in net debt in year	(79.0)
Net debt at 1 January 1999	(469.1)
Net debt at 31 December 1999	<u>(548.1)</u>

**NOTES TO THE FINANCIAL STATEMENTS**  
**For the year ended 31 December 1999**

**1 STATEMENT OF ACCOUNTING POLICIES**

These financial statements have been prepared in accordance with applicable Accounting Standards in the United Kingdom. A summary of the more important accounting policies, which have been applied consistently throughout the current and preceding years except as outlined in note 1(b), is set out below:

**(a) Basis of accounting**

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

**(b) Changes in presentation of financial statements**

A number of new Financial Reporting Standards (FRS) introduced during the year have been adopted with no material effect on the Group's financial statements. It has been necessary to change the method of accounting for infrastructure maintenance expenditure following the adoption of FRS 12 "Provisions, contingent liabilities and contingent assets" and FRS 15 "Tangible Fixed Assets", 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 show planned and actual expenditure since the year to 31 March 1989, when renewal accounting was first adopted in the accounts, as fixed asset depreciation and fixed asset additions respectively. This has the effect of removing the provision for infrastructure renewals of £1.4m at 31 December 1998 and reducing fixed assets by the same amount. This change of accounting disclosure has no effect on the profit and loss account other than to reclassify the previous year's infrastructure renewal charge of £20.2m as depreciation.

In previous years, grants and contributions relating to infrastructure assets have been deducted from the cost of fixed assets. This was not in accordance with schedule 4 of the Companies Act 1985 which requires fixed assets to be shown at their purchase price or production cost but the departure from the requirements of the Act was felt to be necessary in order to show a true and fair view as infrastructure assets were not depreciated. Following the adoption of FRS 12 and FRS 15 as noted above, a depreciation charge is now shown against infrastructure assets within tangible fixed assets. As a consequence, the balance sheet has been restated to show grants and contributions relating to infrastructure assets as accruals and deferred income. This has had the effect of increasing the cost of tangible fixed assets at 31 December 1998 by £55.5m and increasing accruals and deferred income by £50.6m. The difference of £4.9m representing amortisation of grants and contributions in respect of prior years, has been credited to retained profit and loss reserves as a prior year adjustment.

**(c) Basis of consolidation**

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

**(d) Turnover**

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

## 1. STATEMENT OF ACCOUNTING POLICIES (continued)

### (e) **Tangible fixed assets and depreciation**

Tangible fixed assets comprise:

#### (i) **Infrastructure assets**

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

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

The depreciation charge for infrastructure assets is based on the company's independently certified asset management plan which has estimated the level of expenditure required over the next five years to maintain the operating capability of the network.

#### (ii) **Non-Infrastructure assets**

Other assets (including properties, overground plant and equipment) are included at cost less accumulated depreciation and provision for impairment. Additions are included at cost.

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

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

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

Assets in the course of construction are not depreciated until commissioned.

### (f) **Government grants and contributions**

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

Capital grants and contributions relating to other assets are treated as deferred income and amortised in the profit and loss account over the expected useful economic lives of the qualifying assets. Specifically in the case of infrastructure assets the expected useful economic lives have been determined by reference to the physical replacement cycle of these assets.

### (g) **Hire purchase and leasing**

Where assets are financed by hire purchase or leasing arrangements which transfer substantially all the risks and rewards of ownership to the company, the assets are treated as if they had been purchased and the corresponding capital cost is treated as a liability. Rentals or leasing payments are treated as consisting of a capital element and finance costs, the capital element reducing the outstanding liability and the finance costs being charged to the profit and loss account over the period of the hire purchase contract or lease in proportion to the reducing outstanding liability.

Rental costs arising under operating leases are charged to the profit and loss account in the period in which they are incurred.

## 1. STATEMENT OF ACCOUNTING POLICIES (continued)

### (h) Stocks

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

### (i) Pension costs

The cost of providing pension benefits is charged to the profit and loss account so as to spread the cost over the expected average service lives of employees. Differences between the amounts funded and amounts charged to the profit and loss account are treated as prepayments or accruals in the balance sheet.

### (j) Taxation

The charge for current taxation is based on the profit for the year as adjusted for taxation purposes. 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 in the foreseeable future. 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) 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. Exchange gains or losses are recognised in the profit and loss account in the period incurred.

### (l) Research and development

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

### (m) Investments

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

### (n) Derivative Financial Instruments

The company utilises interest rate swaps, forward rate agreements and forward exchange contracts as derivative financial instruments.

A derivative instrument is considered to be used for hedging purposes when it alters the risk profile of an underlying exposure of the company in line with the company's risk management policies.

Interest rate swap agreements are used to manage interest rate exposures. Amounts payable or receivable in respect of these derivatives are recognised over the period of the contracts as adjustments to net interest payable in the profit and loss account.

