

FINANCIAL STATEMENTS
NORTHUMBRIAN WATER LIMITED
FOR THE YEAR ENDED 31 DECEMBER 2000

Registered no: 2366703



Registered office
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Gosforth
Newcastle Upon Tyne
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**FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2000**

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DIRECTORS' REPORT

For the year ended 31 December 2000

The directors present their report and the audited financial statements for the year ended 31 December 2000.

Results and dividends

The group's profit after taxation for the year ended 31 December 2000 amounts to £109.8m (December 1999: £125.5m). The directors propose a final dividend on the ordinary shares of the company of £40.2m (December 1999: £32.2m) which, together with the interim dividend of £36.8m (December 1999: £32.2m), makes a total for the year of £77.0m (December 1999 £64.4m). As explained below under the review of the business, the results for the year include the results relating to the Essex and Suffolk region from 1 April 2000 to 31 December 2000.

Principal activities and review of the business

On 1 April 2000 the trade, employees, assets and liabilities of Essex and Suffolk Water plc were transferred to Northumbrian Water Limited for a consideration of £176.0m. Following agreement with Ofwat, with effect from 1 April 2000, Northumbrian Water Limited's Appointment as a water undertaking has been varied to apply also to Essex and Suffolk Water plc's area of Appointment, and the Appointment of Essex and Suffolk Water plc has been terminated.

The principal activities of the business comprise the supply of potable water in both the Northern and Southern regions, and the collection, treatment and disposal of sewage and sewage sludge throughout the North East of England. Turnover relating to the existing operations has been reduced by the impact of the price reduction of 19.4%, offset by inflation, which was required by Ofwat from April 2000.

The company achieved the best performance in the water industry against the Ofwat customer service measures for the regulatory year ending 31 March 2000. In addition, the investment programme delivered the required obligations by 31 December 2000 and operating efficiencies were achieved as a result of further restructuring and the merger with Essex and Suffolk Water plc. The operating costs show a significant increase on the prior year due to the inclusion of costs relating to the Essex and Suffolk region for 9 months. If the comparative figure is adjusted to include the equivalent operating costs for Essex and Suffolk, the operating cost base would show an absolute reduction of approximately 5%.

The future focus of the company continues to be 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 company has secured a number of significant contracts during the year with major industrial customers to provide advice on how they can optimise their water usage. The directors believe that this demonstrates that the company has developed a competitive edge in the market place.

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 2001 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 £5.3m (December 1999: £4.7m).

DIRECTORS' REPORT (continued)

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. During the year Northumbrian Water and Essex and Suffolk Water continued to operate separate creditors ledgers. For Northumbrian Water, the year end trade creditors expressed as a number of days of purchases made during the year is 27 days (December 1999: 29 days). This has been calculated by dividing the year end trade creditors balance of £1.9m by the aggregate of the average daily amounts invoiced by suppliers during the year. For Essex and Suffolk Water, the year end trade creditors expressed as a number of days of purchases made during the year is 20 days (December 1999: 24 days). This has been calculated by dividing the year end trade creditors balance of £1.3m 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 £57.3m (December 1999: £39.7m). In the opinion of the directors, at 31 December 2000, there is no significant difference between the net book value and market value of property capable of disposal within the foreseeable future.

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.

DIRECTORS' REPORT (continued)

Directors

The directors who served during the year were as follows:

P Babin	
J A Cuthbert	
A J Harding (Managing Director)	
L M Caple	(resigned 31 March 2000)
J Graham	(resigned 31 March 2000)
G Neave	(resigned 31 March 2000)
H D M Speed	(resigned 31 March 2000)
S M Straw	(resigned 31 March 2000)
Dr D A Trebilco	(resigned 31 March 2000)
Sir F G T Holliday (Chairman)	(appointed 1 April 2000)
Sir J D R Bradbeer	(appointed 1 April 2000)
A Chaigneau	(appointed 1 April 2000)
J A Haynes	(appointed 1 April 2000)
M A B Nègre	(appointed 1 April 2000)
R R Allan	(appointed 1 April 2000)
C M Green	(appointed 1 April 2000)

Non executive directors were as follows:

P Babin (43)
HEC MBA
Executive Vice President, Europe and Asia, Water Division, Suez Lyonnaise des Eaux.

Sir J D R Bradbeer (69)
OBE TD
Deputy Chairman
Consultant, Eversheds, Solicitors, Newcastle Upon Tyne

A Chaigneau (50)
Executive Vice President Finance and Administration, Water Division, Suez Lyonnaise des Eaux

J A Haynes (70)
Deputy Chairman
Former Chairman, Wellington Underwriting plc at Lloyd's of London

M A B Nègre (54)
Group Managing Director to 7 March 2001

R R Allan (66)
Non Executive Chairman, Perry Group plc

Sir F G T Holliday (65)
Chairman
Supervisory Board Member, Suez Lyonnaise des Eaux

Directors' interests are disclosed in note 5 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 third 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. 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 introduced HSA Healthplan, which is employee funded, with effect from 1 January 2000.

Employee Investment Schemes

During the financial year and for the fourth consecutive year, the company has operated an employee investment scheme.

The new plan called SPRING 2000 consisted of two elements, which gave employees a choice of two different types of investment. The first investment opportunity 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 1102 employees participated in SPRING 2000.

Pensions

Information about the pension schemes operated by the Group is contained in note 27 to the financial statements.