Forward exchange contracts are valued at the year end rates of exchange. Resultant gains and losses are offset against foreign exchange gains or losses on the related borrowings or, where the instrument is used to hedge a committed future transaction, are deferred until the transaction occurs.

## 2. PRIOR YEAR ADJUSTMENT

As set out in note 1(b), the Group has changed its accounting policies for the treatment of infrastructure renewals and grants and contributions relating to infrastructure assets. As a result of these changes, the comparatives have been restated as follows:

### a) Group profit and loss account

	Operating Costs	Retained Profit
	£'m	£'m
Year ended 31 December 1998 as originally reported	126.4	57.2
Prior year adjustment	(0.7)	0.7
Year ended 31 December 1998 as restated	<u>125.7</u>	<u>57.9</u>

### b) Group balance sheet

	Tangible fixed assets	Provisions for liabilities and charges	Accruals and deferred income	Profit and loss reserve
	£'m	£'m	£'m	£'m
Year ended 31 December 1998 as originally reported	1,508.3	(13.6)	(30.0)	781.9
Prior year adjustment	54.1	1.4	(50.6)	4.9
Year ended 31 December 1998 as restated	<u>1,562.4</u>	<u>(12.2)</u>	<u>(80.6)</u>	<u>786.8</u>

### c) Group cash flow statement

	Cash inflow from operating activities	Capital expenditure and financial investment
	£'m	£'m
Year ended 31 December 1998 as originally reported	195.5	165.8
Prior year adjustment	15.9	15.9
Year ended 31 December 1998 as restated	<u>211.4</u>	<u>181.7</u>

### 3. TURNOVER

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

### 4. OPERATING COSTS, CAPITAL MAINTENANCE AND EXCEPTIONAL COSTS

(a) Operating costs comprise:

	December 1999	December 1998 (as restated)
	£'m	£'m
Materials and consumables	9.6	10.1
Other external charges	16.2	15.5
Manpower costs (note 8)	41.1	42.7
Other operating charges	69.6	67.9
Own work capitalised	(10.9)	(10.5)
	<u>125.6</u>	<u>125.7</u>

(b) Capital maintenance costs comprise:

	December 1999	December 1998 (as restated)
	£'m	£'m
Depreciation:		
Non-Infrastructure assets	30.0	27.4
Non-Infrastructure assets held under finance leases	4.9	2.8
Infrastructure assets	20.8	20.2
Profit on disposal of fixed assets	(1.3)	(0.6)
	<u>54.4</u>	<u>49.8</u>

(c) Exceptional operating costs comprise:

	December 1999	December 1998
	£'m	£'m
Reorganisation/restructuring costs	<u>8.5</u>	<u>2.4</u>

The reorganisation/restructuring costs represent exceptional costs resulting from a new severance scheme which was introduced during 1999.

**4. OPERATING COSTS, CAPITAL MAINTENANCE  
AND EXCEPTIONAL COSTS (continued)**

(d) Profit on ordinary activities before taxation

	December 1999	December 1998 (as restated)
	£'m	£'m
Profit on ordinary activities before taxation is stated after crediting:		
Amortisation of capital grants (note 23)	2.4	2.3
And after charging:		
Operating leases: Plant and machinery	0.8	1.0
Other assets	0.2	0.2
Costs of research and development	4.7	4.5
Directors' emoluments (note 6)	0.5	0.5
Non-audit services provided by the auditors and their associates	-	-

Auditors' remuneration for the audit amounted to £47,750 (December 1998: £45,000).

**5. NET INTEREST**

	December 1999	December 1998
	£'m	£'m
Net interest payable comprises:		
Interest payable:		
Bank loans and overdrafts	38.9	39.6
Debenture stock interest	0.9	0.9
Financing charges payable under finance leases	2.8	2.7
Total interest payable	42.6	43.2
Interest receivable	(8.5)	(9.5)
Net interest payable	34.1	33.7

## 6. DIRECTORS' EMOLUMENTS AND INTERESTS

### Directors' remuneration

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

	<u>December 1999</u>	<u>December 1998</u>
	£'000	£'000
Emoluments (including benefits in kind)	<u>476.8</u>	<u>522.5</u>

### Highest paid director

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

	<u>December 1999</u>	<u>December 1998</u>
	£'000	£'000
Emoluments (including benefits in kind)	<u>169.7</u>	<u>161.5</u>

The accrued pension entitlement under the company's defined benefit scheme of the highest paid director at 31 December 1999 was £49,029 (31 December 1998: £43,470). In addition to the pension, there is a tax free lump sum at normal pension date of which the accrued entitlement at 31 December 1999 was £131,970 (31 December 1998: £119,925).

The directors who held office at 31 December 1999 had no interest in the shares of the company.

The directors who held office at 31 December 1999 had the following beneficial interests in the ordinary shares, other than share options, and debentures of the Company's ultimate parent company, Suez Lyonnaise des Eaux.

Name of Director	Description of Shares or debentures	31 December 1999	1 January 1999 or subsequent date of appointment
H D M Speed	Ordinary Shares of €10	11	251
P Babin	Ordinary Shares of €10	522	336
J A Cuthbert	Ordinary Shares of €10	361	63
J Graham	Ordinary Shares of €10	270	63
A J Harding	Ordinary Shares of €10	468	11
G Neave	Ordinary Shares of €10	213	-
S M Straw	Ordinary Shares of €10	223	32

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

The directors who held office on 31 December 1999 held the following options over ordinary shares of €10 each in Suez Lyonnaise des Eaux:

Name of Director	1 January 1999 or subsequent date of appointment	Granted during the year	31 December 1999	Exercise Price
H D M Speed	1400	-	1400	573 FF
P Babin	3500	-	3500	573 FF
	4000	-	4000	978 FF
	-	4500	4500	€151.11
J A Cuthbert	1200	-	1200	456 FF
	2200	-	2200	573 FF
	2300	-	2300	978 FF
	-	2500	2500	€151.11
J Graham	300	-	300	573 FF
	400	-	400	978 FF
A J Harding	2500	-	2500	573FF
	2600	-	2600	978FF
	-	2800	2800	€151.11
G Neave	500	-	500	573FF
	800	-	800	978FF
	-	800	800	€151.11
S M Straw	200	-	200	573FF
	300	-	300	978FF

No options have been lapsed during the year.

All options with an exercise price of 456FF were granted on 24 July 1996 and are exercisable between 24 July 1998 and 24 July 2004.

All options with an exercise price of 573FF were granted on 17 November 1997 and are exercisable between 17 November 2002 and 17 November 2005.

All options with an exercise price of 978 FF were granted on 16 November 1998 and are exercisable between 16 November 2003 and 16 November 2006.

All options with an exercise price of €151.11 were granted on 15 November 1999 and are exercisable between 15 November 2004 and 15 November 2007.

The highest and lowest prices of the Suez Lyonnaise des Eaux shares during the year were €193.9 and €146.0 respectively.

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

## 7. TRANSACTIONS WITH DIRECTORS AND OFFICERS

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

## 8. EMPLOYEE INFORMATION

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

	<u>December 1999</u>	<u>December 1998</u>
	£'m	£'m
Costs charged to the profit and loss account:		
Wages and salaries	26.7	28.5
Social security costs	2.3	2.5
Other pension costs	2.9	3.2
	<u>31.9</u>	<u>34.2</u>
Costs charged to capital schemes and infrastructure renewals:		
Wages and salaries	7.7	7.1
Social security costs	0.6	0.6
Other pension costs	0.9	0.8
	<u>9.2</u>	<u>8.5</u>

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

	<u>December 1999</u>	<u>December 1998</u>
	Number	Number
Average during the year	<u>1,585</u>	<u>1,768</u>
Total at 31 December	<u>1,469</u>	<u>1,699</u>

## 9. TAXATION

	<u>December 1999</u>	<u>December 1998</u>
	£'m	£'m
Tax on profit on ordinary activities		
United Kingdom corporation tax at 30.25% (December 1998:31%)		
- current year	17.7	16.2
- prior years	-	1.8
Payable in respect of group relief		
- current year	13.7	10.6
- prior years	-	0.9
Payable in respect of advance corporation tax surrendered	-	1.1
	<u>31.4</u>	<u>30.6</u>
Tax charge	<u>31.4</u>	<u>30.6</u>

- (a) The company has provisionally claimed tax losses from fellow subsidiaries in the current year of £45.4m (December 1998: £34.1m) for which payment will be made at the rate of 30.25%. The company has provisionally claimed advance corporation tax of £Nil (December 1998: £1.1m) from Northumbrian Water Group plc for which payment shall be made at full value.
- (b) No deferred taxation has been provided in the financial statements since timing differences at 31 December 1999 are not expected to reverse in the foreseeable future (December 1998: £Nil). The effect of not providing for deferred taxation has been a reduction in the tax charge for the year of £17.6m (December 1998: £20.6m). The full potential amount of deferred taxation calculated at 30% (December 1998: 31%) on all timing differences is as follows:

	<u>December 1999</u>	<u>December 1998</u>
	£'m	£'m
Accelerated capital allowances	283.3	259.9
Other timing differences	(19.1)	(15.0)
	<u>264.2</u>	<u>244.9</u>

The increase in the full potential amount of deferred taxation of £19.3m includes £17.6m in respect of current year items and £1.7m in respect of the prior year adjustment.

Following the adoption of Financial Reporting Standard 12 'Provisions, Contingent Liabilities and Contingent Assets', the method of accounting for infrastructure assets has changed (note 2). The above amounts already include the tax effect of timing differences on infrastructure assets and have been restated to include the tax effect (£0.4m) of the infrastructure maintenance provision within accelerated capital allowances rather than other timing differences.