DIRECTORS' REPORT (continued)

Charitable and Political Contributions

During the year the company made charitable donations of £56,794 (December 1999: £29,706). The company made no donations to any political party during the year (December 1999: £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 2000. 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 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

M Parker
Company Secretary



29 March 2001

REPORT OF THE AUDITORS

To the shareholders of Northumbrian Water Limited:

We have audited the financial statements on pages 7 to 38, 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.

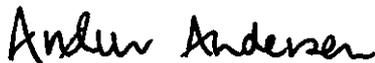
Basis of opinion

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 are consistently applied and are 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 2000 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

29 March 2001

GROUP PROFIT AND LOSS ACCOUNT
For the year ended 31 December 2000

	Note	<u>December 2000</u>	<u>December 1999</u>
		£'m	£'m
Turnover			
Existing Operations	2	337.4	379.5
Acquired Operations	2	78.1	-
		<u>415.5</u>	<u>379.5</u>
Operating costs	3(a)	(169.1)	(125.6)
Capital maintenance costs	3(b)	(63.4)	(54.4)
Exceptional operating costs	3(c)	(2.0)	(8.5)
Total operating expenses	3(d)	<u>(234.5)</u>	<u>(188.5)</u>
OPERATING PROFIT			
Existing Operations		153.8	191.0
Acquired Operations		27.2	-
TOTAL OPERATING PROFIT		<u>181.0</u>	<u>191.0</u>
Net interest payable	4	<u>(58.3)</u>	<u>(34.1)</u>
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION		<u>122.7</u>	<u>156.9</u>
Taxation	8	<u>(12.9)</u>	<u>(31.4)</u>
PROFIT FOR THE FINANCIAL YEAR		<u>109.8</u>	<u>125.5</u>
Dividends	9	<u>(77.0)</u>	<u>(64.4)</u>
PROFIT RETAINED FOR THE YEAR	24	<u><u>32.8</u></u>	<u><u>61.1</u></u>

All turnover and operating profit derive from continuing operations.
The movement on reserves is shown in note 24.

GROUP STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Total recognised gains in the financial year	109.8	125.5
Prior year adjustment	-	4.9
Total gains and losses recognised since last annual report and financial statements	<u>109.8</u>	<u>130.4</u>

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

GROUP BALANCE SHEET

At 31 December 2000

	Note	December 2000 £'m	December 1999 £'m
FIXED ASSETS			
Tangible assets	10	2,248.5	1,719.7
CURRENT ASSETS			
Stocks	12	2.2	1.9
Debtors: amounts falling due within one year	13	93.8	70.7
Debtors: amounts falling due after more than one year	13	-	11.7
Investments	14	0.2	75.0
Cash at bank and in hand		-	3.7
		96.2	163.0
CREDITORS			
Amounts falling due within one year	15	(326.3)	(196.9)
NET CURRENT LIABILITIES			
		(230.1)	(33.9)
TOTAL ASSETS LESS CURRENT LIABILITIES			
		2,018.4	1,685.8
CREDITORS: Amounts falling due after more than one year			
	16	(884.4)	(612.7)
PROVISIONS FOR LIABILITIES AND CHARGES			
	21	(14.7)	(17.8)
ACCRUALS AND DEFERRED INCOME			
	22	(115.9)	(84.7)
		(1,015.0)	(715.2)
NET ASSETS			
		1,003.4	970.6
CAPITAL AND RESERVES			
Called up share capital	23	122.7	122.7
Profit and loss account	24	880.7	847.9
EQUITY SHAREHOLDERS' FUNDS			
	25	1,003.4	970.6

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

Approved on behalf of the board on

Director

Director

29 March 2001

COMPANY BALANCE SHEET

At 31 December 2000

	Note	December 2000	December 1999
		£'m	£'m
FIXED ASSETS			
Tangible assets	10	2,248.5	1,719.7
Investments	11	89.4	47.2
		2,337.9	1,766.9
CURRENT ASSETS			
Stocks	12	2.2	1.9
Debtors: amounts falling due within one year	13	93.8	70.7
Debtors: amounts falling due after more than one year	13	-	11.7
Investments	14	0.2	75.0
Cash at bank and in hand		-	3.7
		96.2	163.0
CREDITORS			
Amounts falling due within one year	15	(326.3)	(196.9)
NET CURRENT LIABILITIES		(230.1)	(33.9)
TOTAL ASSETS LESS CURRENT LIABILITIES		2,107.8	1,733.0
CREDITORS: Amounts falling due after more than one year	16	(973.8)	(659.9)
PROVISIONS FOR LIABILITIES AND CHARGES	21	(14.7)	(17.8)
ACCRUALS AND DEFERRED INCOME	22	(115.9)	(84.7)
		(1,104.4)	(762.4)
NET ASSETS		1,003.4	970.6
CAPITAL AND RESERVES			
Called up share capital	23	122.7	122.7
Profit and loss account	24	880.7	847.9
EQUITY SHAREHOLDERS' FUNDS		1,003.4	970.6