## 10. DIVIDENDS

	<u>December 1999</u>	<u>December 1998</u>
	£'m	£'m
Equity:		
Interim paid of 26.25p (December 1998: 25.031p) per share on an aggregated basis	32.2	30.7
Final proposed of 26.25p (December 1998: 25.031p) per share on an aggregated basis	32.2	30.7
	<u>64.4</u>	<u>61.4</u>

The Directors have a policy which, unless circumstances dictate otherwise, aims to grow dividends on a slow but regular basis and which takes into account the principle of incentive based price cap regulation, including operating and investment performance. The company has maintained its policy of a steady 2% real growth per annum for the Appointed business dividend. Dividends from the Non-Appointed business are determined by the Directors and are based on performance.

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

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

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

## 11. TANGIBLE FIXED ASSETS – GROUP AND COMPANY

	Freehold land and buildings	Infra- structure assets	Operational structures, plant and machinery	Fixtures, fittings, tools and equipment	Assets in the course of construction	Total
	£'m	£'m	£'m	£'m	£'m	£'m
Cost:						
At 1 January 1999 as originally stated	52.9	741.2	626.0	55.2	243.9	1,719.2
Prior year adjustment (note 2)	-	158.4	-	-	-	158.4
At 1 January 1999 restated	52.9	899.6	626.0	55.2	243.9	1,877.6
Additions	-	-	-	-	213.1	213.1
Schemes commissioned	2.5	49.8	97.2	5.0	(154.5)	-
Disposals	-	(12.3)	(0.1)	-	-	(12.4)
At 31 December 1999	55.4	937.1	723.1	60.2	302.5	2,078.3
Depreciation:						
At 1 January 1999 as originally stated	13.4	-	158.5	39.0	-	210.9
Prior year adjustment (note 2)	-	104.3	-	-	-	104.3
At 1 January 1999 restated	13.4	104.3	158.5	39.0	-	315.2
Provision for year	2.3	20.8	26.6	6.0	-	55.7
Disposals	-	(12.3)	-	-	-	(12.3)
At 31 December 1999	15.7	112.8	185.1	45.0	-	358.6
Net book value:						
At 31 December 1999	39.7	824.3	538.0	15.2	302.5	1,719.7
At 31 December 1998 (restated)	39.5	795.3	467.5	16.2	243.9	1,562.4
Leased assets included above:						
Net book value						
At 31 December 1999	-	-	31.1	4.0	-	35.1
At 31 December 1998	-	-	28.3	0.2	-	28.5

Following the introduction of FRS 12 and FRS 15 (as stated in note 1(b) infrastructure assets are now depreciated and the figures for prior years have been restated accordingly.

## 12. FIXED ASSET INVESTMENTS – COMPANY

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

## 13. STOCKS – GROUP AND COMPANY

	December 1999	December 1998
	£'m	£'m
Raw materials and consumables	1.9	2.8

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

## 14. DEBTORS – GROUP AND COMPANY

	December 1999	December 1998
	£'m	£'m
<b>(a) Amounts falling due within one year:</b>		
Trade debtors	34.7	40.8
Amounts owed by other group companies	3.6	3.9
Other debtors	4.0	3.6
Prepayments and accrued income	28.4	20.3
	<u>70.7</u>	<u>68.6</u>
<b>(b) Amounts falling due after more than one year:</b>		
Amounts owed by other group companies	11.7	14.2

Included in amounts owed by other group companies are loans of £14.2m repayable by instalments of which £10.2m (December 1998: £11.6m) falls due in less than five years and £4m (December 1998: £5.0m) falls due after more than five years.

## 15. INVESTMENTS – GROUP AND COMPANY

	<u>December 1999</u>	<u>December 1998</u>
	£'m	£'m
Short term deposits	75.0	103.2

## 16. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR – GROUP AND COMPANY

	<u>December 1999</u>	<u>December 1998</u>
	£'m	£'m
Obligations under finance leases (note 20)	3.7	1.0
Bank overdraft	-	3.3
Loans (note 18)	10.1	26.7
Trade creditors	1.8	1.8
Amounts owed to other group companies	30.5	32.8
Taxation and social security	0.9	0.9
Corporation Tax	18.5	18.5
Other creditors	11.8	11.0
Receipts in Advance	35.9	35.4
Dividend payable	32.2	30.7
Accruals and deferred income	51.5	45.1
	<u>196.9</u>	<u>207.2</u>

The analysis of creditors has been revised to include greater detail and the prior year numbers have been restated to reflect this.

Accruals and deferred income includes accruals related to capital projects of £33.2m (December 1998: £29.5m). Amounts owed to other group companies includes amounts related to capital projects of £2.2m (December 1998: £5.0m).

Included in amounts owed to other group companies is £9.7m (December 1998: £10.7m) payable in respect of tax losses surrendered from fellow Group companies; and £0.1m (December 1998: £1.2m) payable in respect of advance corporation tax surrendered from Northumbrian Water Group plc. Also included in amounts owed to other group companies is £0.3m (December 1998: £Nil) relating to loans repayable within one year (note 21).