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

Approved on behalf of the board on

Director

J. G. Holliday

Director

A. H. H. H.

29 March 2001

GROUP CASH FLOW STATEMENT
For the year ended 31 December 2000

	Note	December 2000	December 1999
		£'m	£'m
NET CASH INFLOW FROM CONTINUING OPERATING ACTIVITIES			
	a	230.2	250.3
Return on investments and servicing of finance			
Interest received		2.6	8.5
Interest paid		(50.3)	(37.0)
Interest element of finance lease rentals		(1.5)	(1.6)
Net cash outflow from returns on investments and servicing of finance		(49.2)	(30.1)
Taxation			
United Kingdom corporation tax paid		(28.4)	(33.5)
Net cash outflow from taxation		(28.4)	(33.5)
Capital expenditure and financial investment			
Purchase of tangible fixed assets		(248.2)	(212.2)
Sale of tangible fixed assets		1.0	1.4
Grants, contributions and connection charges		9.5	6.6
Purchase of business	31c	(0.7)	-
Net cash outflow from capital expenditure and financial investment		(238.4)	(204.2)
Equity dividends paid		(78.9)	(62.9)
Management of liquid resources			
Purchase of short term deposits		(110.5)	(813.4)
Sale of short term deposits		189.7	841.6
Net cash inflow from management of liquid resources		79.2	28.2
Financing			
New loans		94.6	75.0
New leases		-	11.5
Loan repayment receipts from other Group company		-	2.4
Loan repayments		(11.3)	(26.7)
Capital element of finance lease rental payments		(4.2)	(3.0)
Net cash inflow from financing		79.1	59.2
(DECREASE)/INCREASE IN CASH IN THE YEAR		(6.4)	7.0

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

NOTES TO THE CASH FLOW STATEMENT
For the year ended 31 December 2000

a RECONCILIATION OF OPERATING PROFIT TO CASH FLOWS

	Note	December 2000	December 1999
		£'m	£'m
Operating profit		181.0	191.0
Depreciation of tangible fixed assets	3(b)	63.7	55.7
Amortisation of capital grants	3(e)	(3.3)	(2.4)
Profit on sale of fixed assets	3(b)	(0.3)	(1.3)
Decrease in stock		1.4	0.9
Decrease/(Increase) in debtors		2.7	(2.3)
(Decrease)/Increase in creditors		(13.3)	3.1
(Decrease)/Increase in restructuring provision		(1.7)	5.6
Net cash inflow from operating activities		<u>230.2</u>	<u>250.3</u>

The operating cash flows are all from continuing operations.

b ANALYSIS AND RECONCILIATION OF NET DEBT

	1 January 2000	Cash Flow	Other non- cash changes	31 December 2000
	£'m	£'m	£'m	£'m
Cash at bank and in hand	3.7	0.2	(3.9)	-
Overdrafts	-	(6.6)	3.9	(2.7)
	<u>3.7</u>	<u>(6.4)</u>	<u>-</u>	<u>(2.7)</u>
Debt due after 1 year	(560.0)	-	(270.8)	(830.8)
Debt due within 1 year	(10.4)	(83.3)	(14.4)	(108.1)
Finance leases	(56.4)	4.2	(5.2)	(57.4)
	<u>(626.8)</u>	<u>(79.1)</u>	<u>(290.4)</u>	<u>(996.3)</u>
Current asset investments	75.0	(79.2)	4.2	-
Net debt	<u>(548.1)</u>	<u>(164.7)</u>	<u>(286.2)</u>	<u>(999.0)</u>

Reconciliation of cash flow movement to net debt:

	December 2000	December 1999
	£'m	£'m
(Decrease)/Increase in cash in the year	(6.4)	7.0
Cash inflow from increase in debt and lease financing	(79.1)	(59.2)
Cash inflow from reduction in liquid resources	(79.2)	(28.2)
Change in net debt resulting from cash flows	(164.7)	(80.4)
Finance costs incurred during the year	(0.2)	(0.2)
Finance lease interest capitalised	(2.1)	(0.8)
Finance lease non cash movement	(1.0)	-
Movement in loan acquired from debt reorganisation	-	2.4
Debt acquired from Essex and Suffolk Water plc	(106.9)	-
Debt issued to purchase the assets of Essex and Suffolk Water plc	(176.0)	-
Movement in net debt in year	(450.9)	(79.0)
Net debt at 1 January 2000	(548.1)	(469.1)
Net debt at 31 December 2000	<u>(999.0)</u>	<u>(548.1)</u>

NOTES TO THE FINANCIAL STATEMENTS
For the year ended 31 December 2000

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 principal accounting policies, which have been applied consistently throughout the current and preceding years 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) **Basis of consolidation**
The consolidated financial statements include the company and its subsidiary undertakings. The results of subsidiaries and operations acquired during the year are included from the date of their acquisition. Intra-group sales and profits are eliminated fully on consolidation.
- (c) **Turnover**
Turnover, which excludes Value Added Tax, represents the income receivable in the ordinary course of business for services provided within the United Kingdom.
- (d) **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 and on maintaining the operational capability of the network in accordance with defined standards of service, 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 – 80 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.

1. STATEMENT OF ACCOUNTING POLICIES (continued)

(e) **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.

(f) **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.

(g) **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.

(h) **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.

(i) **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.

(j) **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.

(k) **Research and development**

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

(l) **Investments**

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

1. STATEMENT OF ACCOUNTING POLICIES (continued)

(m) 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. TURNOVER

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

3. OPERATING COSTS, CAPITAL MAINTENANCE AND EXCEPTIONAL COSTS

(a) Operating costs comprise:

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Materials and consumables	11.1	9.6
Other external charges	26.5	16.2
Manpower costs (note 7)	52.3	41.1
Other operating charges	92.4	69.6
Own work capitalised	(13.2)	(10.9)
	<u>169.1</u>	<u>125.6</u>

(b) Capital maintenance costs comprise:

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Depreciation:		
Non-Infrastructure assets	29.9	30.0
Non-Infrastructure assets held under finance leases	7.7	4.9
Infrastructure assets	26.1	20.8
Profit on disposal of fixed assets	(0.3)	(1.3)
	<u>63.4</u>	<u>54.4</u>

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

(b) Capital maintenance costs (continued):

The useful economic lives of certain assets, principally operational structures and certain major package applications, have been extended, resulting in a reduction in the depreciation charge relating to non-infrastructure assets of £5.0m for the year ended 31 December 2000. This has offset the depreciation relating to the assets acquired from Essex and Suffolk Water plc on 1 April 2000.