**17. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR – GROUP AND COMPANY**

	December 1999		December 1998	
	Group	Company	Group	Company
	£'m	£'m	£'m	£'m
Obligations under hire purchase contracts and finance leases (note 20)	52.7	52.7	46.1	46.1
Loans (note 18)	227.5	227.5	162.6	162.6
Debenture stocks (note 19)	8.7	8.7	8.7	8.7
Amounts owed to other group companies (note 21)	323.8	371.0	323.9	371.1
Other creditors	-	-	0.4	0.4
	<u>612.7</u>	<u>659.9</u>	<u>541.7</u>	<u>588.9</u>

At 31 December 1999 the group and company had entered into the following interest swap arrangements: £15.0m (December 1998: £15.0m) over a ten year period commencing on 10 May 1994 under which the group and company is required to pay interest at a rate linked to LIBOR and will receive interest at 9.00%, and £10.0m (December 1998: £10.0m) over a seven year period commencing on 16 December 1996 under which the group and company is required to pay interest at a rate linked to LIBOR and will receive interest at 7.45%.

**18. LOANS – GROUP AND COMPANY**

	December 1999	December 1998
	£'m	£'m
Loans are repayable as follows:		
Within one year	10.1	26.7
Between one and two years	11.1	10.1
Between two and five years	65.7	45.6
After five years	150.7	106.9
	<u>237.6</u>	<u>189.3</u>

Loans repayable by instalments wholly repayable within 5 years amount to £10.5m (December 1998: £13.7m). Loans repayable by instalments not wholly repayable within 5 years amount to £137.1m (December 1998: £143.6m) and bear interest rates in the range of 7.2% to 11.1% of which £61.4m (December 1998: £51.7m) falls due in less than 5 years and £75.7m (December 1998: £91.9m) falls due after more than 5 years.

Loans repayable otherwise than by instalments which fall due in less than 5 years amount to £Nil (December 1998: £17.0m).

Loans repayable otherwise than by instalments which fall due after more than 5 years amount to £90.0m (December 1998: £15.0m) and bear interest at rates in the range of 5.9% and 7.95%.

## **18. LOANS – GROUP AND COMPANY (continued)**

The level of capital expenditure which the company is obliged to incur is such that it cannot be wholly financed by internally generated sources. As a result, the company must rely upon raising additional finance on a regular basis to fund the long term assets required in its business. The company's strategy is to finance such investment by raising medium to long term debt, to provide a balance sheet match with long term assets and to fix a major proportion of interest rates.

### **Treasury operations**

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

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

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

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

#### **Liquidity risk**

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

#### **Interest rate risk**

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

#### **Foreign currency risk**

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

## 18. LOANS – GROUP AND COMPANY (continued)

### Interest rate risk profile of financial assets and financial liabilities

The interest rates and currency profile of the net borrowings of the Group and the Company at 31 December 1999 were:

#### Group

	Total net borrowings	Variable rate net borrowings	Fixed Rate Net Borrowings			Financial liabilities on which no interest is paid	
			Fixed Rate Borrowings	Weighted average interest rate	Weighted average period until maturity		
			£'m	%	Years		
	£'m	£'m	£'m	%	Years	Years	£'m
<b>Sterling borrowings:</b>							
External loans	(237.6)	(79.2)	(158.4)	7.72	8.9	8.9	-
Debentures	(8.7)	-	(8.7)	10.58	6.5	6.5	-
Internal loans	(324.1)	(119.5)	(204.6)	7.07	22.6	22.6	-
Finance leases	(56.4)	(47.9)	(8.5)	9.82	1.6	1.6	-
Bank Overdraft	-	-	-	-	-	-	-
<b>Total Borrowings</b>	<b>(626.8)</b>	<b>(246.6)</b>	<b>(380.2)</b>	<b>7.48</b>	<b>16.0</b>	<b>16.0</b>	<b>-</b>
Cash	3.7	3.7	-	-	-	-	-
Short Term Investments	75.0	-	75.0	5.88	0.1	0.1	-
<b>Net borrowings</b>	<b>(548.1)</b>	<b>(242.9)</b>	<b>(305.2)</b>				<b>-</b>