(c) Exceptional operating costs comprise:

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Reorganisation/restructuring costs	<u>2.0</u>	<u>8.5</u>

The reorganisation/restructuring costs represent exceptional costs resulting from a new severance scheme which was introduced during 2000.

(d) Total operating expenses comprise:

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Existing Operations	183.6	188.5
Acquired Operations	<u>50.9</u>	<u>-</u>
	<u>234.5</u>	<u>188.5</u>

(e) Profit on ordinary activities before taxation

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Profit on ordinary activities before taxation is stated after crediting:		
Amortisation of capital grants (note 22)	<u>3.3</u>	<u>2.4</u>

And after charging:

Operating leases: Plant and machinery	0.6	0.8
Other assets	1.8	0.2
Costs of research and development	5.3	4.7
Directors' emoluments (note 5)	<u>0.9</u>	<u>0.5</u>

Auditors' remuneration for the audit amounted to £83,900 (December 1999: £47,750). There were no fees for non audit services (December 1999: £nil).

4. NET INTEREST

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Net interest payable comprises:		
Interest payable:		
Bank loans and overdrafts	55.0	38.9
Debenture stock interest	2.0	0.9
Financing charges payable under finance leases	3.5	2.8
	<u>60.5</u>	<u>42.6</u>
Total interest payable	60.5	42.6
Interest receivable	(2.2)	(8.5)
	<u>58.3</u>	<u>34.1</u>
Net interest payable	58.3	34.1

5. DIRECTORS' EMOLUMENTS AND INTERESTS

Directors' remuneration

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

	<u>December 2000</u>	<u>December 1999</u>
	£'000	£'000
Emoluments (including benefits in kind)	<u>876.1</u>	<u>476.8</u>

Highest paid director

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

	<u>December 2000</u>	<u>December 1999</u>
	£'000	£'000
Emoluments (including benefits in kind)	<u>194.3</u>	<u>169.7</u>

The accrued pension entitlement under the company's defined benefit scheme of the highest paid director at 31 December 2000 was £56,031 (31 December 1999: £49,029). In addition to the pension, there is a tax free lump sum at normal pension date of which the accrued entitlement at 31 December 2000 was £147,529 (31 December 1999: £131,970).

Three of the directors at 31 December 2000 were members of a defined benefit pension scheme where the company makes contributions towards the cost (1999: 4).

The directors who held office at 31 December 2000 had no interest in the shares of the company.

The directors who held office at 31 December 2000 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.

5. DIRECTORS' EMOLUMENTS AND INTERESTS (continued)

Name of Director	Description of Shares or debentures	31 December 2000	1 January 2000 or subsequent date of appointment
P Babin	Ordinary Shares of €10	603	522
J A Cuthbert	Ordinary Shares of €10	710	361
A J Harding	Ordinary Shares of €10	903	468
Sir F G T Holliday	Ordinary Shares of €10	400	400
C M Green	Ordinary Shares of €10	489	264
A Chaigneau	Ordinary Shares of €10	1058	720
M A B Nègre	Ordinary Shares of €10	1510	1510

The directors who held office on 31 December 2000 held the following options over ordinary shares of €10 each in Suez Lyonnaise des Eaux:

Name of Director	1 January 2000 or subsequent date of appointment	Granted during the year	31 December 2000	Exercise Price
P Babin	3500	-	3500	573 FF
	4000	-	4000	978 FF
	4500	-	4500	€151.11
	-	6500	6500	€182.07
J A Cuthbert	1200	-	1200	456 FF
	2200	-	2200	573 FF
	2300	-	2300	978 FF
	2500	-	2500	€151.11
	-	2600	2600	€182.07
A J Harding	2500	-	2500	573FF
	2600	-	2600	978FF
	2800	-	2800	€151.11
	-	2900	2900	€182.07
Sir F G T Holliday	3000	-	3000	573 FF
	3000	-	3000	978 FF
	3000	-	3000	€151.11
	-	3000	3000	€182.07
C M Green	700	-	700	573 FF
	1000	-	1000	978 FF
	700	-	700	€151.11
	-	900	900	€182.07
A Chaigneau	1000	-	1000	456 FF
	3500	-	3500	573 FF
	4000	-	4000	978 FF
	5000	-	5000	€151.11
	-	6000	6000	€182.07
M A B Nègre	2000	-	2000	573 FF
	3000	-	3000	978 FF
	3000	-	3000	€151.11

5. DIRECTORS' EMOLUMENTS AND INTERESTS (continued)

No options have 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.

All options with an exercise price of €182.07 were granted on 20 November 2000 and are exercisable between 28 November 2005 and 28 November 2010.

The highest and lowest prices of the Suez Lyonnaise des Eaux shares during the year were €199.7 and €139.0 respectively.

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

6. 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.