#### Company

	Total net borrowings	Variable rate net borrowings	Fixed Rate Net Borrowings			Financial liabilities on which no interest is paid	
			Fixed Rate Borrowings	Weighted average interest rate	Weighted average period until maturity		
			£'m	%	Years		
	£'m	£'m	£'m	%	Years	Years	£'m
<b>Sterling borrowings:</b>							
External loans	(237.6)	(79.2)	(158.4)	7.72	8.9	8.9	-
Debentures	(8.7)	-	(8.7)	10.58	6.5	6.5	-
Internal loans	(371.3)	(119.5)	(204.6)	7.07	22.6	22.6	(47.2)
Finance leases	(56.4)	(47.9)	(8.5)	9.82	1.6	1.6	-
Bank Overdraft	-	-	-	-	-	-	-
<b>Total Borrowings</b>	<b>(674.0)</b>	<b>(246.6)</b>	<b>(380.2)</b>	<b>7.48</b>	<b>16.0</b>	<b>16.0</b>	<b>(47.2)</b>
Cash	3.7	3.7	-	-	-	-	-
Short Term Investments	75.0	-	75.0	5.88	0.1	0.1	-
<b>Net borrowings</b>	<b>(595.3)</b>	<b>(242.9)</b>	<b>(305.2)</b>				<b>(47.2)</b>

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

## 18. LOANS – GROUP AND COMPANY (continued)

Included within the external sterling loans of the group and the company above are loans amounting to £90m whose rates are fixed for a period of 5 to 7 years from their inception and which, under the terms of the respective loan agreements, can then either be repaid or rolled over for a similar period at a new fixed rate based upon prevailing market rates at that date. The weighted average period for which the rates on such loans are fixed has been taken as the same average period until maturity.

### Currency exposures

At 31 December 1999, the group and the company had no currency exposures.

### Borrowing facilities

The group and the company had no undrawn committed borrowing facilities as at 31 December 1999 but had access to undrawn committed borrowing facilities available to Northumbrian Water Group plc which, at 31 December 1999, amounted to £100m.

The facilities available to Northumbrian Water Group plc at 31 December 1999, in respect of which all conditions precedent have been met expiring in one year or less, is £100m.

### Fair values of financial assets and financial liabilities

Set out below is a comparison by category of book values and fair values of the financial assets and liabilities of the group and the company as at 31 December 1999:

#### Group

	<u>Book value</u>	<u>Fair value</u>
	£'m	£'m
Primary financial instruments held or issued to finance the group's operations:		
Short -term financial liabilities and current portion of long-term borrowings	(14.1)	(15.4)
Long-term borrowings	(612.7)	(629.0)
Financial assets	78.7	78.7
Derivative financial instruments held to manage the interest rate and currency profile:		
Interest rate swaps	-	2.2
As at 31 December 1999	<u>(548.1)</u>	<u>(563.5)</u>

## 18. LOANS – GROUP AND COMPANY (continued)

### Company

	Book value	Fair value
	£'m	£'m
Primary financial instruments held or issued to finance the company's operations:		
Short-term financial liabilities and current portion of long-term borrowings	(14.1)	(15.4)
Long-term borrowings	(659.9)	(676.2)
Financial assets	78.7	78.7
Derivative financial instruments held to manage the interest rate and currency profile:		
Interest rate swaps	-	2.2
As at 31 December 1999	<u>(595.3)</u>	<u>(610.7)</u>

For the group and company, the fair values of the interest rate swaps, and sterling denominated long-term fixed rate debt with a book value of £203.3m, have been determined by reference to prices available from the markets on which the instruments involved are traded. All the other fair values shown above have been calculated by discounting cash flows at prevailing interest rates.

### Gains and losses on hedges

The company's board uses the Northumbrian Water Group plc treasury function to enter into any necessary forward foreign currency contracts on the company's behalf to eliminate the currency exposures that arise on sales denominated in foreign currencies immediately those sales are transacted. The company also uses interest rate swaps to manage its interest rate profile. Changes in the fair value of instruments used as hedges are not recognised in the financial statements until the hedged position matures. An analysis of these unrecognised gains and losses is as follows:

### Group and Company

	Gains	Losses	Total net Gains/Losses
	£'m	£'m	£'m
Unrecognised gains and losses on hedges at 1 January 1999	3.9	(0.4)	3.5
Gains and losses arising in previous years that were recognised in 1999	(0.8)	0.4	(0.4)
Gains and losses arising before 1 January 1999 that were not recognised in 1999	3.1	-	3.1
Gains and losses arising in 1999 that were not recognised in 1999	(0.9)	-	(0.9)
Unrecognised gains and losses on hedges at 31 December 1999	<u>2.2</u>	<u>-</u>	<u>2.2</u>
Of which:			
Gains and losses expected to be recognised in 2000	0.8	-	0.8
Gains and losses expected to be recognised in 2001 or later	1.4	-	1.4
	<u>2.2</u>	<u>-</u>	<u>2.2</u>

## 18. LOANS – GROUP AND COMPANY (continued)

### Market price risk

The company's exposure to market price risk principally comprises interest rate exposure.

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

## 19. DEBENTURE STOCKS – GROUP AND COMPANY

	<u>December 1999</u>	<u>December 1998</u>
	£'m	£'m
Debenture stocks are repayable as follows:		
In five years or more:		
£1, 12.0% Redeemable 2004	5.0	5.0
£1, 12.0% Redeemable 2005	2.0	2.0
£1, 3.75% Redeemable 2012	0.3	0.3
£1, 4.25% Redeemable 2012	0.7	0.7
£1, 5.25% Redeemable 2012	0.7	0.7
	<u>8.7</u>	<u>8.7</u>

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

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

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

	<u>December 1999</u>	<u>December 1998</u>
	£'m	£'m
Amounts due:		
Within one year	3.7	1.0
Between one and two years	4.6	1.5
Between two and five years	7.2	4.6
After five years	80.6	82.6
	<u>96.1</u>	<u>89.7</u>
Less:		
Finance charge allocated to future periods	(39.7)	(42.6)
	<u>56.4</u>	<u>47.1</u>
Disclosed as due:		
Within one year (note 16)	3.7	1.0
After more than one year (note 17)	52.7	46.1
	<u>56.4</u>	<u>47.1</u>

## 21. AMOUNTS DUE TO OTHER GROUP COMPANIES

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

	December 1999		December 1998	
	Group	Company	Group	Company
	£'m	£'m	£'m	£'m
Within one year	0.3	0.3	-	-
Between one and two years	0.7	0.7	0.3	0.3
Between two and five years	2.5	2.5	1.9	1.9
After five years	320.6	367.8	321.7	368.9
	<u>324.1</u>	<u>371.3</u>	<u>323.9</u>	<u>371.1</u>

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

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

By way of a novation agreement dated 5 August 1996, Northumbrian Water Limited took over the obligations of Lyonnaise Europe plc in respect of a £33m loan agreement from the European Investment Bank to Lyonnaise Europe plc, dated July 1990 and known as Lyonnaise Water UK I Project (UK I). Lyonnaise Europe plc had subsequently on-lent the £33m to its subsidiaries, North East Water plc, £13m, and Essex and Suffolk Water plc, £20m, with the agreement of European Investment Bank. By way of an on-lending agreement dated 30 August 1996, Essex and Suffolk Water plc agreed to indemnify Northumbrian Water Limited for the principal and interest due on the £20m borrowed by Essex and Suffolk Water plc in respect of UK I agreement.

By way of a novation agreement dated 5 August 1996, Essex and Suffolk Water plc took over the obligations of Lyonnaise Europe plc in respect of a £65m loan agreement from the European Investment Bank to Lyonnaise Europe plc dated 7 July 1995 and known as Lyonnaise Water UK II Project (UK II). Lyonnaise Europe plc had subsequently on-lent £25m of the loan facility to its subsidiaries, North East Water plc, £10m and Essex and Suffolk Water plc, £15m, with the agreement of European Investment Bank. By way of an on-lending agreement dated 30 August 1996, Northumbrian Water Limited agreed to indemnify Essex and Suffolk Water plc for the principal and interest due on the £10m borrowed by Northumbrian Water Limited in respect of the UK II agreement. On 3 October and 18 November 1996, Essex and Suffolk Water plc drew down from the European Investment Bank the outstanding £40m available under the UK II facility.

The £10m borrowed by Northumbrian Water Limited in respect of the UK II agreement is repayable by instalments, £3.5m falls due in less than five years and £6.5m falls due after more than 5 years. The loan bears interest at 8.55%.

£194.6m is owed to the immediate parent company, Northumbrian Water Group plc. Northumbrian Water Group plc issued £200m Guaranteed Eurobonds maturing 6 February 2023, with an annual coupon of 6.875%. The issue was guaranteed by the company who received issue proceeds by way of an inter-company loan of £194.2m. Finance costs allocated during the year amounted to £0.2m (December 1998: £0.2m).

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

	Reorganisation and Restructuring Provision	Infrastructure Renewals Expenditure	Total
	£'m		£'m
At 1 January 1999 as originally stated	12.2	1.4	13.6
Prior year adjustment (note 2)	-	(1.4)	(1.4)
At 1 January 1999 as restated	12.2	-	12.2
Transferred from profit and loss account	8.5	-	8.5
Utilised during the year	(2.9)	-	(2.9)
At 31 December 1999	17.8	-	17.8

The provision remaining at the end of the year incorporates outstanding pension contributions for staff who left the business on early retirement terms as part of voluntary severance schemes in 1996 and 1998 and outstanding severance and pension payments relating to the additional provision made in the year. The redundancy component of the provision will be paid within twelve months of the balance sheet date, and the pension augmentation component will be paid or amortised following the recommendations of the actuaries of the pension schemes in which the individuals concerned belong.