7. EMPLOYEE INFORMATION

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

	December 2000	December 1999
	£'m	£'m
Costs charged to the profit and loss account:		
Wages and salaries	33.8	26.7
Social security costs	3.0	2.3
Other pension costs	2.8	2.9
	<u>39.6</u>	<u>31.9</u>
Costs charged to capital schemes:		
Wages and salaries	11.2	7.7
Social security costs	0.9	0.6
Other pension costs	0.6	0.9
	<u>12.7</u>	<u>9.2</u>

7. EMPLOYEE INFORMATION (continued)

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

	<u>December 2000</u>	<u>December 1999</u>
	Number	Number
Average during the year	<u>2,158</u>	<u>1,585</u>
Total at 31 December	<u>2,133</u>	<u>1,469</u>

The average monthly number of employees incorporates staff numbers relating to Essex and Suffolk Water from 1 April 2000.

8. TAXATION

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Tax on profit on ordinary activities		
United Kingdom corporation tax at 30% (December 1999: 30.25%)		
- current year	1.5	17.7
- prior years	0.1	-
Payable in respect of group relief		
- current year	11.4	13.7
- prior years	<u>(0.1)</u>	<u>-</u>
Tax charge	<u>12.9</u>	<u>31.4</u>

- (a) The company has provisionally claimed tax losses from fellow subsidiaries in the current year of £38.1m (December 1999: £45.4m) for which payment will be made at the rate of 30%.
- (b) No deferred taxation has been provided in the financial statements since timing differences at 31 December 2000 are not expected to reverse in the foreseeable future (December 1999: £nil). The effect of not providing for deferred taxation has been a reduction in the tax charge for the year of £26.1m (December 1999: £17.6m). The full potential amount of deferred taxation calculated at 30% (December 1999: 30%) on all timing differences is as follows:

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Accelerated capital allowances	368.3	283.3
Other timing differences	<u>(21.0)</u>	<u>(19.1)</u>
	<u>347.3</u>	<u>264.2</u>

9. DIVIDENDS

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Equity:		
Interim paid of 29.99p (December 1999: 26.25p) per share on an aggregated basis	36.8	32.2
Final proposed of 32.76p (December 1999: 26.25p) per share on an aggregated basis	40.2	32.2
	<u>77.0</u>	<u>64.4</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.

Included within the dividend payable of £77.0m is an amount of £10.0m, relating to dividends payable from the profits generated by the operations acquired from Essex and Suffolk Water plc since 1 April 2000.

10. 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 2000	55.4	937.1	723.1	60.2	302.5	2,078.3
Additions	-	-	-	-	243.9	243.9
Schemes commissioned	3.1	102.8	81.1	2.2	(189.2)	-
Assets transferred from Essex and Suffolk Water plc (note 31)	17.8	135.3	181.9	5.0	10.1	350.1
Disposals	(2.1)	(14.8)	(0.1)	-	-	(17.0)
At 31 December 2000	<u>74.2</u>	<u>1,160.4</u>	<u>986.0</u>	<u>67.4</u>	<u>367.3</u>	<u>2,655.3</u>
Depreciation:						
At 1 January 2000	15.7	112.8	185.1	45.0	-	358.6
Provision for year	1.8	26.1	29.8	6.0	-	63.7
Disposals	(0.6)	(14.8)	(0.1)	-	-	(15.5)
At 31 December 2000	<u>16.9</u>	<u>124.1</u>	<u>214.8</u>	<u>51.0</u>	<u>-</u>	<u>406.8</u>
Net book value:						
At 31 December 2000	<u>57.3</u>	<u>1,036.3</u>	<u>771.2</u>	<u>16.4</u>	<u>367.3</u>	<u>2,248.5</u>
At 31 December 1999	<u>39.7</u>	<u>824.3</u>	<u>538.0</u>	<u>15.2</u>	<u>302.5</u>	<u>1,719.7</u>
Leased assets included above:						
Net book value						
At 31 December 2000	<u>17.8</u>	<u>2.2</u>	<u>28.2</u>	<u>6.4</u>	<u>-</u>	<u>54.6</u>
At 31 December 1999	<u>-</u>	<u>-</u>	<u>31.1</u>	<u>4.0</u>	<u>-</u>	<u>35.1</u>

11. FIXED ASSET INVESTMENTS – COMPANY

	December 2000	December 1999
	£'m	£'m
Investment in Newcastle and Gateshead Water plc	47.2	47.2
Investment in Suffolk Water plc	42.2	-
	<u>89.4</u>	<u>47.2</u>

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.

As a result of the acquisition of all the property and assets of Essex and Suffolk Water plc, the company now has a wholly-owned subsidiary undertaking in Suffolk Water plc, whose principal activity is the holding of a loan note due from its immediate parent company. This investment is valued at £42.2m which equates to the net assets of that company. 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.

12. STOCKS – GROUP AND COMPANY

	December 2000	December 1999
	£'m	£'m
Raw materials and consumables	2.2	1.9

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

13. DEBTORS – GROUP AND COMPANY

	December 2000	December 1999
	£'m	£'m
(a) Amounts falling due within one year:		
Trade debtors	56.3	34.7
Amounts owed by other group companies	6.8	3.6
Other debtors	5.3	4.0
Prepayments and accrued income	25.4	28.4
	<u>93.8</u>	<u>70.7</u>
(b) Amounts falling due after more than one year:		
Amounts owed by other group companies	-	11.7

Included in amounts owed by other group companies are loans of £nil (December 1999: £10.2m).