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

	December 1999
	£'m
Capital grants and contributions:	
At 1 January as originally stated	30.0
Prior year adjustment (note 2)	50.6
At 1 January as restated	80.6
Additions	6.5
Amortised during the year	(2.4)
At 31 December	84.7

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

	December 1999	December 1998
	£'m	£'m
Authorised:		
122,650,000 Ordinary Shares of £1 each (December 1998: 122,650,000)	122.7	122.7
	December 1999	December 1998
	£'m	£'m
Allotted, called-up and fully paid:		
122,650,000 Ordinary Shares of £1 each (December 1998: 122,650,000)	122.7	122.7

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

	December 1999	December 1998
	£'m	£'m
At 1 January	781.9	724.7
Prior year adjustment (note 2)	4.9	4.2
At 1 January as restated	786.8	728.9
Profit retained for the year	61.1	57.9
At 31 December	847.9	786.8

As permitted by Section 230 of the Companies Act 1985, the company's profit and loss account has not been included in these financial statements. A profit after tax and before dividends of £125.5m (December 1998: £119.3m as restated) relates to the operations of the company.

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

	December 1999	December 1998 (as restated)
	£'m	£'m
Profit for the financial year	125.5	119.3
Dividends	(64.4)	(61.4)
Net additions to equity shareholders' funds	61.1	57.9
Opening equity shareholders' funds	904.6	847.4
Prior year adjustment (note 2)	4.9	4.2
Closing equity shareholders' funds (as restated)	970.6	909.5

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

(a) Capital expenditure	December 1999	December 1998
	<u>£'m</u>	<u>£'m</u>
Expenditure contracted for	<u>105.6</u>	<u>54.1</u>

(b) Lease commitments:

The company and group has entered into non-cancellable operating leases in respect of land and buildings, plant, machinery and motor vehicles. The total amount payable under these leases in the next year is as follows:-

	<u>December 1999</u>	<u>December 1998</u>
	£'m	£'m
Land and buildings:		
Leases which expire:		
In five years or more	<u>0.3</u>	<u>0.2</u>
	<u>0.3</u>	<u>0.2</u>
Other:		
Leases which expire:		
Within one year	0.3	0.4
Between two and five years	0.5	0.8
	<u>0.8</u>	<u>1.2</u>

**28. PENSIONS**

As a subsidiary of Northumbrian Water Group plc, the company participates in group pension schemes.

The Group operates a funded defined benefit pension scheme providing benefits based on final pensionable remuneration. The Scheme, named the Northumbrian Lyonnaise Pension Scheme, comprises three sections reflecting the transfer from the Water Pension Scheme in 1998 and an existing separation between different businesses within the Group.

The assets of the Scheme are held separately from those of the Group in independently administered funds.

## 28. PENSIONS (continued)

Details of the Scheme and its latest actuarial valuation, carried out as at 31 December 1998 are shown below.

Section	South	North	WPS
Members' contributions	5%	5%	6%
Employer's contributions	Nil	6.3%	17.2%

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

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

The market value of assets for the whole Scheme as at 31 December 1998 was £416.2m. The 1998 valuation disclosed that the value of the assets of the whole Scheme represented 114% of the value of the accrued liabilities of the whole Scheme.

The company also participates in the Water Mirror Image Pension Scheme and the Employer's contribution has been assessed and paid in accordance with the advice of an independent actuary. This Scheme provides a defined benefit pension arrangement for 65 employees. The last actuarial valuation was carried out at 31 March 1996.

The Northumbrian Water Group Personal Pension Plan provides defined contribution benefits to 630 employees.

## 29. RELATED PARTY DISCLOSURES

The company is a wholly owned subsidiary of Northumbrian Water Group plc which produces publicly available financial statements which includes the company. Consequently the company is exempt under the terms of Financial Reporting Standard No 8 "Related Party Disclosures" from disclosing transactions with other members of the group headed by Northumbrian Water Group plc.

Transactions with other members of the group headed by Suez Lyonnaise des Eaux outside of the Northumbrian Water Group, comprised purchases of £16.8m (31 December 1998: £6.7m) and sales of £1.1m (31 December 1998: £0.5m). As at 31 December 1999, the amount due to these companies was £2.1m (31 December 1998: £0.9m) and due from these companies was £0.2m (31 December 1998: £0.2m).

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

Degremont  
Lyonnaise des Eaux Khatib and Alami  
Sita Holding UK Limited  
Suez Lyonnaise des Eaux

### **30. POST BALANCE SHEET EVENTS**

The Director General has approved the merger of Northumbrian Water Limited and Essex and Suffolk plc. They will operate under a single licence from 1 April 2000 as Northumbrian Water Limited but will continue to use their existing names for trading purposes.

### **31. ULTIMATE PARENT COMPANY**

The ultimate parent company and controlling party of the company is Suez Lyonnaise des Eaux, incorporated in France. The largest group which consolidates the results of the company is Suez Lyonnaise des Eaux and copies of the consolidated accounts are available to the public from Suez Lyonnaise des Eaux, 1 Rue d'Astorg, 75008, Paris, France.

The smallest group which consolidates the results of the company is that of which Northumbrian Water Group plc is the parent. Copies of the consolidated accounts may be obtained from Northumbrian Water Group plc, Northumbria House, Regent Centre, Gosforth, Newcastle upon Tyne NE3 3PX. Northumbrian Water Group plc is registered in England and Wales.