14. INVESTMENTS – GROUP AND COMPANY

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Short term deposits	-	75.0
Assets held for resale	0.2	-
	<u>0.2</u>	<u>75.0</u>

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

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Obligations under finance leases (note 19)	4.6	3.7
Bank overdraft	2.7	-
Loans (note 17)	13.5	10.1
Debenture Stock Interest	0.3	-
Trade creditors	3.2	1.8
Amounts owed to other group companies (note 20)	131.3	30.5
Taxation and social security	1.6	0.9
Corporation Tax	16.5	18.5
Other creditors	20.0	11.8
Receipts in Advance	32.7	35.9
Dividend payable	40.2	32.2
Accruals and deferred income	59.7	51.5
	<u>326.3</u>	<u>196.9</u>

Accruals and deferred income includes accruals related to capital projects of £30.3m (December 1999: £33.2m). Amounts owed to other group companies include amounts related to capital projects of £2.4m (December 1999: £2.2m).

Included in amounts owed to other group companies is £8.9m (December 1999: £9.7m) payable in respect of tax losses surrendered from fellow Group companies; and £nil (December 1999: £0.1m) payable in respect of advance corporation tax surrendered from Northumbrian Water Group plc. Also included in amounts owed to other group companies is £94.6m (December 1999: £0.3m) relating to loans repayable within one year (note 20).

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

	December 2000		December 1999	
	Group	Company	Group	Company
	£'m	£'m	£'m	£'m
Obligations under hire purchase contracts and finance leases (note 19)	52.8	52.8	52.7	52.7
Loans (note 17)	318.2	318.2	227.5	227.5
Debenture stocks (note 18)	22.3	22.3	8.7	8.7
Amounts owed to other group companies (note 20)	490.3	579.7	323.8	371.0
Other creditors	0.8	0.8	-	-
	<u>884.4</u>	<u>973.8</u>	<u>612.7</u>	<u>659.9</u>

At 31 December 2000 the group and company had entered into the following interest swap arrangements: £15.0m (December 1999: £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 £4.7m (December 1999: £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%, and £25.0m over a three year period commencing on 7 December 2000 under which the group and company is required to pay interest at 5.61% and will receive interest at a rate linked to LIBOR, and £25.0m over a five year period commencing 23 May 1997 under which the group and company is required to pay interest at a rate linked to LIBOR and will receive interest at 7.45%.

17. LOANS

	December 2000	December 1999
	£'m	£'m
Loans are repayable as follows:		
Within one year	13.5	10.1
Between one and two years	22.6	11.1
Between two and five years	84.0	65.7
After five years	211.6	150.7
	<u>331.7</u>	<u>237.6</u>

Loans repayable by instalments wholly repayable within 5 years amount to £7.2m (December 1999: £10.5m). Loans repayable by instalments not wholly repayable within 5 years amount to £219.5m (December 1999: £137.1m) and bear interest rates in the range of 7.2% to 11.1% of which £97.9m (December 1999: £61.4m) falls due in less than 5 years and £121.6m (December 1999: £75.7m) falls due after more than 5 years.

Loans repayable otherwise than by instalments which fall due in less than 5 years amount to £15.0m (December 1999: £nil) and bear interest at rates in the range of 5.9% and 7.95%.

Loans repayable otherwise than by instalments which fall due after more than 5 years amount to £90.0m (December 1999: £90.0m) and bear interest at rates in the range of 5.9% and 7.95%.

17. LOANS (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 Treasury department 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 liquidity risk, interest rate 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 Limited 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.

17. LOANS (continued)

Interest rate risk profile of financial assets and financial liabilities

The interest rates and currency profile of the net borrowings of the Group at 31 December 2000 were:

	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		Weighted average period for which rate is fixed
	£'m	£'m	£'m	%	Years	Years	£'m
Sterling borrowings:							
External loans	(331.7)	(92.5)	(239.2)	7.58	10.2	10.2	-
Debentures	(22.3)	-	(22.3)	7.76	12.1	12.1	-
Internal loans	(584.9)	(390.1)	(194.8)	6.99	22.1	22.1	-
Finance leases	(57.4)	(50.4)	(7.0)	10.47	4.0	4.0	-
Bank Overdraft	(2.7)	(2.7)	-	-	-	-	-
Total Borrowings	(999.0)	(535.7)	(463.3)	7.54	14.8	14.8	-
Short Term Investments	-	-	-	-	-	-	-
Net borrowings	(999.0)	(535.7)	(463.3)				-

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

	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		Weighted average period for which rate is fixed
	£'m	£'m	£'m	%	Years	Years	£'m
Sterling borrowings:							
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	-	-	-	-	-	-	-
Total Borrowings	(626.8)	(246.6)	(380.2)	7.48	16.0	16.0	-
Cash	3.7	3.7	-	-	-	-	-
Short Term Investments	75.0	-	75.0	5.88	0.1	0.1	-
Net borrowings	(548.1)	(242.9)	(305.2)				-

17. LOANS (continued)

Included within the external sterling loans of the group above are loans amounting to £122m 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 2000, the group had no currency exposures.

Borrowing facilities

The group had no undrawn committed borrowing facilities as at 31 December 2000 but had access to undrawn committed borrowing facilities available to NWG which, at 31 December 2000, amounted to £150m.

The facilities available to NWG at 31 December 2000, in respect of which all conditions precedent have been met, were as follows:

	£'m
Expiring in one year or less	75.0
Expiring in more than one year but not more than three years	75.0
	<u>150.0</u>

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 as at 31 December 2000:

	Book value	Fair value
	£'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	(115.4)	(115.1)
Long-term borrowings	(883.6)	(909.6)
Derivative financial instruments held to manage the interest rate and currency profile:		
Interest rate swaps	0.0	2.3
As at 31 December 2000	<u>(999.0)</u>	<u>(1,022.4)</u>

17. LOANS (continued)

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

	Book value	Fair value
	£'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>

The fair values of the interest rate swaps, and sterling denominated long-term fixed rate debt with a book value of £217.0m, 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

	Gains	Losses	Total net Gains/Losses
	£'m	£'m	£'m
Unrecognised gains and losses on hedges at 1 January 2000	2.2	-	2.2
Gains and losses arising in previous years that were recognised in 2000	(0.8)	-	(0.8)
Gains and losses arising before 1 January 2000 that were not recognised in 2000	1.4	-	1.4
Gains and losses arising in 2000 that were not recognised in 2000	0.9	-	0.9
Unrecognised gains and losses on hedges at 31 December 2000	<u>2.3</u>	<u>-</u>	<u>2.3</u>
Of which:			
Gains and losses expected to be recognised in 2001	0.8	-	0.8
Gains and losses expected to be recognised in 2002 or later	1.5	-	1.5
	<u>2.3</u>	<u>-</u>	<u>2.3</u>

17. LOANS (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.

18. DEBENTURE STOCKS

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Debenture stocks are repayable as follows:		
Between one and two years:		
£1, 11.75% Redeemable 2002/04	<u>8.0</u>	<u>-</u>
Between two and five years:		
£1, 12.0% Redeemable 2004	5.0	5.0
£1, 12.0% Redeemable 2005	2.0	2.0
£1, 11.2% Redeemable 2005/09	3.5	-
In five years or more:		
£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
£1, 3.5% Irredeemable	0.2	-
£1, 4.0% Irredeemable	0.8	-
£1, 5.0% Irredeemable	1.1	-
	<u>22.3</u>	<u>8.7</u>

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

19. OBLIGATIONS UNDER FINANCE LEASES – GROUP AND COMPANY

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

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Amounts due:		
Within one year	4.6	3.7
Between one and two years	3.9	4.6
Between two and five years	7.8	7.2
After five years	78.2	80.6
	<u>94.5</u>	<u>96.1</u>
Less:		
Finance charge allocated to future periods	(37.1)	(39.7)
	<u>57.4</u>	<u>56.4</u>
Disclosed as due:		
Within one year (note 15)	4.6	3.7
After more than one year (note 16)	52.8	52.7
	<u>57.4</u>	<u>56.4</u>

20. AMOUNTS DUE TO OTHER GROUP COMPANIES

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

	<u>December 2000</u>		<u>December 1999</u>	
	Group	Company	Group	Company
	£'m	£'m	£'m	£'m
Within one year	94.6	94.6	0.3	0.3
Between one and two years	-	-	0.7	0.7
Between two and five years	-	-	2.5	2.5
After five years	490.3	579.7	320.6	367.8
	<u>584.9</u>	<u>674.3</u>	<u>324.1</u>	<u>371.3</u>

£47.2m is owed to a subsidiary undertaking of the group, Newcastle & Gateshead Water plc, in the form of an unsecured loan note repayable, at par, otherwise than by instalments 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.

£42.2m is owed to a subsidiary undertaking of the group, Suffolk Water plc, in the form of an unsecured loan note repayable, at par, otherwise than by instalments and is subject to interest at an agreed rate of 0%. The company may exercise an option to repay the loan note at anytime, 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.

20. AMOUNTS DUE TO OTHER GROUP COMPANIES (continued)

£119.5m is owed to a fellow subsidiary, North East Water plc, 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.

£176.0m is owed to a fellow subsidiary, Essex and Suffolk Water plc, 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.

£194.8m 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 the issue proceeds by way of an inter-company loan of £194.2m. Finance costs allocated during the year amounted to £0.2m (December 1999: £0.2m).

£94.6m is owed to the immediate parent company, Northumbrian Water Group plc. Northumbrian Water Group plc has issued commercial paper at rates linked to LIBOR. The Commercial Paper proceeds are then on-lent to the company at the issued rate.

21. PROVISIONS FOR LIABILITIES AND CHARGES – GROUP AND COMPANY

	Reorganisation and Restructuring Provision	Pension Provision	Total
	£'m	£'m	£'m
At 1 January 2000	8.2	9.6	17.8
Transferred from Essex and Suffolk Water plc	0.1	-	0.1
Transferred from profit and loss account	2.7	(0.7)	2.0
Utilised during the year	(5.2)	-	(5.2)
At 31 December 2000	5.8	8.9	14.7

The reorganisation 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 1998 and 1999 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.

The pension provision represents amounts provided in respect of pension contributions for staff leaving the business as part of voluntary severance schemes prior to 1998. The company's actuary has assessed that the company is not required to make cash payments to fund these contributions. Accordingly the provision is being released over the average remaining service life of current employees.

22. ACCRUALS AND DEFERRED INCOME – GROUP AND COMPANY

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Capital grants and contributions:		
At 1 January	84.7	80.6
Transferred from Essex and Suffolk Water plc	25.0	-
Additions	9.5	6.5
Amortised during the year	<u>(3.3)</u>	<u>(2.4)</u>
At 31 December	<u>115.9</u>	<u>84.7</u>

23. CALLED UP SHARE CAPITAL – GROUP AND COMPANY

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Authorised:		
122,650,000 Ordinary Shares of £1 each (December 1999: 122,650,000)	<u>122.7</u>	<u>122.7</u>
	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Allotted, called-up and fully paid:		
122,650,000 Ordinary Shares of £1 each (December 1999: 122,650,000)	<u>122.7</u>	<u>122.7</u>

24. PROFIT AND LOSS ACCOUNT – GROUP AND COMPANY

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
At 1 January	847.9	781.9
Prior year adjustment	-	4.9
At 1 January as restated	847.9	786.8
Profit retained for the year	<u>32.8</u>	<u>61.1</u>
At 31 December	<u>880.7</u>	<u>847.9</u>

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. The profit for the financial year of £109.8m (December 1999: £125.5m) relates to the operations of the company.

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

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Profit for the financial year	109.8	125.5
Dividends	(77.0)	(64.4)
	<hr/>	<hr/>
Net additions to equity shareholders' funds	32.8	61.1
Opening equity shareholders' funds	970.6	904.6
Prior year adjustment	-	4.9
	<hr/>	<hr/>
Closing equity shareholders' funds	<u>1,003.4</u>	<u>970.6</u>

26. COMMITMENTS AND CONTINGENT LIABILITIES – GROUP AND COMPANY

(a) Capital expenditure

	<u>December 2000</u>	<u>December 1999</u>
	£'m	£'m
Expenditure contracted for	36.8	105.6
	<hr/>	<hr/>

(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 2000</u>	<u>December 1999</u>
	£'m	£'m
Land and buildings:		
Leases which expire:		
Within one year	0.3	-
In five years or more	0.4	0.3
	<hr/>	<hr/>
	0.7	0.3
	<hr/>	<hr/>
Other:		
Leases which expire:		
Within one year	0.2	0.3
Between two and five years	0.8	0.5
	<hr/>	<hr/>
	1.0	0.8
	<hr/>	<hr/>

27. 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.

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 60 employees. The last actuarial valuation was carried out at 31 March 1998.

The Northumbrian Water Group Personal Pension Plan provides defined contribution benefits to 670 employees.

28. RELATED PARTY DISCLOSURES

The company is a wholly owned subsidiary of Northumbrian Water Group plc which produces publicly available financial statements which include 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 £25.4m (31 December 1999: £16.8m) and sales of £1.0m (31 December 1999: £1.1m). As at 31 December 2000, the amount due to these companies was £3.2m (31 December 1999: £2.1m) and due from these companies was £0.6m (31 December 1999: £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

29. 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.

30. BILLING ON BEHALF OF WATER AND SEWERAGE COMPANIES

The Group bills and collects charges in respect of sewerage services in some of its area of supply on behalf of Anglian Water Services Limited and Thames Water Utilities Limited who are responsible for those services.

The Group receives commission income for those services, which is included in other operating income. Payments on account from customers due to Anglian Water Services and Thames Water Utilities Limited are included in creditors falling due within one year.

31. ACQUISITION

On 1 April 2000 the company acquired the trade and assets of Essex and Suffolk Water plc for a total consideration of £176.0m. The consideration was satisfied by the issue of a loan note for the full amount.

a) Profit and Loss Account

The summarized profit and loss account for Essex and Suffolk Water plc for the period from 1 January 2000, the beginning of the company's financial year, to the date of acquisition, is as follows:

	<u>3 months ended</u> <u>31 March 2000</u>
	£'m
Turnover	29.1
Operating profit	<u>12.7</u>
Profit on ordinary activities before taxation	10.2
Tax on ordinary activities	<u>(1.6)</u>
Profit on ordinary activities after taxation	<u>8.6</u>

The profit on ordinary activities after taxation for Essex and Suffolk Water plc for the year ended 31 December 1999 was £27.6m.

There were no other recognised gains and losses for the three month period to 31 March 2000 other than profit for the year. For the year ended 31 December 1999, there was a recognised gain of £0.7 m arising from a prior year adjustment as a result of the application of Financial Reporting Standards 12 and 15.

31. ACQUISITION (continued)

b) Assets and Liabilities

The assets and liabilities of Essex and Suffolk Water plc which were acquired on 1 April 2000, are set out below:

	Book Value and Fair Value
	£'m
FIXED ASSETS	350.1
Investments	42.2
	<u>392.3</u>
CURRENT ASSETS	
Stock	1.7
Debtors: amounts falling due within one year	32.3
Debtors: amounts falling due in more than one year	9.7
Investments	4.0
Cash at bank and in hand	-
	<u>47.7</u>
CREDITORS: amounts falling due within one year	(59.9)
NET CURRENT LIABILITIES	<u>(12.2)</u>
TOTAL ASSETS LESS CURRENT LIABILITIES	<u>380.1</u>
CREDITORS: amounts falling due in more than one year	(176.5)
PROVISIONS FOR LIABILITIES AND CHARGES	(2.5)
ACCRUALS AND DEFERRED INCOME	(25.1)
	<u>(204.1)</u>
NET ASSETS	<u>176.0</u>
Satisfied by:	
Loan note	<u>176.0</u>

c) Analysis of the net outflow of cash in respect of the acquisition of the trade and assets of Essex and Suffolk Water plc.

	£'m
Cash consideration	-
Bank overdrafts acquired	(0.7)
	<u>(0.7)</u>
Net outflow of cash	<u>(0.7)</u>

31. ACQUISITION (continued)

- d) The cash flows in respect of Essex and Suffolk Water division during the nine month period commencing 1 April 2000 are as follows:

	<u>£'m</u>
OPERATING CASH INFLOW	<u>38.8</u>
Outflow from returns on investments and servicing of finance	(7.4)
Taxation Paid	(6.4)
Outflow from capital expenditure and financial investment	(18.1)
Equity Dividends Paid	(13.2)
Inflow from management of liquid resources	4.2
Outflow from financing	<u>(3.8)</u>
DECREASE IN CASH IN THE YEAR	<u>(5.9)</u>